

CHINA MOBILE LTD /ADR/  
Form 20-F  
June 12, 2007  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, DC 20549

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**FORM 20-F**

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.. **REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR 12(g) OF THE SECURITIES EXCHANGE ACT OF 1934**

OR

x **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended December 31, 2006

OR

.. **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

OR

.. **SHELL COMPANY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

Date of event requiring this shell company report

Commission file number: 1-14696

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# China Mobile Limited

(Exact Name of Registrant as Specified in Its Charter)

N/A

(Translation of Registrant's Name into English)

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Hong Kong, China

(Jurisdiction of Incorporation or Organization)

60th Floor, The Center

99 Queen's Road Central

Hong Kong, China

(Address of Principal Executive Offices)

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Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class  
Ordinary shares, par value HK\$0.10 per share

Name of Each Exchange on Which Registered  
The New York Stock Exchange, Inc.\*

\* Not for trading, but only in connection with the listing on the New York Stock Exchange, Inc. of American depositary shares representing the ordinary shares.

Securities registered or to be registered pursuant to Section 12(g) of the Act:

None

(Title of Class)

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act:

None

(Title of Class)

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Indicate the number of outstanding shares of each of the issuer's classes of capital or common stock as of the close of the period covered by the annual report.

As of December 31, 2006, 19,967,815,140 ordinary shares, par value HK\$0.10 per share, were issued and outstanding.

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ☐ No ☒

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If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934. Yes ☐ No ☒

Note Checking the box above will not relieve any registrant required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 from their obligations under those Sections.

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☒ No ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer ☒ Accelerated filer ☐ Non-accelerated filer ☐

Indicate by check mark which financial statement item the registrant has elected to follow. Item 17 ☐ Item 18 ☒

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☒

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### **Forward-Looking Statements**

This annual report on Form 20-F contains certain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. These forward-looking statements are, by their nature, subject to significant risks and uncertainties. These forward-looking statements include, without limitation, statements relating to:

our business strategies;

our operations and business prospects;

our network expansion plans and related capital expenditure plans, including, among others, those relating to third generation mobile telecommunications technology, or 3G, network constructions;

the planned development of new mobile technologies and other technologies and related applications;

the expected impact of tariff changes on our business, financial condition and results of operations;

the expected impact of new services on our business, financial condition and results of operations; and

future developments in the telecommunications industry in Mainland China.

The words anticipate, believe, could, estimate, expect, intend, may, seek, will and similar expressions, as they relate to us, are intended to identify certain of these forward-looking statements. We do not intend to update these forward-looking statements.

These forward-looking statements are subject to risks, uncertainties and assumptions, some of which are beyond our control. In addition, these forward-looking statements reflect our current views with respect to future events and are not a guarantee of future performance. Actual results may differ materially from information contained in the forward-looking statements as a result of a number of factors, including, without limitation, the risk factors set forth in Item 3. Key Information Risk Factors and the following:

any changes in the regulatory policies of the Ministry of Information Industry or other relevant government authorities, which could affect, among other things, the granting of requisite government approvals, licenses and permits, interconnection and transmission line arrangements, tariff policies, capital investment priorities, the provision of telephone services in rural areas of the People's Republic of China, or the PRC, and spectrum and numbering resources allocation;

the effect of competition on the demand for and price of our services;

changes in mobile telephony and related technologies, which could affect the viability and competitiveness of our mobile telecommunications networks; and

changes in political, economic, legal and social conditions in Mainland China, including, without limitation, the PRC government's policies with respect to new entrants in the telecommunications industry, the entry of foreign companies into Mainland China's

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telecommunications market and Mainland China's continued economic growth.

In addition, our future network expansion and other capital expenditure and development plans are dependent on numerous factors, including, among others:

our ability to obtain adequate financing on acceptable terms;

the adequacy of currently available spectrum or the availability of additional spectrum;

the availability of transmission lines and equipment, and the availability of the requisite number of sites for locating network equipment, on reasonable commercial terms;

our ability to develop or obtain new technology and related applications; and

the availability of qualified management and technical personnel.

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### **Special Note on Our Financial Information and**

#### **Certain Statistical Information Presented in This Annual Report**

As required under generally accepted accounting principles in Hong Kong, or Hong Kong GAAP, we adopted the purchase accounting method to account for our acquisitions of various regional mobile telecommunications companies and other telecommunications assets, as described in Item 4. Information on the Company The History and Development of the Company . Accordingly, our consolidated financial statements and, except as otherwise noted, all other Hong Kong GAAP financial information presented in this annual report on Form 20-F, include the results of these companies only from the respective dates of acquisition.

For acquisitions before January 1, 2001, positive goodwill arising from acquisitions was eliminated against reserves, and negative goodwill arising from acquisitions was credited to a capital reserve. For acquisitions on or after January 1, 2001, positive goodwill arising from acquisitions is amortized to the consolidated statements of income on a straight-line basis over its estimated useful life, which shall not exceed 20 years. Positive goodwill is stated in the consolidated balance sheets at cost less any accumulated amortization and any impairment loss. Effective January 1, 2005, in order to comply with Hong Kong Financial Reporting Standard 3, Business Combinations , or HKFRS 3, and Hong Kong Accounting Standard 36, Impairment of Assets , or HKAS 36, issued by the Hong Kong Institute of Certified Public Accountants, or HKICPA, we adopted a new accounting policy for goodwill. The new policy has been applied prospectively in accordance with the transitional provisions as set out in HKFRS 3 to the effect that we no longer amortize goodwill, but test goodwill at least annually for impairment. In addition, the cumulative amount of amortization as of January 1, 2005 has been offset against the cost of the goodwill and comparative amounts have not been restated.

Under generally accepted accounting principles in the United States, or U.S. GAAP, as a result of our being under common control with each of these companies prior to the acquisitions, each of the acquisitions was considered to be a combination of entities under common control . Under U.S. GAAP, combinations of entities under common control are accounted for in a manner similar to a pooling-of-interests. Consequently, the assets and liabilities are transferred at their historical amounts and the financial statements of previously separate companies are included in our consolidated financial statements for all periods presented. See Item 5. Operating and Financial Review and Prospects .

Prior to 2005, minority interests were presented in the consolidated balance sheets separately from liabilities and as a deduction from net assets, and minority interests in our results for the year were also separately presented in the consolidated statements of income as a deduction before arriving at the profit attributable to equity shareholders. Effective January 1, 2005, in order to comply with HKAS 1, Presentation of Financial Statements , and HKAS 27, Consolidated and Separate Financial Statements , issued by the HKICPA, we adopted a new accounting policy for minority interests. In particular, minority interests are presented in the consolidated balance sheets and consolidated statements of equity separately from capital and reserves attributable to equity shareholders, and minority interests in our results are presented on the face of the consolidated statements of income as an allocation of the total profit or loss for the year between minority interests and equity shareholders. These changes in presentation have been applied retrospectively and comparative amounts have been restated.

Prior to 2005, land use rights and buildings held for our own use were stated at cost less accumulated depreciation and impairment losses. Depreciation was calculated to write off the cost of these assets on a straight-line basis over their estimated useful lives to residual value. Effective January 1, 2005, in order to comply with HKAS 17, Leases , issued by the HKICPA, we adopted a new accounting policy for land use rights and buildings held for our own use by reclassifying land use rights and buildings held for our own use as being held under an operating lease. The corresponding amortization charges relating to land use rights and buildings held for our own use were reclassified from depreciation to other operating expenses. The new accounting policy has been adopted retrospectively and comparative amounts have been restated. There is no impact on our net assets as of the year end and on our profit attributable to equity shareholders for the periods presented.

Prior to 2005, no employee benefit cost or obligation was recognized when we granted employees (which term includes directors) share options on our shares. When the share options were exercised, capital and reserves attributable to equity shareholders were increased by the amount of the proceeds received. Effective January 1, 2005, in order to comply with HKFRS 2, Share-Based Payments , or HKFRS 2, issued by the HKICPA, we adopted a new accounting policy for the employee share option scheme where the fair value (measured at grant date using the binomial lattice model) of share options granted to employees is recognized as an employee cost with a corresponding increase in capital and reserves attributable to equity shareholders. The new accounting policy has been applied retrospectively and comparative amounts have been restated in accordance with HKFRS 2, except that we have adopted the transitional provisions set out in paragraph 53 of HKFRS 2, under which the new recognition and measurement policies have not been applied to: (i) all share options granted to employees on or before November 7, 2002; and (ii) all share options granted to employees after November 7, 2002 but which had vested before January 1, 2005.





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Under U.S. GAAP, and prior to January 1, 2006, we followed Accounting Principles Board Opinion No. 25, *Accounting for Stock Issued to Employees*, and determined the compensation expense of share options granted based on the excess, if any, of the quoted market price of the shares on the date of grant over the exercise price of the share options. The excess amount was charged to the consolidated statements of income over the vesting period of the share options. As a result, any expenses recognized based on the fair value of share options under Hong Kong GAAP were reversed under U.S. GAAP. Effective January 1, 2006, in order to comply with Statement of Financial Accounting Standards No. 123 (revised 2004), *Share-Based Payment*, issued by the U.S. Financial Accounting Standards Board, we adopted a new accounting policy in respect of compensation expenses of share options and recognized compensation expense for all unvested share-based payment at fair value. We adopted the modified-prospective transition method under which, effective from January 1, 2006, the compensation expense is recognized at fair value for: (i) share options granted after January 1, 2006; and (ii) all share options granted prior to January 1, 2006 that remain unvested at that date. As a result, the U.S. GAAP difference as shown in the net profit reconciliation for the year ended December 31, 2006 represented additional compensation expense recognized under U.S. GAAP using the fair value approach for unvested share options granted to employees before November 7, 2002.

Prior to 2005, convertible notes and bonds were stated in the consolidated balance sheets at face value, less unamortized discount arising upon issuance. The discount was amortized on a straight-line basis over the period from the date of issuance to the date of maturity. Effective January 1, 2005, in order to comply with HKAS 32, *Financial Instruments: Disclosure and Presentation*, and HKAS 39, *Financial Instruments: Recognition and Measurement*, or HKAS 39, issued by the HKICPA, we adopted new accounting policies for financial instruments. Under our new accounting policies, the liability component of the convertible notes and bonds are recognized initially at fair value less attributable transaction costs and the equity component (representing the excess proceeds over the amount initially recognized as the liability component) is recognized in the capital reserve until the notes are converted or redeemed. The liability component of convertible notes and bonds are subsequently carried at amortized cost and the corresponding interest expenses recognized in the consolidated statements of income are calculated using the effective interest method. The new accounting policies have been adopted by way of an opening balance adjustment to retained earnings as of January 1, 2005. Comparative amounts have not been restated as this is prohibited by the transitional arrangements in HKAS 39.

Prior to 2003, deferred tax liabilities were provided using the liability method in respect of the taxation effect arising from all material timing differences between the accounting and tax treatment of income and expenditure, which were expected with reasonable probability to crystallize in the foreseeable future. Deferred tax assets were not recognized unless their realization was assured beyond reasonable doubt. With effect from January 1, 2003, in order to comply with Statement of Standard Accounting Practice 12 (revised), *Income Taxes* (SSAP 12 (revised)), issued by the HKICPA, we adopted a new accounting policy for deferred tax. Under our current accounting policy, deferred tax liabilities are provided in full on taxable temporary differences, while deferred tax assets are recognized to the extent that it is probable that future taxable profits will be available against which the deductible temporary differences can be utilized. As a result, goodwill, deferred tax assets, deferred tax liabilities and reserves in the consolidated balance sheets have been restated. In addition, deferred tax assets and deferred tax liabilities have been reclassified into non-current assets and liabilities, respectively. Income tax in the consolidated statements of income has also been revised.

The statistical information set forth in this annual report on Form 20-F relating to Mainland China is taken or derived from various publicly available government publications that have not been prepared or independently verified by us. This statistical information may not be consistent with other statistical information from other sources within or outside Mainland China.

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### **PART I**

#### **Item 1. Identity of Directors, Senior Management and Advisers.**

Not applicable.

#### **Item 2. Offer Statistics and Expected Timetable.**

Not applicable.

#### **Item 3. Key Information.**

##### **Selected Financial Data**

The following tables present selected historical financial data of our company as of and for each of the years in the five-year period ended December 31, 2006. Except for amounts presented in U.S. dollars, the selected historical income statement data for the years ended December 31, 2004, 2005 and 2006 and the selected historical balance sheet data as of December 31, 2005 and 2006 set forth below are derived from, should be read in conjunction with, and are qualified in their entirety by reference to, our audited consolidated financial statements, including the related notes, included elsewhere in this annual report on Form 20-F. The selected historical Hong Kong GAAP income statement data for the years ended December 31, 2002 and 2003 and the selected historical Hong Kong GAAP balance sheet data as of December 31, 2002, 2003 and 2004 are derived from our audited financial statements that are not included in this annual report on Form 20-F. In this annual report on Form 20-F, we have translated certain Renminbi and Hong Kong dollar amounts into U.S. dollars at the rate of RMB7.8041 = US\$1.00 and HK\$7.7771 = US\$1.00, the noon buying rates for these currencies in New York City for cable transfers as certified for customs purposes by the Federal Reserve Bank of New York on December 29, 2006. We translate these amounts solely for your convenience, and these translations should not be construed as representations that, on such or any other date, the Renminbi or Hong Kong dollar amounts could actually be converted into U.S. dollars at such rates or at all.

Our consolidated financial statements are prepared and presented in accordance with Hong Kong GAAP. As required under Hong Kong GAAP, we adopted the purchase accounting method to account for our acquisitions of the various regional mobile telecommunications companies and other telecommunications assets, as described in Item 4. Information on the Company The History and Development of the Company . Accordingly, our consolidated financial statements and, except as otherwise noted, all other Hong Kong GAAP financial information presented in this annual report on Form 20-F, include the results of the various regional mobile telecommunications companies acquired from China Mobile Hong Kong (BVI) Limited, our immediate holding company, only from the respective dates of acquisition. In contrast, under U.S. GAAP, our acquisitions of these companies are each considered a combination of entities under common control which would be accounted for in a manner similar to a pooling-of-interests. Consequently, the assets and liabilities are transferred at their historical amounts and our consolidated financial statements are adjusted retrospectively to include the financial statements of these previously separate companies for all periods presented. For information regarding significant differences between Hong Kong GAAP and U.S. GAAP as they relate to us, and the effects of such differences on profit attributable to equity shareholders for the years ended December 31, 2004, 2005 and 2006 and shareholders equity as of December 31, 2005 and 2006, see note 40 to our consolidated financial statements. In addition, our condensed consolidated financial statements prepared and presented in accordance with U.S. GAAP for the relevant periods are set forth in note 40 to our consolidated financial statements.

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|   | As of or for the year ended December 31,                       |            |            |            |            |            |
|---|--|------------|------------|------------|------------|------------|
|   | 2002   | 2003       | 2004       | 2005       | 2006       | 2006       |
|   | RMB  | RMB        | RMB        | RMB        | RMB        | US\$       |
|   | (in millions, except share, per share and per ADS information) |            |            |            |            |            |
| Income Statement Data:                                  |  |            |            |            |            |            |
| Hong Kong GAAP  |  |            |            |            |            |            |
| Operating revenue                                       | 128,561  | 158,604    | 192,381    | 243,041    | 295,358    | 37,846     |
| Operating expenses                                      | 79,765   | 105,401    | 132,902    | 169,355    | 203,433    | 26,067     |
| Profit from operations                                  | 48,796   | 53,203     | 59,479     | 73,686     | 91,925     | 11,779     |
| Profit before tax                                       | 48,978   | 52,959     | 60,951     | 78,264     | 96,908     | 12,417     |
| Income tax  | 16,375   | 17,412     | 19,180     | 24,675     | 30,794     | 3,946      |
| Profit for the year attributable to equity shareholders | 32,601   | 35,556     | 41,749     | 53,549     | 66,026     | 8,460      |
| Basic net income per share <sup>(1)</sup>               | 1.70   | 1.81       | 2.12       | 2.71       | 3.32       | 0.43       |
| Diluted net income per share <sup>(1)</sup>             | 1.70   | 1.81       | 2.12       | 2.70       | 3.29       | 0.42       |
| Basic net income per ADS <sup>(1)</sup>                 | 8.51   | 9.04       | 10.61      | 13.57      | 16.60      | 2.13       |
| Diluted net income per ADS <sup>(1)</sup>               | 8.50   | 9.03       | 10.59      | 13.49      | 16.44      | 2.11       |
| Shares utilized in basic calculation (in thousands)     | 19,151,322   | 19,671,654 | 19,673,185 | 19,738,229 | 19,892,968 | 19,892,968 |
| Shares utilized in diluted calculation (in thousands)   | 19,243,050   | 19,762,812 | 19,774,093 | 19,892,163 | 20,078,549 | 20,078,549 |
| U.S. GAAP <sup>(2)</sup>                                |  |            |            |            |            |            |
| Operating revenue                                       | 167,640  | 186,060    | 210,637    | 249,576    | 303,636    | 38,907     |
| Operating expenses                                      | 108,622  | 126,714    | 146,033    | 171,855    | 210,138    | 26,926     |
| Profit from operations                                  | 59,018   | 59,346     | 64,604     | 77,721     | 93,498     | 11,981     |
| Profit before tax                                       | 58,404   | 58,520     | 64,847     | 78,489     | 94,877     | 12,157     |
| Income tax  | 18,986   | 19,009     | 19,764     | 23,945     | 29,715     | 3,808      |
| Net income  | 39,416   | 39,520     | 45,061     | 54,504     | 65,074     | 8,338      |
| Basic net income per share <sup>(1)</sup>               | 2.01   | 2.01       | 2.29       | 2.76       | 3.27       | 0.42       |
| Diluted net income per share <sup>(1)</sup>             | 2.01   | 2.01       | 2.29       | 2.75       | 3.24       | 0.42       |
| Basic net income per ADS <sup>(1)</sup>                 | 10.07  | 10.05      | 11.45      | 13.81      | 16.36      | 2.10       |
| Diluted net income per ADS <sup>(1)</sup>               | 10.06  | 10.03      | 11.43      | 13.73      | 16.20      | 2.08       |
| Share utilized in basic calculation (in thousands)      | 19,561,679   | 19,671,654 | 19,673,185 | 19,738,229 | 19,892,968 | 19,892,968 |
| Share utilized in diluted calculation (in thousands)    | 19,653,406   | 19,762,812 | 19,774,093 | 19,892,163 | 20,078,549 | 20,078,549 |

**Table of Contents****Balance Sheet Data:****Hong Kong GAAP**

## Current assets

|                                      |         |         |         |         |         |        |
|--------------------------------------|---------|---------|---------|---------|---------|--------|
| Cash and cash equivalents            | 32,575  | 39,129  | 45,149  | 64,461  | 71,167  | 9,119  |
| Deposits with banks                  | 11,069  | 17,227  | 20,264  | 41,925  | 82,294  | 10,545 |
| Accounts receivable                  | 6,066   | 6,116   | 6,553   | 6,603   | 7,153   | 917    |
| Property, plant and equipment        | 161,355 | 167,177 | 212,459 | 216,505 | 218,274 | 27,969 |
| Total assets                         | 286,021 | 307,303 | 368,752 | 421,027 | 494,676 | 63,387 |
| Total short-term debt <sup>(3)</sup> | 8,200   | 8,174   | 2,523   | 68      | 68      | 9      |
| Total long-term debt <sup>(4)</sup>  | 12,676  | 672     |         |         |         |        |
| Fixed rate notes <sup>(5)</sup>      | 4,961   | 4,984   |         |         |         |        |
| Convertible notes <sup>(6)</sup>     | 5,711   | 5,735   | 5,725   |         |         |        |
| Bonds                                | 13,000  | 13,000  | 13,000  | 12,912  | 12,937  | 1,658  |
| Deferred payable <sup>(7)</sup>      | 15,176  | 9,976   | 23,633  | 23,633  | 23,633  | 3,028  |
| Total liabilities                    | 112,565 | 108,318 | 135,348 | 147,920 | 175,303 | 22,463 |
| Share capital                        | 2,099   | 2,099   | 2,102   | 2,116   | 2,130   | 273    |
| Shareholders' equity                 | 173,265 | 198,803 | 233,161 | 272,824 | 319,002 | 40,876 |

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|                                     | As of or for the year ended December 31,                       |         |         |         |         |        |
|-------------------------------------|--|---------|---------|---------|---------|--------|
|                                     | 2002   | 2003    | 2004    | 2005    | 2006    | 2006   |
|                                     | RMB  | RMB     | RMB     | RMB     | RMB     | US\$   |
|                                     | (in millions, except share, per share and per ADS information) |         |         |         |         |        |
| U.S. GAAP <sup>(2)</sup>            |  |         |         |         |         |        |
| Property, plant and equipment       | 195,100  | 203,486 | 215,240 | 218,362 | 218,903 | 28,049 |
| Total assets                        | 293,768  | 316,898 | 334,003 | 385,618 | 458,415 | 58,740 |
| Total long-term debt <sup>(4)</sup> | 12,687   | 672     |         |         |         |        |
| Fixed rate notes <sup>(5)</sup>     | 4,961  | 4,984   |         |         |         |        |
| Convertible notes <sup>(6)</sup>    | 5,711  | 5,735   | 5,725   |         |         |        |
| Bonds                               | 13,000   | 13,000  | 13,000  | 12,912  | 12,937  | 1,658  |
| Deferred payable <sup>(7)</sup>     | 15,176   | 9,976   | 23,633  | 23,633  | 23,633  | 3,028  |
| Shareholders' equity                | 159,936  | 190,828 | 198,119 | 237,252 | 282,690 | 36,223 |

**Other Financial Data:****Hong Kong GAAP**

|  |          |          |          |          |           |          |
|--|----------|----------|----------|----------|-----------|----------|
| Capital expenditures and land lease prepayments <sup>(8)</sup> | 41,000   | 43,871   | 59,143   | 67,106   | 77,566    | 9,938    |
| Net cash from operating activities                             | 69,422   | 85,534   | 103,779  | 131,709  | 149,346   | 19,136   |
| Net cash used in investing activities                          | (64,117) | (54,292) | (73,302) | (87,116) | (118,841) | (15,228) |
| Net cash from/(used in) financing activities                   | 5,449    | (24,688) | (24,457) | (25,173) | (23,587)  | (3,022)  |
| Dividend declared or proposed                                  | 6,678    | 7,517    | 13,789   | 21,026   | 31,156    | 3,992    |

**U.S. GAAP<sup>(2)</sup>**

|   |        |        |         |         |         |        |
|---|--------|--------|---------|---------|---------|--------|
| Net cash flow from operating activities | 88,429 | 93,131 | 111,112 | 131,593 | 150,401 | 19,272 |
| Dividend declared or proposed           | 6,678  | 7,517  | 13,789  | 21,026  | 31,156  | 3,992  |

(1) The basic net income per share and per ADS amounts under Hong Kong GAAP for the years ended December 31, 2002, 2003, 2004, 2005 and 2006 have been computed by dividing profit attributable to our equity shareholders by the weighted average number of shares and the weighted average number of ADSs, respectively, outstanding during 2002, 2003, 2004, 2005 and 2006. The diluted net income per share under Hong Kong GAAP for the years ended December 31, 2002, 2003, 2004, 2005 and 2006 has been computed after adjusting for the effects of all dilutive potential ordinary shares, respectively.

The basic net income per share and per ADS amounts under U.S. GAAP for the year ended December 31, 2002 have been computed by dividing profit attributable to equity shareholders by the weighted average number of shares and the weighted average number of ADSs, respectively, as if 827,514,446 ordinary shares representing 165,502,889 ADSs issued to China Mobile Hong Kong (BVI) Limited as part of the consideration in the acquisition of Anhui Mobile, Jiangxi Mobile, Chongqing Mobile, Sichuan Mobile, Hubei Mobile, Hunan Mobile, Shaanxi Mobile and Shanxi Mobile were outstanding during these periods (in addition to shares actually issued during these years). The basic net income per share and per ADS amounts under U.S. GAAP for the years ended December 31, 2003, 2004, 2005 and 2006 have been computed by dividing profit attributable to equity shareholders by the weighted average number of shares and weighted average number of ADSs, respectively, outstanding

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during 2003, 2004, 2005 and 2006.

The diluted net income per share under U.S. GAAP for the years ended December 31, 2002, 2003, 2004, 2005 and 2006 has been computed after adjusting for the effects of all dilutive potential ordinary shares, respectively. For the years ended December 31, 2002, 2003, 2004, 2005 and 2006 all dilutive potential ordinary shares resulting from the share options granted to the directors and employees under the share option scheme would decrease profit attributable to equity shareholders per share. For the years ended December 31, 2002, 2003, 2004 and 2005 all dilutive potential ordinary shares resulting from convertible notes would decrease profit attributable to equity shareholders per share.

- (2) The amounts for the years ended December 31, 2002, 2003, 2004, 2005 and 2006 are presented to reflect our acquisitions of various regional mobile telecommunications companies and other telecommunications assets from our immediate holding company under the as if pooling-of-interests method, as well as the effects of other differences between Hong Kong GAAP and U.S. GAAP.
- (3) Includes short-term bank and other loans, current portion of long-term bank and other loans and current portion of capital lease obligations.
- (4) Includes long-term bank and other loans and obligations under capital leases, net of current portion.
- (5) The fixed rate notes issued on November 2, 1999 with an aggregate principal amount of US\$600 million were fully redeemed on November 2, 2004.
- (6) The convertible notes issued on November 3, 2000 with an aggregate principal amount of US\$690 million were fully redeemed on November 3, 2005.
- (7) Represents the balance of the purchase consideration payable to our immediate holding company for our acquisition of the eight regional mobile telecommunications companies in 2002 and for our acquisition of the ten regional mobile telecommunications companies and other telecommunications assets in 2004, as applicable. See Item 4. Information on the Company.
- (8) Represents payments made for capital expenditures and land lease prepayments during the year.

**Exchange Rate Information**

We publish our consolidated financial statements in Renminbi. Solely for the convenience of the reader, this annual report on Form 20-F contains translations of certain Renminbi and Hong Kong dollar amounts into U.S. dollars and vice versa at RMB7.8041 = US\$1.00 and HK\$7.7771 = US\$1.00, the noon buying rates in New York City for cable transfers as certified for customs purposes by the Federal Reserve Bank of New York on December 29, 2006. These translations should not be construed as representations that the Renminbi or Hong Kong dollar amounts could actually be converted into U.S. dollars at such rates or at all.

The noon buying rates in New York City for cable transfers as certified for customs purposes by the Federal Reserve Bank of New York were RMB7.6377 = US\$1.00 and HK\$7.8116 = US\$1.00, respectively, on June 6, 2007. The following table sets forth the high and low noon buying rates between Renminbi and U.S. dollars and between Hong Kong dollars and U.S. dollars for each month during the previous six months:

**Noon Buying Rate**

|                                | RMB per<br>US\$1.00 |        |                                | HK\$ per<br>US\$1.00 |        |
|--------------------------------|---------------------|--------|--------------------------------|----------------------|--------|
|                                | High                | Low    |                                | High                 | Low    |
| December 2006                  | 7.8350              | 7.8041 | December 2006                  | 7.7787               | 7.7665 |
| January 2007                   | 7.8127              | 7.7705 | January 2007                   | 7.8112               | 7.7797 |
| February 2007                  | 7.7632              | 7.7410 | February 2007                  | 7.8141               | 7.8041 |
| March 2007                     | 7.7454              | 7.7232 | March 2007                     | 7.8177               | 7.8093 |
| April 2007                     | 7.7345              | 7.7090 | April 2007                     | 7.8212               | 7.8095 |
| May 2007                       | 7.7065              | 7.6463 | May 2007                       | 7.8236               | 7.8044 |
| June 2007 (up to June 6, 2007) | 7.6503              | 7.6377 | June 2007 (up to June 6, 2007) | 7.8116               | 7.8062 |

The following table sets forth the average noon buying rates between Renminbi and U.S. dollars and between Hong Kong dollars and U.S. dollars for each of 2002, 2003, 2004, 2005 and 2006, calculated by averaging the noon buying rates on the last day of each month during the relevant year.

**Table of Contents****Average Noon Buying Rate**

|      | <b>RMB per US\$1.00</b> | <b>HK\$ per US\$1.00</b> |
|------|-------------------------|--------------------------|
| 2002 | 8.2772                  | 7.7996                   |
| 2003 | 8.2771                  | 7.7864                   |
| 2004 | 8.2768                  | 7.7899                   |
| 2005 | 8.1826                  | 7.7755                   |
| 2006 | 7.9579                  | 7.7685                   |

**Risk Factors**

We wish to caution readers that the following important factors, and those important factors described in other reports submitted to, or filed with, the U.S. Securities and Exchange Commission, among other factors, could affect our actual results and could cause our actual results to differ materially from those expressed in any forward-looking statements made by us or on our behalf, and that such factors may materially and adversely affect our business and financial results and therefore the value of your investment.

**Risks Relating to Our Business**

*Extensive government regulation may limit our flexibility to respond to market conditions, competition or changes in our cost structure.*

The Ministry of Information Industry of the PRC regulates, among other things, the following areas of the telecommunications industry under the leadership of the State Council of the PRC, or the State Council:

formulating and enforcing industry policy, standards and regulations;

granting telecommunications licenses and permits;

formulating interconnection and settlement standards for implementation between telecommunications networks;

together with other relevant regulatory authorities, formulating tariff and service charge standards for certain telecommunications services;

supervising the operations of telecommunications services providers;

promoting fair and orderly market competition among operators; and

allocating and administering public telecommunications resources, such as radio frequencies, numbering resources, domain names and addresses of telecommunications networks.

Other PRC government authorities also take part in regulating the telecommunications industry in the areas such as tariff policies and foreign investment. The regulatory framework within which we operate may limit our flexibility to respond to market conditions, competition or changes in our cost structure. Moreover, we cannot predict when or if changes in tariff policies or rates may occur. Future adverse changes in tariff policies and rates could decrease our revenues and reduce our profitability.



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We operate our businesses with approvals granted by the State Council and under licenses granted by the Ministry of Information Industry. If these approvals or licenses are revoked or suspended, or if the conditions or other obligations relating to these approvals or licenses are amended in any material adverse respect, our business and operations will be materially and adversely affected. Moreover, while we are actively preparing for 3G business, we cannot assure you that we will be granted the requisite approvals and licenses by the PRC government in a timely manner, or at all.

*We may be affected by future regulatory changes.*

To provide a uniform regulatory framework for the orderly development of the telecommunications industry, the Ministry of Information Industry, under the direction of the State Council, has been preparing a draft telecommunications law. According to the 2007 legislation agenda of the National People's Congress, the draft telecommunications law has not yet been scheduled for review or adoption, although it is reportedly one of nine draft legislations reserved for potential review. If and when the telecommunications law is adopted by the National People's Congress, it is expected to become the fundamental telecommunications statute and the legal basis for telecommunications regulations in Mainland China. In 2000, the State Council promulgated a set of

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telecommunications regulations, or the Telecommunications Regulations, that apply in the interim period prior to the adoption of the telecommunications law. Although we expect that the telecommunications law will positively affect the overall development of the telecommunications industry in Mainland China, we do not fully know what the nature and scope of the telecommunications law will be. The telecommunications law and other new telecommunications regulations or rules may contain provisions that could materially and adversely affect our business, financial condition and results of operations.

***The PRC government may require major operators, including us, to provide universal services with specified obligations, and we may not be compensated adequately for providing such services.***

Under the Telecommunications Regulations, telecommunications operators in Mainland China are required to fulfill universal service obligations in accordance with relevant regulations to be promulgated by the PRC government, and the Ministry of Information Industry has the authority to delineate the scope of universal service obligations. The Ministry of Information Industry, together with other PRC governmental authorities, is also responsible for formulating administrative rules relating to the establishment of a universal service fund and compensation schemes for universal services. These rules have not yet been promulgated, and there are currently no specific regulatory requirements relating to the provision of universal services in Mainland China.

While the scope of specific universal services obligations is not yet clear, we believe that such services may include mandatory provision of basic mobile telecommunications services in less economically developed areas in Mainland China and mandatory contribution to a universal service fund. In addition, as part of the transitional measures prior to the formalization of a universal service obligation framework, the Ministry of Information Industry has required major telecommunications services providers in Mainland China, including China Mobile Communications Corporation, or CMCC, to participate in a project to provide basic telecommunications services in remote villages in Mainland China.

We cannot predict whether we will be required to provide universal services in the future and, if so, whether we will be adequately compensated by the government or by the universal service fund. We also cannot assure you whether we will be required to make contribution to the universal service fund. Any of these events may materially and adversely affect our financial condition and results of operations.

***Competition from other telecommunications services providers may affect our subscriber growth and profitability by causing the rate of our subscriber growth to decline and bringing about decreases in tariff rates and increases in selling and promotional expenses.***

We compete with other telecommunications services providers in all of the thirty-one provinces, autonomous regions and directly-administered municipalities in Mainland China. The PRC government encourages orderly competition in the telecommunications industry in Mainland China. In particular, the PRC government has extended favorable regulatory policies to some of our competitors, such as China United Telecommunications Corporation, or China Unicom, in order to help them become more viable competitors. For example, the PRC government has permitted China Unicom to lower its mobile telecommunications services tariffs by up to 10% below the government standard rates. We believe this policy has helped China Unicom capture a significant number of price-sensitive mobile telecommunications services subscribers.

In addition, China Telecommunications Corporation, or China Telecom, and China Netcom Communications Group Corporation, or China Netcom, provide Xiaolingtong services to their customers. Xiaolingtong is a local area wireless telephone service with limited mobility and limited coverage. Xiaolingtong offers lower-priced services. As a result, Xiaolingtong services have, to a certain extent, attracted customers principally in the low-end markets. Competition from other wireless telecommunications services, including Xiaolingtong, could materially and adversely affect our business and prospects.

Increased competition from other telecommunications services providers, including China Unicom, China Telecom and China Netcom, introduction of new competitors, or the issuance of additional mobile telecommunications services licenses, including 3G licenses, could adversely affect our business by, among other factors, causing the rate of our subscriber growth to decline and bringing about decreases in tariff rates and increases in selling and promotional costs and expenses. This could in turn have a material adverse effect on our financial condition, results of operations and prospects.

***New entrants in and further restructuring of the telecommunications industry in Mainland China may further intensify competition and materially and adversely affect our business and prospects.***

The current prevailing PRC government policy concerning the telecommunications sector is to encourage orderly competition. In particular, we face competition from other telecommunications services providers, including China Unicom, China Telecom and China Netcom. See Item 4. Information on the Company The History and Development of the Company Industry



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Restructuring and Changes in Our Shareholding Structure . The State Council may approve additional telecommunications services providers in the future, including providers of mobile telecommunications services that may compete with us. If and when the State Council approves additional providers of mobile telecommunications services, any increased competition from these new entrants in Mainland China's telecommunications industry could materially and adversely affect our financial condition and results of operations as a result of, among others, decreases in the rate of subscriber growth or tariff rates or increases in selling and promotional expenses.

In addition, the rapid development of new technologies and other factors may cause the PRC government to further adjust the existing structure of the PRC telecommunications industry, which might change the competitive landscape of the industry. We are not currently aware of any specific government plan relating to any industry restructuring. On the other hand, media reports about potential restructurings have been published from time to time, and there continues to be market speculation and expectation about potential restructurings. Any further industry restructuring may affect the operations of all or some telecommunications operators in China, including us. We may be subject to competition from new providers of telecommunications services as a result of technological developments and the convergence of various telecommunications services. These new entrants and the industry restructuring may also cause the existing competition in the telecommunications industry in Mainland China to intensify, which may materially and adversely affect our business, financial condition, results of operations and prospects. In addition to any potential intensified competition, any further industry restructuring, whether or not directly involving us, may also result in changes that could materially and adversely affect our business, financial condition, results of operations and prospects.

### ***We are controlled by CMCC, which may not always act in our best interest.***

As of May 31, 2007, CMCC indirectly owned an aggregate of approximately 74.46% of our outstanding shares. Accordingly, CMCC is, and will be, able to:

nominate substantially all of the members of our board of directors and, in turn, indirectly influence the selection of our senior management;

determine the timing and amount of our dividend payments; and

otherwise control or influence actions that require approvals of our shareholders.

The interests of CMCC as our ultimate controlling person may conflict with the interests of our minority shareholders.

In addition, CMCC provides our operating subsidiaries in Mainland China with services that are necessary for our business activities, including:

international services arrangements including, among others, international roaming arrangements, international interconnection arrangements and international transmission lines leasing arrangements;

the coordination of the provision of inter-provincial transmission leased lines from the relevant transmission line providers in Mainland China to us; and

certain property leasing and telecommunications services arrangements.

The interests of CMCC as the provider of these services to our operating subsidiaries in Mainland China may conflict with our interests. Furthermore, the State-Owned Assets Supervision and Administration Commission, or the SASAC, an agency of the State Council established in 2003, has responsibilities as an investor of state-owned assets on behalf of the PRC government and promulgates rules, regulations and policies from time to time that govern, among other things, the supervision, reform and management of state-owned enterprises, including CMCC. Actions taken by the SASAC may have an indirect material and adverse effect on our business, financial condition and results of operations, and may conflict with the interests of our minority shareholders.

*The limited spectrum allocated to us may constrain our future network capacity growth.*

A mobile telecommunications network's capacity is to a certain extent limited by the amount of frequency spectrum available for its use. Since the Ministry of Information Industry allocates frequency spectrum to mobile telecommunications operators in Mainland China, the capacity of our mobile telecommunications network is limited by the amount of spectrum that the Ministry of Information Industry allocates to our parent company, CMCC. The Ministry of Information Industry has allocated a total of 44 MHz of spectrum, used for transmission and reception nationwide, respectively, in the 900 MHz frequency band and the 1800 MHz frequency band to our parent company, CMCC. Under the existing agreement between CMCC and us, we have the exclusive rights to use the allocated frequency spectrum in Mainland China.

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We believe that our current spectrum allocation is sufficient for anticipated subscriber growth in the near term. However, we may need additional spectrum to accommodate future subscriber growth or to develop mobile telecommunications services using new wireless telecommunications technologies. Moreover, we may not be able to obtain additional spectrum from the Ministry of Information Industry. Our network expansion plans may be affected if we are unable to obtain additional spectrum. This could in turn constrain our future network capacity growth and materially and adversely affect our business and prospects as well as our financial condition and results of operations.

### ***Changes to our interconnection and leased line arrangements may increase our operating expenses and adversely affect our profitability.***

Our mobile telecommunications services depend, in large part, upon our interconnection arrangements and access to other networks. Interconnection is necessary in the case of all local calls between our subscribers and subscribers of other networks. Interconnection and leased line arrangements are also necessary for international and certain domestic calls. We have entered into interconnection and transmission line leasing agreements with other operators. We cannot assure you that increasing usage of the other networks would not result in additional strain on its switching capacity, or that the existing quality of the other networks will remain adequate.

The terms of our interconnection arrangements and leased line arrangements have a material effect on our operating revenue and expenses. In addition, our business and operations may be materially and adversely affected if we cannot enter into future interconnection and leased line agreements on acceptable terms or on a timely basis.

### ***We may be unable to obtain sufficient financing to fund our substantial capital requirements, which could limit our growth potential and future prospects.***

We estimate that we will require approximately RMB293.8 billion (approximately US\$37.6 billion) for capital expenditures from 2007 through the end of 2009 for a range of projects and other expenditures, including among others, the construction of GSM networks, support systems, transmission and structural facilities, and the development of new technologies and new businesses. These amounts, however, do not include specific capital expenditures that would be required for the construction of 3G networks.

We believe that cash from operations, together with any necessary borrowings, will provide sufficient financial resources to meet our projected capital and other expenditure requirements. We may require additional funds to the extent we have underestimated our capital requirements or overestimated our future cash flows from operations. In addition, a significant feature of our business strategy is to continue exploring opportunities in developing new technologies and new businesses in the telecommunications industry, which may require additional capital resources.

The cost of implementing new technologies and upgrading our networks or expanding network capacity may also be significant. In order for us to effectively respond to technological changes, we may be required to make substantial capital expenditures in the near future. In particular, to the extent we are granted any 3G license by the Ministry of Information Industry, we may need to make substantial capital expenditures and other investments in order to effectively implement new 3G-based technologies. However, the timing and magnitude of these capital expenditures and other investments involve many uncertainties that are beyond our control, and depend in part on when we may be granted such a license, how many licenses the Ministry of Information Industry may issue and which 3G-based technology standard we will be required to adopt. If we are required to make substantial capital expenditures and other investments in order to effectively implement new 3G-based technologies, our financial condition, results of operations and cash flow may be materially and adversely affected in one or more given periods.

Financing may not be available to us on acceptable terms or on a timely basis. In addition, any future issuance of equity securities, including securities convertible into or exchangeable for or that represent the right to receive equity securities, may require approval from the relevant government authorities. If adequate capital is not available, our growth potential and future prospects could be materially and adversely affected. Our ability to obtain additional financing on favorable commercial terms will depend on a number of factors, including:

our future financial condition, results of operations and cash flows;

general market conditions for financing activities by telecommunications companies; and

economic, political and other conditions in the markets where we operate.



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### ***Changes in technology may render our current technologies obsolete and thus affect our business and market position.***

The telecommunications industry is dependent upon rapidly changing and increasingly complex technologies. Accordingly, although we strive to keep our technologies up to international standards, the mobile telecommunications technologies that we currently employ may become obsolete or subject to competition from new technologies in the future, including new wireless telecommunications technologies. In addition, the development and application of new technologies involves time, substantial costs and risks. We may encounter unexpected technological difficulties in implementing new technologies, including any 3G-based technology, and as a result may incur substantial costs or service disruptions, which could have a material adverse effect on our business, financial condition and results of operations. Furthermore, the new technologies we may implement, such as 3G, may not generate an acceptable or commercially viable rate of return.

### ***Failure to capitalize on new business opportunities may have a material adverse effect on our growth potential.***

We intend to pursue new growth opportunities in the broader telecommunications industry. Our success will depend in large part on our ability to offer services that address the market demand arising from these opportunities. In addition, our ability to deploy and deliver these services depends, in many instances, on new and unproven technologies. Our wireless telecommunications technologies may not perform as expected. We may not be able to successfully develop or obtain new technologies to effectively and economically deliver these services. Furthermore, we may not be able to compete successfully in the delivery of telecommunications services based on new technologies. Moreover, we may pursue acquisitions from time to time, and we cannot assure you that we will be successful in pursuing such acquisitions or will otherwise be able to successfully integrate any acquired companies or assets into our existing operations. Any failure to capitalize on new business opportunities may have a material adverse effect on our competitive position and future profitability.

### ***Actual or perceived health risks associated with the use of mobile devices could impair our ability to retain and attract customers, reduce wireless telecommunications usage or result in litigation.***

There has been public speculation about possible health risks to individuals from exposure to electromagnetic fields from base stations and from the use of wireless telephone handsets. While a substantial amount of scientific research conducted to date by various independent research bodies has shown that radio signals, at levels within the limits prescribed by public health authority safety standards and recommendations, present no adverse effect to human health, we cannot be certain that future studies, irrespective of their relative reliability or trustworthiness, will not impute a link between electromagnetic fields and adverse health effects. Research into these issues is ongoing by government agencies, international health organizations and other scientific bodies in order to develop a better scientific understanding and public awareness of these issues. In addition, several wireless industry participants were the targets of lawsuits alleging various health consequences as a result of wireless phone usage or seeking protective measures. While we are not aware of any scientific studies or objective evidence which substantiates such alleged health risks, we cannot assure you that the actual, or perceived, risks associated with radio wave transmission will not impair our ability to retain customers and attract new customers, reduce wireless telecommunications usage or result in litigation.

### ***Any failure to achieve and maintain effective internal controls could have a material adverse effect on our reputation, business, results of operations and the market prices of our shares and ADSs.***

Effective internal controls are necessary for us to provide reasonable assurance with respect to our financial reports and to effectively prevent fraud. If we cannot provide reasonable assurance with respect to our financial reports and effectively prevent fraud, our reputation, business and results of operations could be harmed.

We are required to comply with various Hong Kong and U.S. laws and regulations on internal controls, including the Sarbanes-Oxley Act of 2002. In particular, Section 404 of the Sarbanes-Oxley Act of 2002 requires that we include a report of management on our internal control over financial reporting in our Annual Reports on Form 20-F, beginning with this Annual Report on Form 20-F for the fiscal year ended December 31, 2006, that contains an assessment by management of the effectiveness of our internal control over financial reporting. In addition, our independent registered public accounting firm must attest to and report on management's assessment of the effectiveness of our internal control over financial reporting.

Internal controls may not prevent or detect misstatements because of their inherent limitations, including the possibility of human error, the circumvention or overriding of controls, or fraud. Therefore, even effective internal controls can provide only reasonable assurance with respect to the preparation and fair presentation of financial statements. If we fail to maintain the adequacy of our internal control over financial reporting, as these standards are modified, supplemented or amended from time to time, our management may not be able to conclude on an ongoing basis that we have effective internal control over financial reporting in accordance with Section 404. Moreover, even if our management concludes that our internal control over financial reporting is effective, our independent registered public accounting firm may disagree. If our independent registered public accounting firm is not satisfied with our internal control over financial reporting or the level at which our controls



are documented, designed, operated or

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reviewed, or if the independent registered public accounting firm interprets the requirements, rules or regulations differently from us, then it may decline to attest to our management's assessment or may issue an adverse opinion. Any of these possible outcomes could result in an adverse reaction in the financial marketplace due to a loss of investor confidence in the reliability of our consolidated financial statements, which ultimately could negatively impact the market prices of our shares and ADSs. In addition, ineffective internal control over financial reporting could expose us to increased risk of fraud or misuse of corporate assets and subject us to potential delisting from the New York Stock Exchange, regulatory investigations and civil or criminal sanctions.

***We may conduct an A share offering in the PRC, which may result in increased regulatory scrutiny and compliance costs as well as increased fluctuations in the prices of our ordinary shares and ADSs listed in overseas markets.***

We intend to conduct a public offering and listing of our A shares in the PRC, which are a separate class of our ordinary shares denominated in Renminbi and listed on a PRC stock exchange, although no specific timetable for the offering has been set. The precise timing of our A share offering would depend on a number of factors, including the receipt of relevant regulatory approvals and market conditions. If the A share offering is completed, we would become subject to the applicable laws, rules and regulations governing public companies listed in the PRC, in addition to the various laws, rules and regulations that we are currently subject to in Hong Kong and the United States. The listing and trading of our securities in multiple jurisdictions and multiple markets may lead to increased compliance costs for us, and we face the risk of significant intervention by regulatory authorities in these jurisdictions and markets.

In addition, under the current laws, rules and regulations in the PRC, our ordinary shares listed on the Hong Kong Stock Exchange and our A shares are neither interchangeable nor fungible, and there is no trading or settlement between these two markets. Furthermore, these two markets have different trading characteristics and investor bases, including different levels of retail and institutional participation. As a result of these differences, the trading prices of our ordinary shares listed on the Hong Kong Stock Exchange and our A shares may not be the same. The issuance of A shares and fluctuations in our A share trading price may also lead to increased volatility in, and may otherwise materially and adversely affect, the prices of our ordinary shares and ADSs listed in overseas markets.

## **Risks Relating to the Telecommunications Industry in Mainland China**

***China's accession into the World Trade Organization has gradually eased, and may continue to ease, restrictions on foreign ownership in the telecommunications industry and may increase competition in the mobile telecommunications services sector.***

On December 11, 2001, China officially joined the World Trade Organization, or the WTO. On January 1, 2002, the Administration of Foreign-Funded Telecommunications Enterprises Provisions was also adopted, thereby implementing China's commitments to the WTO. Those commitments included the gradual reduction of foreign ownership restrictions in the telecommunications industry and the opening of the telecommunications market in Mainland China to foreign investors. See Item 4. Information on the Company Business Overview Competition. This could lead to increased foreign investment in the telecommunications market in Mainland China, which may in turn increase competition and foreign participation in the mobile telecommunications services sector in Mainland China. Increased competition and foreign participation may have a material adverse effect on our financial condition and results of operations as well as our business and prospects.

***Our share price has been and may continue to be volatile in response to conditions in the global securities markets generally and in the telecommunications and technology sectors in particular.***

Our share price has been subject to significant volatility, in part due to highly volatile securities markets, particularly for telecommunications companies' shares, as well as variations in our sales and profit from operations. Factors other than our results of operations that may affect our share price include, among other things, overall market conditions and performance, market expectations of our performance, projected growth in the mobile telecommunications market in Mainland China and adverse changes in our brand value. In addition, our share price may be affected by factors such as the level of business activity or perceived growth (or the lack thereof) in the telecommunications market in general, the performance of other telecommunications companies, announcements by or the results of operations of our competitors, customers and suppliers, the success of 3G mobile networks and new technologies, products and services. See Item 9. The Offer and Listing for information regarding the trading price history of our ordinary shares and ADSs.

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### **Risks Relating to Mainland China**

***An economic slowdown in Mainland China could materially and adversely affect our financial condition, results of operations and prospects.***

We conduct most of our business and generate substantially all our revenues in Mainland China. As a result, economic, political and legal developments in Mainland China have a significant effect on our financial condition and results of operations, as well as our future prospects. In recent years, Mainland China has been one of the world's fastest growing economies in terms of GDP growth. However, such growth may not be sustained in the future. Moreover, the slowdown in other major economies of the world, such as the United States, the European Union and certain Asian countries may adversely affect economic growth in Mainland China. Our financial condition and results of operations, as well as our prospects, could be materially and adversely affected by an economic downturn in Mainland China.

***Adverse changes in the economic policies of the PRC government could have a material adverse effect on the overall economic growth of Mainland China, which could reduce the demand for our services and have a material adverse effect on our business, financial condition and results of operations.***

Since the late 1970s, the PRC government has been reforming the Chinese economic system. These reforms have resulted in significant economic growth and social progress. Although we believe that economic reform and macroeconomic policies and measures adopted by the PRC government may continue to have a positive effect on the economic development of Mainland China and that we may continue to benefit from such policies and measures, these policies and measures may from time to time be modified or revised. Adverse changes in economic and social conditions in Mainland China, in the policies of the PRC government or in the laws and regulations in Mainland China could have a material adverse effect on the overall economic growth of Mainland China and investment in the telecommunications industry in Mainland China. These developments could materially and adversely affect our business, such as reducing the demand for our services, as well as our financial condition and results of operations.

***The Renminbi is not a freely convertible currency, which could limit the ability of our subsidiaries in Mainland China to obtain sufficient foreign currencies to satisfy their foreign currency requirements or pay dividends to us.***

Substantially all of our revenues and operating expenses are denominated in Renminbi, while a portion of our capital expenditures and indebtedness are denominated in U.S. dollars and other foreign currencies. The Renminbi is currently freely convertible under the current account, which includes dividends, trade and service-related foreign currency transactions, but not under the capital account, which includes foreign direct investment, unless the prior approval of the State Administration of Foreign Exchange is obtained.

Our operating subsidiaries are foreign invested enterprises. Currently, they may purchase foreign currency without the approval of the State Administration of Foreign Exchange for settlement of current account transactions, including payment of dividends, by providing commercial documents evidencing these transactions. They may also retain foreign exchange in their current accounts (subject to a cap approved by the State Administration of Foreign Exchange) to satisfy foreign currency liabilities or to pay dividends. However, the relevant PRC government authorities may limit or eliminate our operating subsidiaries' ability to purchase and retain foreign currencies in the future. In addition, our subsidiaries incorporated in Mainland China may not be able to obtain sufficient foreign currencies to satisfy their foreign currency requirements or pay dividends to us for our use in making any future dividend payments or in meeting our other foreign currency payment requirements. Foreign currency transactions under the capital account are still subject to limitations and require approvals from the State Administration of Foreign Exchange. This could affect our subsidiaries' ability to obtain foreign currencies through debt or equity financing, including by means of loans or capital contributions from us.

***Fluctuations in exchange rates could materially and adversely affect our financial results.***

Substantially all of our revenues and operating expenses are denominated in Renminbi, while a portion of our capital expenditures and indebtedness are denominated in foreign currencies, such as U.S. dollars and Hong Kong dollars. The value of the Renminbi against the U.S. dollar and other currencies may fluctuate and is affected by, among other things, changes in China's political and economic conditions. The conversion of the Renminbi into U.S. dollars and other foreign currencies has been based on the rates set by the People's Bank of China. On July 21, 2005, the PRC government changed its decade-old policy of pegging the value of the Renminbi solely to the U.S. dollar. Instead, the value of the Renminbi is now pegged against a basket of currencies, determined by the People's Bank of China, against which it is permitted to fluctuate within a managed band. On May 18, 2007, the People's Bank of China widened the floating band of the Renminbi trading prices against the U.S. dollar in the inter-bank spot foreign exchange market from 0.3% to 0.5%. The value of the Renminbi may fluctuate significantly against the U.S. dollar in the future, depending on, among other things, the fluctuation of the basket of currencies against which the Renminbi is currently valued. In addition, the Renminbi may in the future be permitted to enter into a full float, which may also result in a significant

fluctuation of the Renminbi against the U.S. dollar. Fluctuations in exchange rates, primarily those involving the U.S. dollar, may have a material adverse effect on our financial condition and results of operations.

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### ***The PRC legal system contains uncertainties which could limit the legal protections available to our shareholders.***

The PRC legal system is a civil law system based on written statutes. Unlike common law systems, it is a system in which decided legal cases have little precedential value. Since the late 1970s, the PRC government has been promulgating a comprehensive system of laws and regulations governing economic matters in general. Legislation since then has significantly enhanced the protection afforded to foreign investment in Mainland China. Our existing subsidiaries in Mainland China are wholly foreign-owned enterprises, which are enterprises incorporated in Mainland China and wholly-owned by Hong Kong, Macau, Taiwan or foreign investors, and subject to the laws and regulations applicable to foreign investment in Mainland China. However, the interpretation and enforcement of some of these laws, regulations and other legal requirements involve uncertainties that could limit the legal protections available to our shareholders. Moreover, China's entry into the WTO has resulted and may in the future result in the abolition of or substantial amendments to the existing laws, regulations and other legal requirements. See Item 4. Information on the Company Business Overview World Trade Organization .

### ***Any future outbreak of severe acute respiratory syndrome, avian flu or similar adverse public health developments in China may have a material adverse effect on our financial condition and results of operations.***

In late 2002 and the first half of 2003, China and certain other countries and regions experienced an outbreak of severe acute respiratory syndrome, or SARS. On July 5, 2003, the World Health Organization declared that the SARS outbreak had been contained. Moreover, certain countries and regions, including China, have recently encountered incidents of the H5N1 strain of bird flu, or avian flu. We are unable to predict the effect, if any, that avian flu may have on our business. In particular, any future outbreak of SARS, avian flu or similar adverse public health developments may, among other things, significantly disrupt our ability to adequately staff our business, and may generally disrupt our operations. Furthermore, an outbreak may severely restrict the level of economic activity in affected areas, which may in turn materially and adversely affect our business and prospects. As a result, any future outbreak of SARS, avian flu or similar adverse public health developments may have a material adverse effect on our financial condition and results of operations.

## **Item 4. Information on the Company.**

We provide a full range of mobile telecommunications services in all 31 provinces, autonomous regions and directly-administered municipalities in Mainland China as well as in Hong Kong. As of December 31, 2006, the total population residing in Mainland China is approximately 1.3 billion. Based on publicly available information, we are the leading provider of mobile telecommunications services in Mainland China and the largest provider of mobile telecommunications services in the world as measured by total number of subscribers as of December 31, 2006. As of December 31, 2006, our total number of subscribers was approximately 301.2 million, representing approximately 67.5% of all mobile telecommunications services subscribers in Mainland China. As of April 30, 2007, our total number of subscribers reached approximately 321.4 million.

### **The History and Development of the Company**

We were incorporated under the laws of Hong Kong on September 3, 1997 as a limited liability company under the name China Telecom (Hong Kong) Limited . We changed our name to China Mobile (Hong Kong) Limited on June 28, 2000 and to China Mobile Limited on May 29, 2006 after obtaining the approval of our shareholders.

We completed our initial public offering in October 1997. Our ordinary shares are listed on the Hong Kong Stock Exchange, and our American Depositary Shares, or ADSs, each currently representing the right to receive five ordinary shares, are listed on the New York Stock Exchange.

### ***Expansion Through Acquisitions***

Our initial mobile telecommunications operations included those in Guangdong Province conducted by Guangdong Mobile Communication Company Limited (currently known as China Mobile Group Guangdong Co., Ltd.), or Guangdong Mobile, and in Zhejiang Province conducted by Zhejiang Mobile Communication Company Limited (currently known as China Mobile Group Zhejiang Co., Ltd.), or Zhejiang Mobile. As part of the restructuring in preparation for our initial public offering in 1997, the former Ministry of Posts and Telecommunications transferred to us a 100% equity interest in Guangdong Mobile and a 99.63% equity interest in Zhejiang Mobile. Since then, we have significantly expanded the geographical coverage of our operations through a series of acquisitions from CMCC, our indirect controlling shareholder, of mobile telecommunications operations conducted by its regional subsidiaries. In particular:

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We acquired Jiangsu Mobile Communication Company Limited (currently known as China Mobile Group Jiangsu Co., Ltd.), or Jiangsu Mobile, on June 4, 1998 for a cash consideration of HK\$22.5 billion.

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We acquired Fujian Mobile Communication Company Limited (currently known as China Mobile Group Fujian Co., Ltd.), or Fujian Mobile, Henan Mobile Communication Company Limited (currently known as China Mobile Group Henan Co., Ltd.), or Henan Mobile, and Hainan Mobile Communication Company Limited (currently known as China Mobile Group Hainan Co., Ltd.), or Hainan Mobile, on November 12, 1999 for a total purchase price of HK\$49.7 billion, consisting of HK\$19.0 billion in cash and the remaining HK\$30.7 billion in the form of 1,273,195,021 new shares. In addition, we acquired the remaining 0.37% equity interest in Zhejiang Mobile in June 1999.

We acquired Beijing Mobile Communication Company Limited (currently known as China Mobile Group Beijing Co., Ltd.), or Beijing Mobile, Shanghai Mobile Communication Company Limited (currently known as China Mobile Group Shanghai Co., Ltd.), or Shanghai Mobile, Tianjin Mobile Communication Company Limited (currently known as China Mobile Group Tianjin Co., Ltd.), or Tianjin Mobile, Hebei Mobile Communication Company Limited (currently known as China Mobile Group Hebei Co., Ltd.), or Hebei Mobile, Liaoning Mobile Communication Company Limited (currently known as China Mobile Group Liaoning Co., Ltd.), or Liaoning Mobile, Shandong Mobile Communication Company Limited (currently known as China Mobile Group Shandong Co., Ltd.), or Shandong Mobile, and Guangxi Mobile Communication Company Limited (currently known as China Mobile Group Guangxi Co., Ltd.), or Guangxi Mobile, on November 13, 2000 for a total purchase price of HK\$256.0 billion, consisting of HK\$74.6 billion in cash and the remaining HK\$181.4 billion in the form of 3,779,407,375 new shares.

We acquired Anhui Mobile Communication Company Limited (currently known as China Mobile Group Anhui Co., Ltd.), or Anhui Mobile, Jiangxi Mobile Communication Company Limited (currently known as China Mobile Group Jiangxi Co., Ltd.), or Jiangxi Mobile, Chongqing Mobile Communication Company Limited (currently known as China Mobile Group Chongqing Co., Ltd.), or Chongqing Mobile, Sichuan Mobile Communication Company Limited (currently known as China Mobile Group Sichuan Co., Ltd.), or Sichuan Mobile, Hubei Mobile Communication Company Limited (currently known as China Mobile Group Hubei Co., Ltd.), or Hubei Mobile, Hunan Mobile Communication Company Limited (currently known as China Mobile Group Hunan Co., Ltd.), or Hunan Mobile, Shaanxi Mobile Communication Company Limited (currently known as China Mobile Group Shaanxi Co., Ltd.), or Shaanxi Mobile, and Shanxi Mobile Communication Company Limited (currently known as China Mobile Group Shanxi Co., Ltd.), or Shanxi Mobile, on July 1, 2002 for a total purchase price of US\$8,573 million, consisting of an initial consideration of US\$5,773 million and a deferred consideration of US\$2,800 million. The initial consideration of US\$5,773 million consisted of a cash payment of US\$3,150 million and the issuance of new shares for the remaining US\$2,623 million to China Mobile Hong Kong (BVI) Limited on the completion of acquisition. We financed the cash portion of the initial consideration by applying a portion of our existing internal cash resources, in the amount of US\$2,400 million, combined with proceeds from the issuance of new shares in the amount of HK\$5.85 billion (equivalent to approximately US\$750 million) to Vodafone Holdings (Jersey) Limited, a wholly owned subsidiary of Vodafone Group Plc., or Vodafone. After the share placement, Vodafone's share holding in us increased from 2.18% to approximately 3.27%. The deferred consideration of US\$2,800 million is payable by the fifteenth anniversary of the date of the completion of acquisition, and we may make an early payment of all or part of the deferred consideration at any time. We used the entire proceeds from the RMB3 billion guaranteed bonds due 2007 and RMB5 billion guaranteed bonds due 2017, both issued on October 28, 2002 by Guangdong Mobile, our wholly-owned subsidiary, to satisfy part of the US\$2,800 million deferred consideration.

We acquired Neimenggu Mobile Communication Company Limited (currently known as China Mobile Group Neimenggu Co., Ltd.), or Neimenggu Mobile, Jilin Mobile Communication Company Limited (currently known as China Mobile Group Jilin Co., Ltd.), or Jilin Mobile, Heilongjiang Mobile Communication Company Limited (currently known as China Mobile Group Heilongjiang Co., Ltd.), or Heilongjiang Mobile, Guizhou Mobile Communication Company Limited (currently known as China Mobile Group Guizhou Co., Ltd.), or Guizhou Mobile, Yunnan Mobile Communication Company Limited (currently known as China Mobile Group Yunnan Co., Ltd.), or Yunnan Mobile, Xizang Mobile Communication Company Limited (currently known as China Mobile Group Xizang Co., Ltd.), or Xizang Mobile, Gansu Mobile Communication Company Limited (currently known as China Mobile Group Gansu Co., Ltd.), or Gansu Mobile, Qinghai Mobile Communication Company Limited (currently known as China Mobile Group Qinghai Co., Ltd.), or Qinghai Mobile, Ningxia Mobile Communication Company Limited (currently known as China Mobile Group Ningxia Co., Ltd.), or Ningxia Mobile, Xinjiang Mobile Communication Company Limited (currently known as China Mobile Group Xinjiang Co., Ltd.), or Xinjiang Mobile, Beijing P&T Consulting & Design Institute Company Limited (currently known as China Mobile Group Design Institute Co., Ltd.), or Jingyi, and China Mobile Communication Company Limited, or CMC, on July 1, 2004 for a total purchase price of US\$3,650 million, consisting of an initial consideration of US\$2,000 million and a deferred consideration of US\$1,650 million. The deferred consideration of US\$1,650 million is interest bearing and payable by the fifteenth anniversary of the date of the completion of acquisition, and we may make an early payment of all or part of the deferred consideration at any time.





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In addition, the Company acquired all of the issued and outstanding shares of China Resources Peoples Telephone Company Limited (currently known as China Mobile Peoples Telephone Company Limited, or Peoples), a mobile telecommunications services provider based in Hong Kong, on March 28, 2006 for a total purchase price of approximately HK\$3,384 million (US\$436 million). As a result, Peoples became our wholly-owned subsidiary.

These acquisitions have significantly enlarged our subscriber base and expanded the geographical coverage of our business. In addition, the integration of these acquired operations has enabled us to realize synergies and economies of scale. A discussion of the financial impact of these acquisitions is set forth in Item 5. Operating and Financial Review and Prospects.

### ***Industry Restructuring and Changes in Our Shareholding Structure***

Prior to 1993, all public telecommunications networks and services in Mainland China were controlled and operated by the former Ministry of Posts and Telecommunications through the former Directorate General of Telecommunications, provincial telecommunications administrations and their city and county level bureaus.

As part of the PRC government's restructuring of the telecommunications industry, the Ministry of Information Industry was formed in March 1998 to assume, among others, the responsibilities of the former Ministry of Posts and Telecommunications. One of the principal objectives of the restructuring was to separate the government's regulatory function from its business management functions in respect of state-owned enterprises. In the first half of 2000, the PRC government substantially completed the industry restructuring. As a result, the Ministry of Information Industry ceased to have an indirect controlling interest in us, and no longer exercises control over telecommunications operations, but continues in its capacity as industry regulator providing industry policy guidance as well as exercising regulatory authority over all telecommunications services providers in Mainland China.

In addition, as part of the restructuring, the telecommunications operations previously controlled by the former Ministry of Posts and Telecommunications were separated along four business lines: fixed-line telecommunications, mobile telecommunications, paging and satellite telecommunications. CMCC was established in July 1999 as a state-owned company to hold and operate the mobile telecommunications business nationwide resulting from the separation. As part of this separation, in July 1999 CMCC obtained the approximately 57% holding of voting shares and economic interest in China Mobile (Hong Kong) Group Limited, our indirect controlling shareholder, previously held by Telco Communications (Group) Limited, an entity 100% controlled by the former Ministry of Posts and Telecommunications. In addition, the remaining 43% interest in China Mobile (Hong Kong) Group Limited previously held by the Directorate General of Telecommunications was transferred to CMCC in May 2000. As a result, CMCC became the owner of all voting shares and economic interest in China Mobile (Hong Kong) Group Limited and thus all of the PRC government's interest in us. In addition, following the completion of the acquisition of the ten regional mobile telecommunications companies and other telecommunications assets by us in July 2004, CMCC ceased to operate mobile telecommunications businesses in Mainland China other than through us. As of May 31, 2007, CMCC indirectly owned approximately 74.46% of all our outstanding shares, including shares represented by ADSs.

As a state-owned company, the former China Telecommunications Corporation owns and operates fixed-line telephone and data telecommunications networks. In November 2001, the State Council formally approved the restructuring of the former China Telecommunications Corporation, China Netcom Corporation Limited and Jitong Network Communications Company Limited. Under the restructuring plan, China Netcom was formed in May 2002. China Netcom consists of ten regional telecommunications companies that were originally owned by the former China Telecommunications Corporation in Beijing, Tianjin, seven provinces and one autonomous region, China Netcom Corporation Limited and Jitong Network Communications Company Limited. China Telecom retained the telecommunications companies originally owned by the former China Telecommunications Corporation in the remaining provinces, autonomous regions and directly-administered municipalities. As a result, apart from us, principal participants in the telecommunications industry in Mainland China also include China Telecom, China Netcom, China Unicom, China Railway Communications Corporation Limited and China Satellite Communications Corporation. Among these six participants, China Unicom and we are the two operators that are licensed to provide mobile telecommunications services in Mainland China.

### **Organizational Structure**

As of May 31, 2007, CMCC, a company incorporated in China, owned 74.46% equity interest in us through intermediate holding companies. As of May 31, 2007, we owned 100% equity interests in Guangdong Mobile, Zhejiang Mobile, Jiangsu Mobile, Fujian Mobile, Henan Mobile, Hainan Mobile, Beijing Mobile, Shanghai Mobile, Tianjin Mobile, Hebei Mobile, Liaoning Mobile,



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Shandong Mobile, Guangxi Mobile, Anhui Mobile, Jiangxi Mobile, Chongqing Mobile, Sichuan Mobile, Hubei Mobile, Hunan Mobile, Shaanxi Mobile, Shanxi Mobile, Neimenggu Mobile, Jilin Mobile, Heilongjiang Mobile, Guizhou Mobile, Yunnan Mobile, Xizang Mobile, Gansu Mobile, Qinghai Mobile, Ningxia Mobile, Xijiang Mobile, Jingyi, CMC and Peoples through intermediate holding companies, and a 66.41% equity interest in Aspire Holdings Limited, or Aspire, a company incorporated in the Cayman Islands. We operate in all thirty-one provinces, autonomous regions and directly-administered municipalities throughout Mainland China and in Hong Kong. CMCC no longer operates mobile telecommunications businesses in Mainland China, other than through us.

## **General Information**

Our principal executive offices are located at 60th Floor, The Center, 99 Queen's Road Central, Hong Kong, China; telephone: 852-3121-8888. We also maintain a regional headquarters in each of our regional mobile telecommunications companies in Mainland China and Hong Kong. Our web site address is [www.chinamobileltd.com](http://www.chinamobileltd.com). The information on our web site is not a part of this annual report on Form 20-F.

## **Business Overview**

We offer mobile telecommunications services principally using the Global System for Mobile Communications, or GSM, standard. GSM is a pan-European mobile telecommunications system based on digital transmission and mobile telecommunications network architecture with roaming capabilities. Our GSM networks currently reach virtually all cities and counties and major roads and highways throughout Mainland China and, through the network of Peoples, a substantial part of Hong Kong.

## ***Our Strategy***

As a pioneer and the market leader in the world's largest mobile telecommunications market, we intend to further consolidate our market leading position in the mobile telecommunications market by innovatively developing new customers and new voice usage and value-added business opportunities as well as further expanding our efforts in exploring the markets in rural areas. We intend to continue enhancing our competitive advantages in terms of scale of operations, networks, support systems, brands, marketing and sales channels and services, and strengthening our ability to innovate in terms of services, businesses, technologies and management, so as to further develop our multi-media communications services and become the leader in providing mobile information. Moreover, we will commit ourselves fully to servicing the 2008 Beijing Olympics and carrying out planning and operational preparation for the new generation of mobile telecommunications networks and technologies.

We believe the mobile telecommunications market in Mainland China will continue to expand, and we have designed our business strategy to achieve sustainable growth. Our business strategy includes the following key elements:

develop new customers, particularly new corporate customers, and further expand our efforts in exploring the markets in rural areas;

develop new voice usage opportunities;

expand our efforts in developing value-added business;

enhance our competitive advantages in terms of scale of operations and networks;

refine and optimize our telecommunications and information technology supporting networks;

enhance our brand and improve our customer services;

strengthen our proprietary sales channels and our online sales and marketing channels;

continue to emphasize innovation in terms of services, businesses, technologies and management;

commit to serving the 2008 Beijing Olympics; and

plan and prepare for the construction and operation of the new generation of mobile telecommunications networks and technologies.

***Subscribers and Usage***

Our subscriber base has grown substantially from approximately 204.3 million at the end of 2004 to approximately 301.2 million at the end of 2006. Nearly half of our subscriber growth in 2006 came from rural areas. As of December 31, 2006, we had a market share of approximately 67.5% in Mainland China. As of April 30, 2007, our total number of subscribers reached approximately 321.4 million. Our subscriber growth is primarily attributable to a number of factors, including:

significant economic growth in our markets, including the development of rural areas;

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the PRC government's promotion of informatization ;

relatively low mobile penetration rates in the central and western regions as well as small and medium-sized cities and rural areas;

decreased cost of initiating services due to a decline in handset prices as well as the decrease in other tariffs for our services;

our increased marketing and sales efforts and new business initiatives; and

our competitive advantages in terms of scale of operations, networks, support systems, brands, marketing and sales channels and services.

Our acquisition of a total of 29 regional mobile telecommunications companies in Mainland China between June 1998 and July 2004 and our acquisition of Peoples in March 2006 have also substantially expanded our subscriber base. Our aggregate subscriber usage volume reached 1,252.1 billion minutes in 2006, representing an increase of approximately 38.6% from 2005. As of December 31, 2006, the number of our value-added business users reached 270.4 million, representing an increase of approximately 30.8% from December 31, 2005. Furthermore, our SMS usage volume reached 353.4 billion messages in 2006, representing an increase of approximately 41.6% from 2005.

The following table sets forth selected historical information about our subscriber base and subscriber usage for the periods indicated.

|  | As of or for the year ended |       |         |
|--|-----------------------------|-------|---------|
|  | December 31,                |       |         |
|  | 2004                        | 2005  | 2006    |
| Subscribers (in millions) <sup>(1)</sup>                                       |                             |       |         |
| Contract subscribers <sup>(2)</sup>  | 59.9                        | 61.3  | 65.3    |
| Prepaid subscribers <sup>(2)</sup>   | 144.4                       | 185.4 | 235.9   |
| Total  | 204.3                       | 246.7 | 301.2   |
| Minutes of Usage (in billions) <sup>(1) (3)</sup>                              |                             |       |         |
| Contract subscribers <sup>(2)</sup>  | 366.0                       | 428.1 | 511.1   |
| Prepaid subscribers <sup>(2)</sup>   | 294.9                       | 475.0 | 741.0   |
| Total  | 660.9                       | 903.1 | 1,252.1 |
| Average Minutes of Usage Per Subscriber Per Month (minutes) <sup>(1) (4)</sup> |                             |       |         |
| Contract subscribers <sup>(2)</sup>  | 517                         | 589   | 671     |
| Prepaid subscribers <sup>(2)</sup>   | 194                         | 241   | 293     |
| Blended  | 297                         | 335   | 381     |
| Average Revenue Per Subscriber Per Month (RMB) <sup>(1) (5)</sup>              |                             |       |         |
| Contract subscribers <sup>(2)</sup>  | 167                         | 185   | 207     |
| Prepaid subscribers <sup>(2)</sup>   | 56                          | 55    | 55      |
| Blended  | 92                          | 90    | 90      |
| Average Monthly Churn Rate (%) <sup>(1) (6)</sup>                              | 1.31                        | 1.87  | 2.73    |

(1) The historical information about our subscriber base and subscriber usage for 2006 includes that of the newly acquired Peoples.



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- (2) For management reference purposes, contract subscribers are classified to include GoTone subscribers and subscribers who have signed service contracts with us, while prepaid subscribers are classified to include subscribers of Shenzhouxing and M-Zone and local brands or packages targeting low usage volume users.
- (3) The total minutes of usage in 2004 include the full year minutes of usages of the ten regional mobile telecommunications companies we acquired in 2004 as if the acquisition occurred at the beginning of 2004 and are presented for ease of comparison.
- (4) Calculated by (A) dividing the total minutes of usage (calculated in the manner as set forth in note (3) above) during the relevant year by the average number of subscribers during the year (calculated as the average of the numbers of subscribers at the end of each of the thirteen calendar months from the end of the previous year to the end of the current year) and (B) dividing the result by 12.
- (5) Calculated by (A) dividing the operating revenue during the relevant year by the average number of subscribers during the year (calculated in the same manner as in note (4) above) and (B) dividing the result by 12. For purposes of this note (5) only, both operating revenues and average numbers of subscribers in 2004 take into account the full year effect of the ten regional mobile telecommunications companies we acquired in 2004 as if the acquisition occurred at the beginning of 2004.
- (6) Measures the monthly rate of subscriber disconnections from mobile telecommunications services, determined by dividing: (A) the result obtained by dividing (i) the sum of voluntary and involuntary terminations from our network (excluding internal transfer) during the relevant year by (ii) the average number of subscribers during the year (calculated in the same manner as in note (4) above) by (B) 12. On this basis, our calculated average monthly churn rate will be affected by the number of voluntary and involuntary terminations and the significant growth in our subscriber base. The average monthly churn rate in 2004 is calculated based on the full year information pertaining to the relevant regional mobile telecommunications companies we acquired in 2004, as if the acquisition occurred at the beginning of 2004, and is presented for ease of comparison.

### ***Businesses***

Our businesses primarily consist of voice business and value-added business.

***Voice Business.*** Our voice business refers to the business where our subscribers make and receive calls with a mobile phone at any point within the coverage area of our mobile telecommunications networks. The services include local calls, domestic long distance calls, international long distance calls, intra-provincial roaming, inter-provincial roaming and international roaming. Our voice business has continued to grow significantly, and total voice usage volume increased approximately 38.6% in 2006 compared to 2005.

***Value-added Business.*** Our value-added business includes voice value-added services, short message services, or SMS, and non-SMS data business.

Our voice value-added services mainly include caller identity display, caller restrictions, call waiting, call forwarding, call holding, voice mail, conference calls and others.

Our SMS mainly includes subscriber-to-subscriber messages, Monternet -based short messages and others.

Our non-SMS data business mainly includes Color Ring , wireless application protocol, or WAP, multimedia messaging service, or MMS, Java Applications services, instant messaging, or IM, Mobile Music, Mobile Mailbox, Mobile Blog, Mobile Paper, Mobile Search and Location-Based Services .

We believe that value-added business, in particular SMS and non-SMS data business, will continue to be one of the fastest growing segments of the telecommunications market in Mainland China over the next several years. In 2006, we increased the promotion of our value-added business by providing customers with diversified and personalized services. Revenue from our value-added business significantly increased to RMB69,309 million in 2006, an increase of 38.1% from 2005. As a percentage of operating

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revenue, revenue generated from value-added business increased from 20.6% in 2005 to 23.5% in 2006. As of December 31, 2006, the number of our value-added business users reached 270.4 million, which represented a 30.8% increase compared to 206.7 million users as of December 31, 2005. We continued to maintain a leading position in value-added business in Mainland China during 2006.

We plan to continue developing new applications and functions for SMS to further stimulate the growth of the SMS business. Focusing on businesses such as Color Ring and WAP, we intend to further strengthen business sales and promotion as well as product optimization to drive the growth in revenue. Regarding businesses such as MMS, IM and Mobile Paper, we plan to nurture customers' consumption habits and expand subscriber base, with a view to achieving the rapid growth of these businesses. At the same time, we expect to enhance the preparation for new products and new applications such as Mobile Search, Mobile Music, Mobile Mailbox, Mobile Blog and Location-Based Services. We also plan to focus on the promotion of industry-specific applications of value-added business to corporate customers to further enhance the penetration and utilization of value-added business. Large-scale promotional campaigns have been launched for key industry-specific application products such as Weather Information Service, Campus Information Service, Banking Information Service, Police Information Service and Municipal Information Service.

**SMS.** SMS refers to services which employ the existing resources of GSM networks and the corresponding functions of mobile telecommunications terminals to deliver and receive text messages, including subscriber-to-subscriber messages, Monternet-based short messages and others. SMS offers convenience and multi-functionality to our subscribers, and this business has grown rapidly in recent years. In particular, short message usage volume reached 353,384 million in 2006 from 249,609 million in 2005, and revenue generated from SMS business reached RMB32,201 million in 2006 compared to RMB24,671 million in 2005. Furthermore, the SMS penetration rate (SMS subscribers as a percentage of total subscribers) reached approximately 89.8% in 2006 compared to 83.8% in 2005.

**Color Ring.** Color Ring refers to the service where subscribers can customize the answer ring tone from a wide selection of songs, melodies, sound effects or voice recordings to replace the monotonous ring connecting tone that the caller would hear. We continued to experience significant growth in our Color Ring business in 2006. Revenue generated from our Color Ring business reached RMB6,751 million in 2006 compared to RMB3,423 million in 2005.

**WAP services.** WAP is a technology that allows users to access information instantly via handheld wireless devices such as mobile phones. Subscribers of our WAP services are able to access the Internet via the micro-browsers on their handheld wireless devices. We continued to experience significant growth in our WAP-based businesses in 2006. Revenue generated from WAP services reached RMB6,875 million in 2006 compared to RMB3,570 million in 2005.

**MMS.** MMS is a technology that allows users to exchange multimedia communications, such as graphics, animated color pictures, sound files and short text messages, over wireless networks. We experienced significant growth in our MMS businesses in 2006. Revenue generated from MMS business reached RMB984 million in 2006 compared to RMB364 million in 2005.

**Instant Messaging.** IM enables mobile services subscribers to communicate instantly through various means, including SMS, for chatting, dating or interactive entertainment. Our IM business provided by Fetion showed significant growth potential in 2006.

**Mobile Music.** Mobile Music refers to a service that provides music services to subscribers through mobile telecommunications networks. In 2006, we increased our efforts in business model innovation and strengthened our cooperation with the music media to stimulate and direct customers to try out, use and get accustomed to mobile music products based on Color Ring, IVR for Mobile Music and Ringtone Download. As a result, our Mobile Music business grew significantly in 2006.

**Mobile Paper.** Mobile Paper is a business we have developed in cooperation with mainstream media in Mainland China and elsewhere, which provides customers with updated information services (including contents such as news, sports, entertainment, cultural activities and lifestyle) through MMS, WAP and other types of service. We plan to continue to promote our Mobile Paper business.

Our value-added business also includes Mobile Mailbox, Mobile Blog and Mobile Search, which enable our subscribers to access the Internet through their wireless telephone handsets.

In addition, we provide wireless Internet access by utilizing general packet radio service, or GPRS, and wireless local area network, or WLAN, technologies to access WAP websites and Internet websites. GPRS supports a higher transmission rate than the traditional GSM cellular technology and enables network operators to provide more information and applications via a wireless connection. The usage of WAP-based services has grown significantly as the transmission speed and reliability has improved in





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recent years. WLAN is a wireless data transmission network which enables users to easily access local area networks via terminals with electromagnetic transmission, and is a complement to, and an extension of, wired local area networks access. We have been providing WLAN services at hot spots, such as airports, hotels, conference and exhibition centers and office buildings, within certain major cities in Mainland China.

### ***Tariffs***

The tariffs payable by our subscribers include primarily usage charges, monthly fees and service fees for voice value-added services and data services. Usage charges for both our contract and prepaid subscribers include base usage charges plus, where applicable, an additional component reflecting domestic and international long distance tariffs. When using roaming services, subscribers incur a roaming charge instead of the base usage charges, plus applicable domestic and international long distance charges.

We have flexible long distance tariff plans distinguishing between day time and night time, and offer tailored service plans based upon customer requirements as well as our network resources.

Our tariffs are subject to regulation by various government authorities, including the Ministry of Information Industry, the National Development and Reform Commission and the relevant price regulatory authorities in Mainland China. The actual price range in each service area is proposed by a network operator in that service area and must generally be approved by the relevant price regulatory authorities in that service area. In general, base usage charges, monthly fees, maximum domestic roaming charges and maximum applicable long distance tariffs (other than tariffs for Internet Protocol phone calls) are also determined by the Ministry of Information Industry in consultation with the National Development and Reform Commission. In August 2005, the Ministry of Information Industry amended its tariff regulations relating to some telecommunications services, pursuant to which network operators have more flexibility in setting their domestic and international long distance tariffs and domestic roaming charges, among others, provided that these tariffs set by network operators do not exceed the respective maximum tariffs determined by the Ministry of Information Industry in consultation with the National Development and Reform Commission and that the tariff plans are filed with the Ministry of Information Industry and the National Development and Reform Commission or, in some cases, the relevant price regulatory authorities at the provincial level.

In addition, the Ministry of Information Industry has been encouraging mobile telecommunications operators in Mainland China to implement the caller-party-pays regime. For example, officials from the Ministry of Information Industry and the National Development and Reform Commission indicated in April 2007 that the caller-party-pays regime will be phased in within approximately two years. As a result, mobile telecommunications operators, including us, have been gradually implementing the caller-party-pays regime. In particular, all of the new calling plan packages that we have been offering in the PRC since the beginning of 2007 are based on tariffs substantially equivalent to the caller-party-pays regime. We cannot predict with certainty, at this point in time, what effect the full implementation of the caller-party-pays regime may have on our business, financial condition and results of operations, although we expect decreases in tariff charges to generally result in usage volume increases.

We offer our subscribers a variety of tariff packages which have different monthly fees, levels of basic usage and charges for usage exceeding the covered basic usage, voice value-added services, data services or other features. In general, the higher the monthly fee of a tariff package, the greater the price concession we offer. The tariff packages often incorporate different complimentary voice value-added services and data services packages.

Given the rapid growth in mobile penetration rates and increased competition, in order to remain competitive in terms of price and performance with other mobile telecommunications operators, we provide certain discounts and promotional offers in and during corresponding service areas and call periods targeting different customers. These discounts and promotional offers mainly include rewards for the pre-payment of fees, free trials of voice value-added services or data services, tariff discounts during off-peak hours and in low-traffic areas, and tariff discounts for specified call recipients.

### ***Interconnection***

Interconnection refers to various arrangements that permit the connection of our networks to other networks such as the fixed-line networks. These agreements provide for the sharing and settlement of revenues from the base usage charges and, if applicable, roaming charges and domestic and international long distance charges.

Our networks interconnect with the networks of other operators, allowing our subscribers to communicate with the subscribers of these operators and to make and receive local, domestic and international long distance calls. Each of our operating subsidiaries has interconnection agreements with those operators in its service area. The economic terms of these agreements are standardized from province to province.



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### ***Roaming***

We provide roaming services to our subscribers, which allow them to access our mobile telecommunications services while they are physically outside of their registered service area or in the coverage areas of other mobile telecommunications networks in other countries and regions with which we have roaming arrangements.

As of December 31, 2006, our GSM global roaming services covered 219 countries and regions, while our GPRS global roaming services coverage was extended to 138 countries and regions.

A mobile telecommunications services subscriber using roaming services is charged at our per-minute roaming charge (instead of the base usage charge) for both incoming and outgoing calls, plus applicable long distance charges.

In recent years, our international and domestic roaming charges have generally declined, resulting in lower average revenue per minute from roaming services. However, the negative impact from declining roaming charges have been more than offset by the growth in voice volume usage, including usage growth driven by the decrease in roaming charges.

### ***Research and Development***

Our research and development efforts, undertaken jointly by our research institute and other relevant departments and business units, primarily focus on:

developing advanced business solutions and end-to-end data application solutions suitable for the consumer markets in Mainland China; and

monitoring technological trends, including advancement in the new generation of mobile telecommunications technologies, which may have an impact on the development of our current business and the implementation of our wireless data strategy.

We have applied for a number of patents in Mainland China. Moreover, we have submitted to international standardization organizations a number of contributions, many of which have been accepted. In light of the increasingly competitive and rapidly evolving telecommunications market in Mainland China, we expect to continue to devote resources to the research and development of new products, services and technology applications.

### ***Sales and Customer Services***

***Sales Channels.*** We offer our services through an extensive network of proprietary sales outlets and retail outlets. In addition to providing retail sales and network connection services, most of our proprietary sales outlets also offer differentiated services to subscribers under different service brands, including, for example, billing information and payment collection, services consultation, handset repair and other customer services. Furthermore, most of our proprietary sales outlets provide training and service demonstrations to retail outlets. The retail outlets offer our services according to agency agreements with us. In connection with these sales, all applicable fees payable after initial connection are paid to us. In addition, we offer certain online services to our customers, including, among others, subscription of voice value-added services, change of tariff plans, credit loading for Shenzhouxing pre-paid services and certain wireless data services, and redemption of GoTone points. Furthermore, we have enhanced our service capabilities in 2006 through the expansion and optimization of our proprietary sales channels, the expansion of online sales and marketing channels and the integration of the resources relating to sales and marketing channels in the community. The number of our proprietary sales outlets totaled approximately 34,000 in 2006. Moreover, we established sales and service networks at low cost by utilizing existing resources in rural areas to serve and expand our customer base in these areas.

We also establish concept stores in major cities within Mainland China to showcase our services and products, particularly our wireless data services, and to facilitate certain sales and marketing activities.

***Market Segmentation Strategy.*** As subscribers' demands for mobile telecommunications become more varied and complex, we have conducted research on market segmentation and have launched brands and products which cater to the specific needs of different subscriber groups. We mainly promote three brands, each with a different focus. GoTone targets high to middle-end subscribers, Shenzhouxing targets the mass market and the M-Zone brand targets the young user group through the integration of voice and data services.

Moreover, we provide differentiated applications and services to our corporate customers under customized service contracts. As of December 31, 2006, we had signed service contracts with approximately 1.39 million corporate customers, and individual customers served under these service contracts with corporate accounts accounted for approximately 26.4% of our total subscribers. With the expansion of our corporate customer base, we also seek to provide customized total solutions to these

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corporate customers in response to their particular requirements. Furthermore, we have developed customized products and service packages in response to the unique consumption characteristics of rural areas, such as Shenzhouxing Village-only Card, small denomination top-up, over-the-air recharging and the Agricultural Information Service. We have also encouraged handset producers to introduce inexpensive handsets with moderate functions to lower the barrier of using mobile phones in the rural areas.

**Customer Services.** Our customer support service centers offer 24-hour staff-answering and automatic-answering service hotlines in Mainland China, dealing with customer enquiries regarding services and billing, as well as handling customer complaints. In order to retain high-value and corporate customers and enhance customer satisfaction, we offer a series of personalized and differentiated services targeted at high-value and corporate customers, including dedicated account executives, on-site visits and systems for collecting comments and handling complaints.

In 2006, we upgraded our customer service hotlines and continued to optimize our customer service processes to remove service bottlenecks, resulting in sustained improvement in customer services and achieving a steady improvement in customer satisfaction levels. Overall customer satisfaction rate reached 79.6% in 2006.

**Customer Retention.** As a result of intensified competition, we place great emphasis on customer retention. Our strategy is to attract and retain high-value customers by providing high quality services. We have implemented a Customer Point Reward Program, which is a bonus point based scheme that rewards customers according to their service consumption, loyalty and payment history. This represents an important measure by us to retain high-value customers. Customers are identified and grouped as GoTone Diamond, GoTone Gold and GoTone Silver card members according to their respective value contribution and points accrued. Different levels of membership entitle members to different privileges. Customers in these classifications are eligible to receive targeted rewards, including some of our own products and services, as well as those of our business partners. In 2006, we further differentiated our GoTone service and enhanced customer loyalty of our GoTone service through the targeted allocation of marketing resources. In addition, we offer special services to our GoTone members, including cross-region services, airport VIP services, hospital VIP services, golf clubs and handset service clubs.

In developing our M-Zone brand, we focused on expanding the subscriber base, offering new services and gaining recognition as representative of youth culture. We enhanced the brand image and the number of customers as a result of our increased advertising efforts and expansion of new businesses, including the launch of brand alliances and the implementation of product and service upgrades.

In addition, we further enhanced customer loyalty through a series of efforts in 2006 including, among others, developing our portfolio of products, increasing services and industry penetration, allocating more resources in the fast-growing new businesses and optimizing management systems and procedures.

**Churn Management.** We have devised internal monitoring systems to detect subscribers who are prone to discontinue their subscriptions. In particular, our churn alert system prompts customer service representatives to proactively approach those subscribers, and customers who have recently discontinued their service, to improve customer relations and minimize churn.

**Credit Control.** We have implemented subscriber registration procedures, such as identity checks for individual customers and information checks for corporate customers, to assist in credit control. In certain situations, we require contract subscribers to pay an advance deposit representing a pre-determined amount of usage charges before certain telecommunications services are activated. The actual usage charges incurred are verified against the balance of the amount deposited at regular intervals on a daily basis, and if there are unusual circumstances, control measures will be implemented. Direct debit services are available in each geographical area. The accounts of contract subscribers are required to be settled on a monthly basis, and a late payment fee is imposed on each subscriber whose account balance is not settled by the monthly due date. If the subscriber's account remains overdue, the subscriber's services will be deactivated and such subscriber must pay all overdue amounts, including applicable late payment fees, to reactivate services. To further control credit risk, we have expanded the sphere of service offerings that require subscribers to pre-pay for services.

We make an allowance for doubtful accounts based on our assessment of the recoverability of accounts receivable on maturity. In particular, for any accounts receivable older than three months, we make an allowance for the full amount of such receivable. The total amount of our allowance for doubtful accounts in each of 2004, 2005 and 2006 was RMB2,273 million, RMB2,968 million and RMB3,852 million, respectively, or 1.2%, 1.2% and 1.3% of total operating revenue, respectively.

**Promotions Relating to the 2008 Beijing Olympics.** In 2006, as the only mobile telecommunications services partner for the 2008 Beijing Olympics, we actively participated in various promotional activities sponsored by the Beijing Olympic Games.



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Preparatory Committee to further enhance our brand. These include providing the mobile telecommunications transmission on a real time basis for the release of information relating to the 2008 Beijing Olympics via SMS, Color Ring and MMS.

**Corporate Social Responsibility.** We are committed to fulfilling our responsibility to the community. We have strived to build an informationalized society, help eliminate the perceived digital divide, care for the underprivileged and proactively support public welfare initiatives. We have also focused on energy conservation and environmental protection. We have established a corporate social responsibility management structure, with a designated department that reports directly to our Chairman being in charge of the planning and promotion of our corporate social responsibility initiatives. We also issued our first Corporate Responsibility Report in March 2007.

## ***Information Systems***

Our information systems primarily consist of a network management system, a business operation support system and a management information system. The network management system collects and processes the operating data from each network, and manages, supervises and controls our networks for safe and efficient operation. The business operation support system provides day-to-day operational support to each business unit, and is a unified and comprehensive system that enables the sharing of information resources. This system standardizes and integrates each of our sales, billing, settlement, customer service and network failure handling databases in a centralized and orderly manner. The management information system collects and processes our management information and provides support to our management personnel. In addition, this system has computerized and automated our management in finance, inventory, procurement and projects. Furthermore, we have an internal communications network, which consists of our office automation system, our internal computer network, video conference system, telephone system and others, the combination of which supports our internal communications. In 2006, we upgraded and expanded these systems to improve our management and operations.

**Trademark.** We market our services under the CHINA MOBILE trademark, which is the trademark we use throughout Mainland China. CHINA MOBILE is a registered trademark in Mainland China owned by our parent company, CMCC. In July 2002, we entered into a non-exclusive licensing agreement with CMCC for the use of the CHINA MOBILE name and logo by us and our operating subsidiaries. Under this agreement, no license fee is payable by us for the first five years from the effective date of the trademark registration in China and any fees payable after that will be no less favorable than fees paid by other affiliates of CMCC. In addition, each of the companies that we acquired in July 2004, other than Jingyi, has entered into a licensing agreement with CMCC for the use of the CHINA MOBILE name and logo. Under these agreements, no license fee is payable until December 31, 2007.

In addition, the CHINA MOBILE name has been registered as a trademark by CMCC in Australia, Canada, Hong Kong, Macau, Taiwan, Brunei, Cambodia, Indonesia, New Zealand, South Korea, Thailand, Switzerland and the United States. Furthermore, CMCC has filed applications to register the CHINA MOBILE name and logo as a trademark in Bangladesh, India, Malaysia and Philippines. CMCC has also filed applications for trademark registration under the Protocol Relating to the Madrid Agreement Concerning the International Registration of Marks.

## ***Mobile Telecommunications Networks***

We offer mobile telecommunications services using the GSM standard. Each of our GSM networks consists of:

base stations, which are transmitters and receivers that serve as a bridge between all mobile users in a cell and connect mobile calls to the mobile switching center;

base station controllers, which connect to, and monitor and control, the base station within each cell, performing the functions of message exchange and frequency administration;

mobile switching centers, which are central switching points to which each call is connected, and which control the base station controllers and the routing of calls;



transmission lines, which link the mobile switching centers, base station controllers, base stations and other telecommunications networks; and

software applications that drive the mobile telecommunications infrastructure.

***GSM Network Capacity Expansion and Optimization Plans.*** All of our subscribers currently use digital GSM services. We intend to continue our network expansion and optimization with an emphasis on improving network utilization and operating efficiency as well as expanding the coverage and capacity of our GSM networks. Our network expansion and optimization plans depend to a large extent upon the availability of sufficient spectrum.

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***Spectrum.*** A mobile telecommunications network's capacity is to a certain extent limited by the amount of frequency spectrum available. The Ministry of Information Industry allocated a total of 44 MHz of spectrum, used for transmission and reception nationwide, respectively, in the 900 MHz frequency band and the 1800 MHz frequency band to our parent company, CMCC. Under the existing agreement between CMCC and us, we have the exclusive right to use such frequency spectrum in Mainland China.

***Transmission Infrastructure.*** The physical infrastructure linking our base stations, base station controllers and mobile switching centers and interconnecting our networks to other networks consists of transmissions lines, which provide the backbone infrastructure by which mobile call traffic is carried.

***Intra-Provincial Transmission Lines.*** In addition to our own transmission lines, we also lease intra-provincial and local transmission lines from other operators and pay them fees based on tariff schedules stipulated by the relevant regulatory authorities after adjusting for the discounts that we have negotiated.

***Inter-Provincial Transmission Lines.*** Following the completion of our acquisition of the ten regional mobile telecommunications companies and other telecommunications assets in July 2004, we no longer lease any inter-provincial transmission lines from CMCC, and for the inter-provincial transmission lines we leased from other providers through CMCC, CMCC collects leasing fees from us and pays the same to the relevant transmission line providers.

***Network Operations and Maintenance.*** We believe that we have considerable network operation and maintenance experience and technical expertise. Day-to-day traffic management, troubleshooting, system maintenance and network optimization are conducted by our experienced team of engineers and technicians. Technical staffs are available for emergency repair work 24 hours a day and we employ specialist teams for central maintenance of the networks. Currently, most technical difficulties relating to the networks are resolved by our staff, although our equipment suppliers also provide back-up maintenance and technical support.

***Base Station Sites.*** In urban areas, our base station sites are located mostly on existing structures, typically at the top of tall buildings. In rural areas, masts are often constructed for locating base stations. Typically, base station sites are of limited size, as base station equipment does not generally require significant space. As of the end of 2006, we had approximately 234,000 base stations. Generally, depending on the length of time required for negotiation with respect to use of the land or buildings, construction of a base station takes approximately one to three months in an urban area and approximately three to six months in a rural area. We anticipate that we will need a significant number of new sites in connection with the expansion of our mobile telecommunications networks. There can be no assurance that we will be able to obtain the requisite number of sites on reasonable commercial terms.

***Equipment Suppliers.*** We select our principal suppliers from among leading international and domestic manufacturers of mobile telecommunications equipment and in accordance with technical standards set by the Ministry of Information Industry. In 2006, we purchased our GSM networks equipment primarily from Huawei Technologies, Ericsson, Nokia, Motorola and Alcatel-Lucent. In addition, in light of the development of 3G-based technologies, most of our newly-purchased GSM networks equipment is also compatible with 3G-based technologies.

### ***Strategic Alliance with Vodafone***

We have a strategic alliance agreement with Vodafone, which provides for a number of cooperation arrangements between us and Vodafone, including:

the exchange and sharing of corporate management, technical and operational expertise and resources;

joint research and development;

the introduction of global products and services for the mobile community; and

the development and implementation of standards and protocols relevant to mobile telecommunications.

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Under the agreement, Vodafone is our preferred partner in the above mentioned areas, and we are Vodafone's sole strategic partner in China for all areas of potential cooperation within the scope of the strategic alliance. As part of the alliance, Dr. J. Brian Clark, Chief Executive in the Asia Pacific Region of Vodafone, served as a Non-Executive Director of our company from August 2003 until March 2005. Sir Julian Michael Horn-Smith, Deputy Chief Executive Officer and Executive Director of Vodafone, served as a Non-Executive Director of our company from March 2005 until June 2006. Mr. Paul Michael Donovan, Chief Executive Officer for Central Europe, Middle East, Asia-Pacific and Affiliates of Vodafone, joined our board of directors as a Non-Executive Director in June 2006. See Item 6. Directors, Senior Management and Employees. In addition, as of May 31, 2007, Vodafone held approximately 3.21% of our outstanding shares. See The History and Development of Company Expansion Through Acquisitions.

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We believe that the strategic alliance with Vodafone has enhanced our strengths in the telecommunications market in Mainland China and will better position us to pursue further expansion opportunities globally. In particular, this alliance has enabled us to have frequent and broad exchanges of expertise and market information. Moreover, this strategic alliance will enable Vodafone and us to share information and establish benchmarks to better assess and enhance each other's performance, thereby better positioning both parties in the global telecommunications market.

### ***Strategic Alliance Agreement with Phoenix and Memorandum of Understanding with News Corporation and STAR Group Limited***

On June 8, 2006 we entered into a strategic alliance agreement with Phoenix Satellite Television Holdings Limited, or Phoenix, a leading satellite television operator broadcasting into Mainland China, pursuant to which we and Phoenix will cooperate in the joint development, marketing and delivery of innovative wireless content, products, services and applications, among others. The strategic alliance agreement became unconditional on August 25, 2006, and we currently have a number of cooperative initiatives underway with Phoenix.

In addition, on June 8, 2006, we entered into a memorandum of understanding with News Corporation and STAR Group Limited in connection with the intention of the parties to build a long-term wireless media strategic partnership and to explore various areas of cooperation, which may include the aggregation, development and marketing of multimedia content and other wireless value-added services, by combining the strength and experience of one of the largest media companies in the world and one of the largest mobile telecommunications companies in the world. We are currently working with News Corporation and STAR Group Limited on a number of cooperative initiatives.

### ***Competition***

We compete with other telecommunications services providers. We are one of the two licensed mobile telecommunications services providers in Mainland China. The PRC government encourages orderly and fair competition in the telecommunications industry in Mainland China. In particular, the PRC government has extended favorable regulatory policies to some of our competitors, such as China Unicom, in order to help them become more viable competitors to us. For example, the PRC government has permitted China Unicom to apply mobile service tariffs as much as 10% below the governmental standard rates. We believe this policy has helped China Unicom's market share by capturing a significant number of price-sensitive mobile telecommunications services subscribers.

In accordance with the PRC government policy of encouraging competition in the PRC telecommunications industry, the government has previously authorized new entrants to offer IP-based long distance call services, data and Internet services. In 2001, the State Council formally approved the restructuring of the former China Telecommunications Corporation, China Netcom Corporation Limited and Jitong Network Communications Company Limited, which created two large telecommunications companies, China Telecom and China Netcom. Increased competition from new entrants in China's telecommunications industry could adversely affect our financial condition and results of operations. See Item 3. Key Information Risk Factors New entrants in and further restructuring of the telecommunications industry in Mainland China may further intensify competition and materially and adversely affect our business and prospects.

We are facing intensified competition from other operators. China Unicom provides mobile telecommunications services through GSM and CDMA networks throughout Mainland China. In addition, China Telecom and China Netcom offer local wireless access services, such as Xiaolingtong services, throughout Mainland China. Xiaolingtong services are local telecommunications services based on the Personal Access System technology, which provide subscribers with wireless access in a low-mobility environment through radio base stations with short-distance coverage. In addition, China Unicom, China Telecom and China Netcom launch from time to time promotional offers, such as handset subsidies and tariff packages, to attract customers. China Telecom and China Netcom also offer Xiaolingtong services together with fixed-line services as a package. Despite intensified competition, we believe that we have significant competitive advantages due to:

economies of scale;

our superior mobile telecommunications networks;

our advanced and flexible support systems;

our widely-recognized brand name and logo that are closely identified with us by consumers;

our broad distribution networks and our focus on customer services;

our extensive range of value-added business;

our experienced management team and seasoned employees; and

our financial resources.

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We believe these advantages have contributed to our superior subscriber quality compared to that of our competitors, as measured by average usage levels, average revenues per subscriber and doubtful accounts levels.

The State Council and the Ministry of Information Industry may approve additional mobile service providers in the future that may compete with us. We may also be subject to competition from providers of new telecommunications services based on existing or new technologies, such as 3G. Nonetheless, given the relatively low mobile penetration rates in the central and western regions as well as small and medium-sized cities and rural areas, we believe there is substantial growth potential for our mobile telecommunications business. We believe that the restructuring of the telecommunications industry in Mainland China has helped to create a fair, orderly, transparent and healthy telecommunications market.

### World Trade Organization

China officially joined the WTO on December 11, 2001. Under the Protocol on the Accession of the People's Republic of China, dated as of November 11, 2001, China agreed to gradually open various segments and regions of its telecommunications market to foreign investment. Pursuant to this accession protocol, both the percentage of ownership of Sino-foreign joint ventures offering telecommunications services in China and the regions where those joint ventures are permitted to offer telecommunications services have been gradually expanded over a period of six years. Under the accession protocol, the telecommunication market is divided into fixed-line services, mobile voice and data services, paging services and value-added services. Value-added services include electronic mail, voice mail and online information and database retrieval. By December 11, 2004, foreign investors were permitted to own up to 49% of joint ventures that offer mobile voice and data services in 17 cities in China. By December 11, 2006, such joint ventures were permitted to offer mobile voice and data services in China without any geographic restrictions.

The table below summarizes the foreign ownership restrictions for telecommunications joint ventures in China as well as applicable geographic restrictions:

### Foreign Ownership Percentage and Geographic Restrictions for Foreign-Funded Telecommunications Enterprises

| Sector      | As of December 31,               |                                   |                     |                                   |      |                                   |                     |
|-------------|----------------------------------|-----------------------------------|---------------------|-----------------------------------|------|-----------------------------------|---------------------|
|             | 2001                             | 2002                              | 2003                | 2004                              | 2005 | 2006                              | 2007                |
| Mobile      | 25%<br>(3 cities) <sup>(1)</sup> | 35%<br>(17 cities) <sup>(2)</sup> |                     | 49%<br>(17 cities) <sup>(2)</sup> |      | 49%<br>(nationwide)               |                     |
| Fixed-line  | N/A                              | N/A                               | N/A                 | 25%<br>(3 cities) <sup>(1)</sup>  |      | 35%<br>(17 cities) <sup>(2)</sup> | 49%<br>(nationwide) |
| Value-added | 30%<br>(3 cities) <sup>(1)</sup> | 49%<br>(17 cities) <sup>(2)</sup> | 50%<br>(nationwide) |                                   |      |                                   |                     |
| Paging      | 30%<br>(3 cities) <sup>(1)</sup> | 49%<br>(17 cities) <sup>(2)</sup> | 50%<br>(nationwide) |                                   |      |                                   |                     |

Source: the official website of the PRC Ministry of Information Industry.

(1) The initial three cities are Beijing, Shanghai and Guangzhou.

(2) The 17 cities include Beijing, Chengdu, Chongqing, Dalian, Fuzhou, Guangzhou, Hangzhou, Nanjing, Ningbo, Qingdao, Shenyang, Shanghai, Shenzhen, Xiamen, Xi'an, Taiyuan and Wuhan.

### Regulation

The mobile telecommunications industry in Mainland China is highly regulated. Regulations issued or implemented by the State Council, the Ministry of Information Industry and other relevant government authorities including the National Development and Reform Commission and the Ministry of Commerce, which consolidated the functions of the former Ministry of Foreign Trade and Economic Cooperation, encompass all key aspects of mobile telecommunications network operations, including entry into the telecommunications industry, scope of permissible business, interconnection and transmission line arrangements, technology and equipment standards, tariff standards, capital investment priorities,

foreign investment policies and spectrum and numbering resources allocation.

The Ministry of Information Industry, under the leadership of the State Council, is responsible for, among other things:

formulating and enforcing industry policy, standards and regulations;

granting telecommunications licenses and permits;

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formulating interconnection and settlement standards for implementation between telecommunications networks;

together with other relevant regulatory authorities, formulating tariff and service charge standards for telecommunications services;

supervising the operations of telecommunications services providers;

promoting fair and orderly market competition among operators; and

allocating and administering public telecommunications resources, such as radio frequencies, numbering resources, domain names and addresses of telecommunications networks.

In order to provide a uniform regulatory framework to encourage the orderly development of the telecommunications industry, the Ministry of Information Industry, under the direction of the State Council, has been preparing a draft telecommunications law. According to the 2007 legislation agenda of the National People's Congress, the draft telecommunications law has not yet been scheduled for review or adoption, although it is reportedly one of nine draft legislations reserved for potential review. We expect that, if and when the telecommunications law is adopted by the National People's Congress, it will become the basic telecommunications statute and the legal source of telecommunications regulations in Mainland China. In addition, the State Council promulgated a set of telecommunications regulations on September 25, 2000. These regulations apply in the interim period prior to the adoption of the telecommunications law. Although we expect that the telecommunications law will have a positive effect on the overall development of the telecommunications industry in Mainland China, we cannot predict what the ultimate nature and scope of the telecommunications law will be.

**Entry into the Industry.** Under the current regulations, operators of mobile telecommunications networks, providers of other basic telecommunications services such as local and long distance fixed-line telephone services, and value-added service providers whose telecommunications services cover two or more provinces, directly-administered municipalities or autonomous regions in China must apply for specific permits from the Ministry of Information Industry in order to provide such services. Granting of permits for providing basic telecommunications services will be through a tendering process. Currently, in addition to us, China Unicom is also authorized to provide mobile telecommunications services in all provinces, directly-administered municipalities and autonomous regions in China.

On December 11, 2001, China officially joined the WTO. To implement China's commitments under the WTO, the Administration of Foreign-Funded Telecommunications Enterprises Provisions became effective on January 1, 2002, permitting foreign investment in joint ventures that provide telecommunications services in China. However, such investments will presumably bear no direct relation to the issuance of licenses to providers of telecommunications services in Mainland China, as the issuance of new licenses by the relevant authority is governed by a separate set of rules and regulations. Pursuant to the Administration of Foreign-Funded Telecommunications Enterprises Provisions, foreign ownership in a telecommunications enterprise may be gradually increased to 49% if such enterprise provides basic telecommunications services and 50% if such enterprise provides value-added telecommunications services (including radio paging services).

**Spectrum Usage.** In coordination with the relevant provincial authorities, the Ministry of Information Industry regulates the allocation of radio frequency. The frequency assigned to an entity is not allowed to be leased or, without approval of the Ministry of Information Industry, transferred by the entity to any other third party. In accordance with a joint circular from the National Development and Reform Commission and the Ministry of Finance, CMCC entered into an agreement with us that specifies the amount of fees to be paid to the Ministry of Information Industry for spectrum usage by each mobile telecommunications network operator based on the bandwidth of the frequency used and the number of base stations within the relevant operator's networks.

On May 2, 2002, the relevant regulatory authorities in China informed us that the standard spectrum usage fees for GSM networks would be adjusted progressively over a period of three years, and that the adjustments would be effective for a period of five years from July 1, 2002. For the first year, spectrum usage fees for GSM networks would be charged at the annual rate of RMB7.5 million per MHz frequency. For the second year, the annual fee would be RMB11.25 million per MHz frequency and from the third year onward, the annual fee would be RMB15 million per MHz frequency. All adjusted annual fees are charged on the basis that upward and downward frequencies are separately charged. The relevant regulatory authorities in China may review these fee arrangements in the future. However, we expect that we will be able to continue to use our currently allocated spectrum.



**Numbering Resources.** The Ministry of Information Industry is responsible for the administration of the telecommunications numbering resources within Mainland China, including the telecommunications network numbers and subscriber numbers. The use of numbering resources by any telecommunications operator is subject to the approval by the Ministry of

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Information Industry. In January 2003, the Ministry of Information Industry issued Measures on Administration of Telecommunications Network Numbering Resources. In accordance with these measures, the telecommunications network numbering resources are owned by the state, and the user of numbering resources is required to pay a usage fee to the state starting March 1, 2003. The measures also provide for procedures for application for the use, upgrade and adjustment of numbering resources by telecommunications operators. In December 2004, the Ministry of Information Industry, the Ministry of Finance and the National Development and Reform Commission jointly issued the Provisional Administrative Measures with respect to the Collection of the Usage Fee of Telecommunications Network Numbering Resources, under which telecommunications companies are required to pay a usage fee to the PRC government by the 10th day of the first month of each quarter. Moreover, under these provisional measures, mobile telecommunications companies are required to pay an annual usage fee of RMB12 million for each network number.

***Tariff Setting.*** The levels and categories of our tariffs are subject to regulation by various government authorities, including the Ministry of Information Industry, the National Development and Reform Commission and, at the local level, the relevant provincial price regulatory authorities. Under the current telecommunications regulations, telecommunications tariffs are categorized into market based tariffs, government guidance tariffs and government standard tariffs. In general, base usage charges, monthly fees, maximum domestic roaming charges and maximum tariffs for all domestic long distance calls and international calls (other than Internet Protocol phone calls) are fixed jointly by the Ministry of Information Industry and the National Development and Reform Commission. In August 2005, the Ministry of Information Industry amended its tariff regulations relating to some telecommunications services, pursuant to which network operators have, among other things, more flexibility in setting their domestic and international long distance tariffs and domestic roaming charges, provided that these tariffs set by network operators do not exceed the respective maximum tariffs determined by the Ministry of Information Industry in consultation with the National Development and Reform Commission and that the tariff plans are filed with the Ministry of Information Industry and the National Development and Reform Commission or, in some cases, the relevant price regulatory authorities at the provincial level. Furthermore, officials from the Ministry of Information Industry and the National Development and Reform Commission indicated in April 2007 that these two regulatory authorities intend to further reduce the maximum domestic roaming charges and allow network operators more flexibility in lowering their domestic roaming charges. Our international roaming charges are set in accordance with agreements between CMCC and the relevant foreign mobile operators. Under the current telecommunications regulations, tariffs for those telecommunications businesses that are considered fully competitive may be set by the service providers as market based tariffs.

The Ministry of Information Industry has also been encouraging mobile telecommunications operators in Mainland China to implement the caller-party-pays regime. Officials from the Ministry of Information Industry and the National Development and Reform Commission indicated in April 2007 that the caller-party-pays regime will be phased in within approximately two years.

***Interconnection Arrangements and Lease Line Arrangements.*** Under the current telecommunications regulations, parties seeking interconnection must enter into an interconnection agreement and file such interconnection agreement with the Ministry of Information Industry. Major telecommunications services providers that have control over essential telecommunications infrastructure and possess significant market share must allow interconnection to their networks by other operators. They must establish interconnection rules and procedures based on the principles of non-discrimination and transparency and submit such rules and procedures to the Ministry of Information Industry for approval. Such rules and procedures will be binding upon those major telecommunications services providers. The termination of any interconnection arrangements will require prior approval by the Ministry of Information Industry.

The applicable regulations provide that interconnection related equipment must conform to the technical standards approved by the Ministry of Information Industry. See **Technical Standards** below. The Ministry of Information Industry also determines the standard lease tariffs to be paid by telecommunications operators with respect to the leasing of transmission lines that facilitate interconnection between telecommunications networks.

***Technical Standards.*** Certain regulatory authorities in Mainland China, including the Ministry of Information Industry, set technical standards and control the type and quality of mobile telecommunications equipment used in or connected to public networks, all radio telecommunications equipment and all interconnection related equipment.

The establishment of base stations requires the approval of the relevant provincial regulatory authorities. We have not experienced and do not expect to experience material difficulty in obtaining permission to establish additional sites.

***Capital Investment.*** Some of our major investment projects, including mobile telecommunications network development projects, may be required to obtain approvals from relevant regulatory authorities in Mainland China.

**Table of Contents*****Employees***

As of December 31, 2004, 2005 and 2006, we had 88,127, 99,104 and 111,998 employees, respectively. Substantially all of our employees are located in Mainland China. The employees as of December 31, 2006 are classified in the following table. Approximately 75.8% of our permanent employees have college or graduate degrees.

|                           |                |
|---------------------------|----------------|
| Management                | 20,272         |
| Technical and engineering | 32,031         |
| Sales and marketing       | 53,087         |
| Financial and accounting  | 6,608          |
| <b>Total</b>              | <b>111,998</b> |

We provide benefits to certain employees, including housing, retirement benefits and hospital, maternity, disability and dependent medical care benefits. Most of our employees are members of a labor association. We have not experienced any strikes, slowdowns or labor disputes that have interfered with our operations to date, and we believe that our relations with our employees are good.

**Properties, Plants and Equipment**

We own, lease or have usage rights in various properties which consist of land and buildings for offices, administrative centers, staff quarters, retail outlets and technical facilities. For some of our properties under construction, we have not obtained land use right certificates or property title certificates. However, such deficiencies do not affect our use of these properties. We believe that all of our owned and leased properties are well maintained and are suitable and adequate for their present use.

**Item 4A. Unresolved Staff Comments.**

None.

**Item 5. Operating and Financial Review and Prospects.**

You should read the following discussion and analysis in conjunction with our consolidated financial statements, together with the related notes, included elsewhere in this annual report on Form 20-F. Our consolidated financial statements have been prepared in accordance with Hong Kong GAAP, which differ in certain significant respects from U.S. GAAP. Note 40 to our consolidated financial statements summarizes the significant differences between Hong Kong GAAP and U.S. GAAP as they relate to us and provides a reconciliation to U.S. GAAP of profit attributable to equity shareholders and shareholders' equity. In addition, note 40 to our consolidated financial statements includes our condensed consolidated financial statements prepared and presented in accordance with U.S. GAAP for the relevant periods. Our consolidated financial statements present, and the discussion and analysis in this section pertain to, our consolidated financial position and results of operations as of and for the years ended December 31, 2004, 2005 and 2006. Our consolidated financial statements reflect the results of Neimenggu Mobile, Jilin Mobile, Heilongjiang Mobile, Guizhou Mobile, Yunnan Mobile, Xizang Mobile, Gansu Mobile, Qinghai Mobile, Ningxia Mobile, Xinjiang Mobile, Jingyi and CMC from July 1, 2004, the date of the acquisition. Our consolidated financial statements reflect the results of Peoples from January 5, 2006.

**Overview of Our Operations**

During 2004, 2005 and 2006, our network capacity, subscriber base and usage and operations continued to experience significant growth. We believe that with the ongoing market-oriented restructuring of the telecommunications industry, as well as the continued development of the Chinese economy and increase in per capita income in Mainland China, the telecommunications industry will continue to grow rapidly. Given the relatively low penetration rates in Mainland China in general and, in particular, in the central and western regions, we believe that there is substantial potential for continued future subscriber growth.

We operate in an extensively regulated environment and our operations and financial performance are significantly affected by the PRC government's regulation of the telecommunications industry. These regulations and policies may affect, among other things, our interconnection and transmission line leasing arrangements, technology and equipment standards and capital investment, as described in more detail under "Item

3. Key Information   Risk Factors   Adverse changes in the economic policies

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of the PRC government could have a material adverse effect on the overall economic growth of Mainland China, which could reduce the demand for our services and have a material adverse effect on our business, financial condition and results of operations and Item 4. Information on the Company Business Overview Regulation . Our financial performance is also subject to the economic and social conditions in Mainland China and foreign currency exchange rate fluctuations.

On March 16, 2007, the PRC Enterprise Income Tax Law was enacted, and will become effective on January 1, 2008. The PRC Enterprise Income Tax Law adopts a uniform tax rate of 25% for all enterprises (including foreign-invested enterprises). The exact impact of this new law on our financial condition and results of operations will depend on detailed pronouncements that are to be subsequently issued, including implementation rules on transitional policy of preferential tax treatments granted under the current tax law and administrative regulations, and consequently we cannot reasonably estimate the financial impact of the new law on us at this stage. However, we expect this new law to have an overall positive impact on our financial condition and results of operations.

### ***Our Previous Acquisitions of Regional Mobile Telecommunications Companies and Other Telecommunications Assets in Mainland China and Hong Kong Have Materially Impacted Our Financial Results***

Following our acquisition of Neimenggu Mobile, Jilin Mobile, Heilongjiang Mobile, Guizhou Mobile, Yunnan Mobile, Xizang Mobile, Gansu Mobile, Qinghai Mobile, Ningxia Mobile, Xinjiang Mobile, Jingyi and CMC on July 1, 2004, we began to provide a full range of mobile telecommunications services in all thirty-one provinces, autonomous regions and directly-administered municipalities in Mainland China. Moreover, we acquired all of the issued and outstanding shares of Peoples in 2006. See Item 4. Information on the Company The History and Development of Company Expansion Through Acquisitions. We have adopted the purchase accounting method to account for these acquisitions under Hong Kong GAAP. Accordingly, our consolidated financial statements include the results of these companies from the respective dates of the acquisitions. Under U.S. GAAP, except for our acquisition of Peoples, our acquisitions of these other companies are considered a combination of entities under common control which would be accounted for in a manner similar to a pooling-of-interests. Consequently, the assets and liabilities are transferred at their historical amounts and our consolidated financial statements are adjusted retrospectively to include the financial statements of these previously separate companies for all periods presented.

These acquisitions have had a material impact on our overall results of operations. In particular, our financial results in 2004 were significantly affected by the inclusion of the results of operations for the ten regional mobile telecommunications companies and other telecommunications assets we acquired in July 2004, and our financial results in 2006 also included the results of operations for Peoples we acquired in 2006. These acquisitions have, among other things, significantly expanded the size of the mobile telecommunications markets we serve and increased the number of our subscribers and usage of our services. As a result, our operating revenue and operating expenses have also increased significantly.

### ***Operating Arrangements We Entered Into Over the Last Several Years Have Materially Impacted Our Financial Results***

Our current organizational structure was established pursuant to the restructuring completed in September 1997 in preparation for our initial public offering and our subsequent acquisitions of regional mobile telecommunications companies and other telecommunications assets in Mainland China and Hong Kong. In connection with these transactions, we entered into various operating arrangements to facilitate the transfer of the operations to us, to integrate these operations within our operating structure and to improve our overall operational efficiency. These arrangements included:

interconnection revenue sharing and settlement arrangements with other operators;

intra-provincial transmission line leasing agreements with other operators;

service agreement with CMCC and certain other operators with respect to various telecommunications services and support;

a change in the tax treatment of connection fees and certain surcharge revenue for our services; and

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the revaluation of property, plant and equipment and land lease prepayments of the companies we acquired as of the respective dates set forth in the financial statements included in this annual report on Form 20-F.

The original terms of our agreements relating to interconnection, leased lines and roaming have been revised as a result of tariff adjustments by the government and/or commercial negotiation with the relevant parties.

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Our financial results reflect the impact of the above arrangements as of the dates they became effective. These arrangements and changes have had a material impact on our overall results of operations.

### ***Our Operating Arrangements with CMCC Have Affected and May Continue to Affect Our Financial Results***

Following the completion of our acquisition of the telecommunications assets from CMCC in July 2004, CMCC no longer provides mobile telecommunications services in Mainland China other than through us. Therefore, from July 1, 2004, the domestic roaming arrangements between CMCC and us were terminated and we no longer lease any inter-provincial transmission lines from CMCC. Moreover, we entered into an agreement with CMCC on July 1, 2004 with respect to, among other things, inter-provincial interconnection and roaming, international interconnection and roaming, and inter-provincial and international transmission lines leasing. Pursuant to this agreement, for the inter-provincial transmission lines we leased from other providers through CMCC, CMCC maintains the existing inter-provincial transmission line leasing arrangements with the relevant transmission line providers, and collects leasing fees from us and pays the same to the relevant transmission line providers. Moreover, under this agreement, CMCC: (i) maintains the existing settlement arrangements with respect to international interconnection and roaming with the relevant telecommunications services providers in foreign countries and regions; and (ii) collects the relevant usage fees and other fees from us or the relevant telecommunications services providers in foreign countries and regions and pays the same to the relevant mobile telecommunications services providers in foreign countries and regions or us, as the case may be. In addition, under this agreement, with respect to the inter-provincial interconnection with the relevant telecommunications services providers in Mainland China, CMCC maintains the existing inter-provincial interconnection arrangements with the relevant telecommunications services providers in Mainland China, and collects the relevant usage fees and other fees from us and pays the same to the relevant telecommunications services providers in Mainland China.

### ***Tariff Adjustments***

The PRC government has introduced a wide range of tariff adjustments since 2001, which include, among other things, the shortening of the billing unit for long distance charges (other than for IP-based long distance call services), from one minute to six seconds, the general reduction in domestic and international long distance call rates, the elimination of various surcharges, and connection fees charged to new contract subscribers and, a general reduction in leased line tariffs. Moreover, we are allowed to offer our subscribers a variety of tariff packages which have different monthly fees, levels of basic usage and charges for usage exceeding the covered basic usage, voice value-added services, data services or other features. In general, the higher the monthly fee of a tariff package, the greater the price concession we offer. The tariff packages often incorporate different complimentary voice value-added services and data services packages.

In addition, our international and domestic roaming charges have generally declined in recent years. Officials from the Ministry of Information Industry and the National Development and Reform Commission also indicated in April 2007 that these two regulatory authorities intend to further reduce the maximum domestic roaming charges and allow network operators more flexibility in lowering their domestic roaming charges. Moreover, encouraged by the Ministry of Information Industry, mobile telecommunications operators in Mainland China have been gradually implementing a caller-party-pays regime. Officials from the Ministry of Information Industry and the National Development and Reform Commission indicated in April 2007 that the caller-party-pays regime will be phased in within approximately two years.

Our average revenue per minute has reflected a downward trend in recent years. However, such decline stimulated a strong price elasticity, which in turn led to a strong growth in our voice usage volume that generally more than offset the adverse effect of the lower average revenue per minute on our overall revenue.

### ***Renminbi Bond Offerings***

Following the approval by the relevant PRC regulatory authorities, on June 18, 2001 our wholly-owned subsidiary, Guangdong Mobile, issued RMB5,000 million of guaranteed bonds due in 2011 at a floating interest rate, payable annually. These bonds are listed on the Shanghai Stock Exchange.

We have issued an irrevocable guarantee for the performance of these bonds, and CMCC has issued a further guarantee in relation to the performance by us of our guarantee. The bonds are rated AAA by China Chengxin International Credit Rating Company Limited, an affiliate of Fitch International Limited.

The net proceeds from the offering were applied solely to repay part of the RMB12,500 million syndicated loans we raised through our wholly-owned subsidiary, China Mobile (Shenzhen) Limited, in 2000 for our acquisition of the seven regional mobile telecommunications companies.





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Following the approval by the relevant PRC regulatory authorities, Guangdong Mobile issued RMB3,000 million guaranteed bonds due 2007 and RMB5,000 million guaranteed bonds due 2017 on October 28, 2002. These bonds commenced trading on the Shanghai Stock Exchange on January 22, 2003. The RMB3,000 million guaranteed bonds and RMB5,000 million guaranteed bonds bear fixed interest of 3.5% and 4.5%, respectively, payable annually.

We have issued a joint and irrevocable guarantee for the performance of these bonds, and CMCC has issued a further guarantee in relation to the performance by us of our guarantee obligation. These bonds received a consolidated credit rating of AAA by China Chengxin International Credit Rating Company Limited, an affiliate of Fitch International Limited, and a consolidated credit rating of AAA by Dagong Global Credit Rating Co. Ltd.

The entire net proceeds from the offering were applied solely to satisfy part of the US\$2,800 million deferred consideration for the acquisition by the Company of the entire interest in Anhui Mobile, Jiangxi Mobile, Chongqing Mobile, Sichuan Mobile, Hubei Mobile, Hunan Mobile, Shaanxi Mobile and Shanxi Mobile in 2002.

## **Critical Accounting Policies and Estimates**

The following discussion and analysis is based on our consolidated financial statements, which have been prepared in accordance with Hong Kong GAAP. The preparation of financial statements in conformity with Hong Kong GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and revenues and expenses during the years reported. Actual results could differ from those estimates. Estimates are used when accounting for certain items such as provision for customer point reward program, allowance for doubtful accounts, depreciation and amortization period, amortization of other intangible assets, impairment of long lived assets including property, plant and equipment, goodwill and other intangible assets arising from acquisitions (including that taken initially to reserves) and fair value of share options granted. Actual results may differ from those estimates under different assumptions or conditions.

We believe that the following critical accounting policies have a more significant impact on our consolidated financial statements, either because of the significance of the financial statement elements to which they relate, or because they require judgment and estimation.

### ***Provision for Customer Point Reward Program***

We invite our subscribers to participate in a customer point reward program, or the Reward Program, which provides subscribers the option of electing to receive free telecommunications services or other non-cash gifts. The level of bonus points earned under the Reward Program varies depending on the subscribers' service consumption, loyalty and payment history. The estimated incremental costs of providing these free rewards are expensed in the consolidated statements of income and are accrued as a current liability on the consolidated balance sheets based on: (i) the number of subscribers who are qualified to exercise their redemption right at period/year end and the estimated rate of redemptions based on past experience; (ii) the estimated number of subscribers who have no right to redeem the incentives at period/year end, but who will ultimately earn and claim awards under the Reward Program; and (iii) type of incentives that subscribers will select for redemption based on past experience. As subscribers redeem rewards or their entitlements expire, the provision is reduced accordingly.

### ***Allowance for Doubtful Accounts***

We maintain allowances for doubtful accounts based upon evaluation of the recoverability of the accounts receivable and other receivables at each balance sheet date. We base our estimates on the ageing of our accounts receivable and other receivable balances and our historical write-off experience, net of recoveries. If the financial condition of our customers were to deteriorate, additional allowances may be required.

### ***Depreciation***

Depreciation is based on the estimated useful lives of items of property, plant and equipment, less their estimated residual value, if any, to write off the cost of these items over their estimated useful lives. We review the estimated useful lives and residual values of our assets annually in accordance with Hong Kong GAAP. The useful lives and residual values of each class of our telecommunications assets are reviewed periodically and, if there has been a significant change in the expected pattern of consumption of the future economic benefits embodied in the asset, the method is changed to reflect the changed pattern. The depreciation expense for future period is adjusted if there are significant changes from previous estimates. We determine the useful life of our telecommunications assets based on our historical experience with similar assets, expected usage of the assets and anticipated technological changes with respect to those assets. Estimates and assumptions used in setting depreciable lives require both judgment and estimation. Our policies regarding accounting for these assets are set forth in note 2(g) to our consolidated financial statements. In 2006, taking into consideration the evolution of wireless mobile technologies, we revised the estimated

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life of our second generation mobile telecommunications technology, or 2G, wireless network equipment from seven years to five years. In addition, due to the expected changes of mobile switching technologies, including the development of soft switching technologies, to conform with the new generation of mobile technologies in 2007 and for years beyond, we revised the estimated useful life of our existing switching center equipment (excluding soft switching equipment, which conforms with the new generation of mobile technologies) from seven years to five years in 2007. The additional depreciation charges resulting from this revision in 2007 are estimated to be less than the additional depreciation charges resulting from our revision in the estimated useful life of our 2G wireless network equipment in 2006.

***Amortization of Other Intangible Assets***

Amortization of other intangible assets is calculated to write off the cost of items of other intangible assets using the straight-line method over their estimated useful lives unless such lives are indefinite. We review the estimated useful lives of other intangible assets annually in order to determine the amount of amortization expense to be recorded during any reporting period. The useful lives are based on the estimated period over which future economic benefits will be received by us and taking into account any unexpected adverse changes in circumstances or events. The amortization expense for future periods is adjusted if there are significant changes from previous estimates. Our policies regarding accounting for these assets are set forth in note 2(e) to our consolidated financial statements.

***Impairment of Property, Plant and Equipment, Goodwill and Other Intangible Assets***

Our property, plant and equipment, consisting primarily of telecommunications transceivers, switching centers, transmission and other network equipment, comprise a significant portion of our total assets. Changes in technology or industry conditions may cause the estimated period of use or the value of these assets to change. Long-lived assets, including property, plant and equipment and other intangible assets subject to amortization, are reviewed for impairment at least annually or whenever events or changes in circumstances have indicated that their carrying amounts may not be recoverable. If any such indication exists, the asset's recoverable amount is estimated. In addition, for goodwill and other intangible assets that have indefinite useful lives, the recoverable amount is estimated annually whether or not there is any indication of impairment.

The recoverable amount of an asset is the greater of its net selling price and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset, which requires significant judgment relating to level of revenue and amount of operating costs. We use all readily available information in determining an amount that is a reasonable approximation of the recoverable amount, including estimates based on reasonable and supportable assumptions and projections of revenue and operating costs. Changes in these estimates could have a significant impact on the carrying value of the assets and could result in additional impairment charge or reversal of impairment in future periods.

Estimates and assumptions used in testing for recoverability require both judgment and estimation. Our policies regarding accounting for these assets and assessing their recoverability are set forth in note 2(i) to our consolidated financial statements.

***Fair Value of Share Options Granted***

The fair value of share options granted to our employees is recognized as an employee cost with a corresponding increase in a capital reserve within equity and is measured based on a binomial lattice model. In applying the model, we estimate the expected volatility based on the historical volatility of our share price (calculated based on the weighted average remaining life of the share option), adjusted for any expected changes (based on publicly available information) to future volatility. We also estimate expected dividends based on our historical dividends and planned dividend payout ratio, if any. Changes in the subjective input assumptions could materially affect the fair value estimate of share options.

**Table of Contents****Results of Operations**

As a result of our acquisitions, our results of operations are not directly comparable with those in prior years.

The following table sets forth selected income statement data for the periods indicated:

|                           | Year Ended December 31,<br>2004      2005      2006<br>(in millions of RMB) |          |          |
|---------------------------|---|----------|----------|
| Operating revenue:        |   |          |          |
| Usage fees                | 128,534   | 156,710  | 189,710  |
| Monthly fees              | 24,760  | 25,055   | 21,629   |
| Value-added services fees | 30,236  | 50,187   | 69,309   |
| Other operating revenue   | 8,851   | 11,089   | 14,710   |
| Total operating revenue   | 192,381   | 243,041  | 295,358  |
| Operating expenses:       |   |          |          |
| Leased lines              | 3,861   | 3,224    | 2,451    |
| Interconnection           | 12,072  | 15,309   | 18,783   |
| Depreciation              | 44,186  | 56,368   | 64,574   |
| Personnel                 | 9,972   | 14,200   | 16,853   |
| Other operating expenses  | 62,811  | 80,254   | 100,772  |
| Total operating expenses  | 132,902   | 169,355  | 203,433  |
| Profit from operations    | 59,479  | 73,686   | 91,925   |
| Amortization of goodwill  | (1,930)   |          |          |
| Other net income          | 3,167   | 3,284    | 2,872    |
| Non-operating net income  | 900   | 1,025    | 1,017    |
| Interest income           | 1,014   | 1,615    | 2,604    |
| Finance costs             | (1,679)   | (1,346)  | (1,510)  |
| Profit before tax         | 60,951  | 78,264   | 96,908   |
| Income tax                | (19,180)  | (24,675) | (30,794) |
| Profit for the year       | 41,771  | 53,589   | 66,114   |
| Attributable to:          |   |          |          |
| Equity shareholders       | 41,749  | 53,549   | 66,026   |
| Minority interests        | 22  | 40       | 88       |
| Profit for the year       | 41,771  | 53,589   | 66,114   |

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### **Year Ended December 31, 2006 Compared to Year Ended December 31, 2005**

**Operating Revenue.** Our operating revenue is mainly derived from usage fees, monthly fees and value-added services fees. Usage fees include standard local usage fees for airtime and applicable domestic and international long distance charges receivable from subscribers for the use of our mobile telecommunications networks and facilities, and fees in respect of roaming out calls made by our subscribers outside their registered service areas. Value-added services fees are mainly derived from voice value-added services, SMS and non-SMS data business. Other operating revenue mainly represents interconnection revenue.

Operating revenue increased 21.5% from RMB243,041 million in 2005 to RMB295,358 million (US\$37,846 million) in 2006. This increase was primarily due to the continued expansion in our subscriber base, notably in the central and western regions of Mainland China, the continued growth in voice usage volume and the rapid expansion of our value-added business. Our total number of subscribers was approximately 301.2 million as of December 31, 2006, compared to approximately 246.7 million as of December 31, 2005.

Revenue from usage fees increased 21.1% from RMB156,710 million in 2005 to RMB189,710 million (US\$24,309 million) in 2006. This increase principally resulted from the continued rapid economic development in the PRC, the continued expansion in our subscriber base and the further increase in our voice usage volume during 2006. Although our average revenue per minute reflected a downward trend from 2005 to 2006, such decline stimulated a strong price elasticity, which in turn led to a strong growth in our voice usage volume that more than offset the adverse effect of the lower average revenue per minute on our overall revenue from usage fees in 2006. With the expected phase-in of the caller-party-pays regime within approximately two years and potential further declines in roaming charges, our tariffs may continue to decline in future periods, but we currently expect the impact of such developments on our operating revenue to be more than offset by the expected growth in our voice usage volume as most of our subscribers are lower-end. As a percentage of operating revenue, usage fees slightly decreased from 64.5% in 2005 to 64.2% in 2006.

Revenue from monthly fees decreased 13.7% from RMB25,055 million in 2005 to RMB21,629 million (US\$2,771 million) in 2006. This decrease was mainly due to the impact of service package substitution at point of access for specific bundles of features and services with no charge of monthly fees. As a percentage of operating revenue, monthly fees decreased from 10.3% in 2005 to 7.3% in 2006.

Revenue from value-added services increased 38.1% from RMB50,187 million in 2005 to RMB69,309 million (US\$8,881 million) in 2006. This increase was mainly due to our efforts in promoting and developing our value-added services by providing customers with diversified and personalized value-added services. Our value-added services include voice value-added services, SMS and non-SMS data business. Revenue generated from SMS reached RMB32,201 million in 2006, as compared to RMB24,671 million in 2005, representing an increase of 30.5%. At the same time, revenue generated from Color Ring and WAP, which are part of our non-SMS data business, grew substantially by 97.2% and 92.6% to RMB6,751 million and RMB6,875 million, respectively, as compared to the previous year. In addition, the expansion of our subscriber base was another growth driver for our value-added services. As a percentage of operating revenue, value-added services fees increased from 20.6% in 2005 to 23.5% in 2006. We expect further growth in our value-added business, in particular SMS and non-SMS data business, over the next several years.

Other operating revenue increased 32.7% from RMB11,089 million in 2005 to RMB14,710 million (US\$1,885 million) in 2006. This increase resulted principally from an increase in interconnection revenue as a result of the expansion in our subscriber base and an incremental increase in voice usage. As a percentage of operating revenue, other operating revenue increased from 4.6% in 2005 to 5.0% in 2006.

**Operating Expenses.** Operating expenses include leased line expenses, interconnection expenses, depreciation expenses relating to our mobile telecommunications network and other property, plant and equipment, personnel expenses and other operating expenses. Other operating expenses primarily consist of selling and promotion expenses, allowance for doubtful accounts, operating lease charges, maintenance charges, debt collection fees, spectrum charges and numbering resources charges, write-off of property, plant and equipment, amortization of other intangible assets and other miscellaneous expenses.

Operating expenses increased 20.1% from RMB169,355 million in 2005 to RMB203,433 million (US\$26,067 million) in 2006. This increase was due to the increase in depreciation expenses, interconnection expenses, personnel expenses and other operating expenses.

Total leased line payments decreased 24.0% from RMB3,224 million in 2005 to RMB2,451 million (US\$314 million) in 2006. This decrease was largely a result of the termination of surplus leased lines as we continued to use more self-constructed transmission lines and also augmented our networks to increase their efficiency. As a percentage of operating expenses, total leased line payments decreased from 1.9% in 2005 to 1.2% in 2006.



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Interconnection expenses increased 22.7% from RMB15,309 million in 2005 to RMB18,783 million (US\$2,407 million) in 2006. This increase was mainly due to the increase of subscriber base and voice usage volume. Interconnection expenses as a percentage of operating expenses increased from 9.0% in 2005 to 9.2% in 2006.

Depreciation expense increased 14.6% from RMB56,368 million in 2005 to RMB64,574 million (US\$8,274 million) in 2006. This increase was mainly due to the revision in the estimated useful life of our 2G wireless network equipment from seven years to five years, which resulted in an additional depreciation charge of RMB11,451 million in 2006. The effect of this additional depreciation charge during 2006 was partially offset by the effect of a reduced basis for calculating depreciation as a result of our substantial disposal and write-off of property, plant and equipment carried out in prior years. As a percentage of operating expenses, depreciation expense decreased from 33.3% in 2005 to 31.8% in 2006.

Personnel expenses increased 18.7% from RMB14,200 million in 2005 to RMB16,853 million (US\$2,160 million) in 2006. This increase was primarily due to the recognition of compensation expenses relating to share options granted in the aggregate amount of RMB2,264 million and an increase in headcount from 99,104 at the end of 2005 to 111,998 at the end of 2006. As a percentage of operating expenses, personnel expenses slightly decreased from 8.4% in 2005 to 8.3% in 2006.

Other operating expenses increased 25.6% from RMB80,254 million in 2005 to RMB100,772 million (US\$12,912 million) in 2006. This increase was primarily due to the increased sales and marketing expenses in 2006 as a result of our efforts in promoting brand development, rewarding and retaining our existing and high-value customers, and improving customer service quality with an aim towards enhancing customer loyalty. Our sales and marketing expenses may further increase if industry competition continues to intensify and adversely affects our subscriber growth and retention of our existing customers. However, we will continue implementing and refining our cost control measures and enhancing our advantage in terms of economies of scale. The increase in other operating expenses was also due to the additional network maintenance fee incurred in 2006. As a percentage of operating expenses, other operating expenses increased from 47.4% in 2005 to 49.5% in 2006. Apart from that, other operating expenses also included amortization of other intangibles assets totaling RMB203 million as a result of our acquisition of Peoples in 2006.

**Profit from Operations.** As a result of the foregoing, profit from operations increased 24.8% from RMB73,686 million in 2005 to RMB91,925 million (US\$11,779 million) in 2006, and operating margin (profit from operations as a percentage of operating revenue) increased from 30.3% in 2005 to 31.1% in 2006.

**Amortization of Goodwill.** Effective January 1, 2005, in order to comply with HKFRS 3 and HKAS 36, we adopted a new accounting policy for goodwill. The new policy has been applied prospectively in accordance with the transitional provisions as set out in HKFRS 3, whereby we no longer amortize goodwill over its estimated useful life but test it at least annually for impairment.

**Other Net Income.** Other net income represents primarily gross profit from sales of SIM cards, handsets and accessories. Other net income decreased 12.5% from RMB3,284 million in 2005 to RMB2,872 million (US\$368 million) in 2006. This decrease was principally due to the declining selling price of SIM cards and handsets.

**Non-Operating Net Income.** Non-operating net income slightly decreased by 0.8% from RMB1,025 million in 2005 to RMB1,017 million (US\$130 million) in 2006. Non-operating net income is mainly comprised of exchange loss, penalty income, amortization of deferred tax credit on purchase of domestic telecommunications equipment and other miscellaneous non-operating income. Although amortization of deferred tax credit increased 39.2% from RMB526 million in 2005 to RMB732 million in 2006, it was offset in part by an increase in exchange loss in the amount of RMB82 million from RMB130 million in 2005 to RMB212 million in 2006 and a reduction in other miscellaneous income as compared to 2005.

**Interest Income.** Interest income increased 61.2% from RMB1,615 million in 2005 to RMB2,604 million (US\$333 million) in 2006. The higher interest income in 2006 was primarily due to our larger cash balances as a result of the continued improvement in our cash generating capability, which was reflected in the increase of our net cash from operating activities from year to year. See also Item 5. Operating and Financial Review and Prospects Liquidity and Capital Resources Liquidity.

**Finance Costs.** Finance costs increased 12.2% from RMB1,346 million in 2005 to RMB1,510 million (US\$193 million) in 2006. This increase was primarily due to an increase in interest rate for deferred payable, which represented the balance of the purchase consideration payable to our immediate holding company in connection with our acquisition of the eight regional mobile

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telecommunications companies in 2002 and the ten regional mobile telecommunications companies and other telecommunications assets in 2004, computed at the rate of two-year U.S. dollar LIBOR swap rate per annum. The average interest rate for deferred payable increased in July 2006 from 2.76% to 5.41%, resulting in a substantial increase in finance costs. In 2006, the average interest rate that we paid on our outstanding borrowings was approximately 4.11%.

**Profit before Tax.** As a result of the foregoing, profit before tax increased 23.8% from RMB78,264 million in 2005 to RMB96,908 million (US\$12,417 million) in 2006.

**Taxation.** Our income tax expense increased 24.8% from RMB24,675 million in 2005 to RMB30,794 million (US\$3,946 million) in 2006. This increase was primarily due to an increase in our profit before tax. Our effective tax rate was 31.5% in 2005 and 31.8% in 2006, respectively.

**Profit attributable to equity shareholders.** As a result of the foregoing and after taking into account minority interests, profit attributable to equity shareholders increased 23.3% from RMB53,549 million in 2005 to RMB66,026 million (US\$8,460 million) in 2006. This increase was primarily due to our organic growth. Net profit margin (profit attributable to equity shareholders as a percentage of operating revenue) increased from 22.0% in 2005 to 22.4% in 2006.

### **Year Ended December 31, 2005 Compared to Year Ended December 31, 2004**

**Operating Revenue.** Operating revenue increased 26.3% from RMB192,381 million in 2004 to RMB243,041 million in 2005. This increase was primarily due to the continued expansion in our subscriber base, the continued growth in voice usage volume, the rapid expansion of our value-added business and the full-year effect of our acquisition of the ten regional mobile telecommunications companies and other telecommunications assets in July 2004. Our total number of subscribers was approximately 246.7 million as of December 31, 2005, compared to approximately 204.3 million as of December 31, 2004.

Revenue from usage fees increased 21.9% from RMB128,534 million in 2004 to RMB156,710 million in 2005. This increase was principally due to our organic subscriber growth, the organic increase in voice usage volume and the full-year effect of our acquisition of the ten regional mobile telecommunications companies and other telecommunications assets in July 2004. As a percentage of operating revenue, usage fees decreased from 66.8% in 2004 to 64.5% in 2005.

Revenue from monthly fees increased 1.2% from RMB24,760 million in 2004 to RMB25,055 million in 2005. This increase was mainly due to the continued increase in contract subscribers and the full-year effect of our acquisition of the ten regional mobile telecommunications companies and other telecommunications assets in July 2004. As a percentage of operating revenue, monthly fees decreased from 12.9% in 2004 to 10.3% in 2005.

Revenue from value-added services increased 66.0% from RMB30,236 million in 2004 to RMB50,187 million in 2005. This increase was mainly due to the increased revenue from wireless data and various value-added services as well as the full-year effect of our acquisition of the ten regional mobile telecommunications companies and other telecommunications assets in July 2004. As a percentage of operating revenue, value-added services fees increased from 15.7% in 2004 to 20.6% in 2005.

Other operating revenue increased 25.3% from RMB8,851 million in 2004 to RMB11,089 million in 2005. This increase resulted principally from increased interconnection revenue as well as the full-year effect of our acquisition of the ten regional mobile telecommunications companies and other telecommunications assets in July 2004.

**Operating Expenses.** Operating expenses increased 27.4% from RMB132,902 million in 2004 to RMB169,355 million in 2005. This increase was primarily due to the increase in depreciation expenses, personnel expenses and other operating expenses, as well as the full-year effect of our acquisition of the ten regional mobile telecommunications companies and other telecommunications assets in July 2004.

Total leased line payments decreased 16.5% from RMB3,861 million in 2004 to RMB3,224 million in 2005. This decrease was largely a result of the termination of surplus leased lines as we continued to use more self-constructed transmission lines and also augmented our networks to increase their efficiency. As a percentage of operating expenses, total leased line payments decreased from 2.9% in 2004 to 1.9% in 2005.

Interconnection expenses increased 26.8% from RMB12,072 million in 2004 to RMB15,309 million in 2005. This increase was mainly due to the increase of subscriber base and voice usage volume and the full-year effect of our acquisition of the ten regional mobile telecommunications companies and other telecommunications assets in July 2004. Interconnection expenses as a percentage of operating expenses decreased from 9.1% in 2004 to 9.0% in 2005.





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Depreciation expense increased 27.6% from RMB44,186 million in 2004 to RMB56,368 million in 2005. This increase was mainly due to the expansion of our network capacity, the construction of various support networks and the full-year effect of our acquisition of the ten regional mobile telecommunications companies and other telecommunications assets in July 2004. As a percentage of operating expenses, depreciation expense slightly increased from 33.2% in 2004 to 33.3% in 2005.

Personnel expenses increased 42.4% from RMB9,972 million in 2004 to RMB14,200 million in 2005. This increase was primarily due to the recognition of the compensation expenses of share options granted in the aggregate amount of RMB1,553 million as a result of our adoption of HKFRS 2 during the year and the full-year effect of our acquisition of the ten regional mobile telecommunications companies and other telecommunications assets in July 2004. As a percentage of operating expenses, personnel expenses increased from 7.5% in 2004 to 8.4% in 2005.

Other operating expenses increased 27.8% from RMB62,811 million in 2004 to RMB80,254 million in 2005. This increase was primarily due to the increase in selling and promotion expenses and the full year effect of our acquisition of the ten regional mobile telecommunications companies and other telecommunications assets in July 2004. As a percentage of operating expenses, other operating expenses increased from 47.3% in 2004 to 47.4% in 2005.

**Profit from Operations.** As a result of the foregoing, profit from operations increased 23.9% from RMB59,479 million in 2004 to RMB73,686 million in 2005, and operating margin (profit from operations as a percentage of operating revenue) decreased from 30.9% in 2004 to 30.3% in 2005.

**Amortization of Goodwill.** The amount in 2004 represented the amortization of goodwill arising from acquisitions of regional mobile telecommunications companies and other telecommunications assets on or after January 1, 2001. Effective January 1, 2005, in order to comply with HKFRS 3 and HKAS 36, we adopted a new accounting policy for goodwill. The new policy has been applied prospectively in accordance with the transitional provisions as set out in HKFRS 3, whereby we no longer amortize goodwill over its estimated useful life but test it at least annually for impairment.

**Other Net Income.** Other net income represents primarily gross profit from sales of SIM cards, handsets and accessories. Other net income increased 3.7% from RMB3,167 million in 2004 to RMB3,284 million in 2005. This increase was principally due to the increase in sales of SIM cards.

**Non-Operating Net Income.** Non-operating net income increased 13.8% from RMB900 million in 2004 to RMB1,025 million in 2005. This increase was primarily due to the increase of amortization of deferred tax credits in the amount of RMB174 million from RMB352 million in 2004 to RMB526 million in 2005. The increase in amortization of deferred tax credit was primarily due to the increase in the tax credits we received as a result of our purchase of domestic telecommunications equipment.

**Interest Income.** Interest income increased 59.3% from RMB1,014 million in 2004 to RMB1,615 million in 2005. The higher interest income in 2005 was primarily due to our larger cash balances as a result of the increase of our net cash from operating activities.

**Finance Costs.** Finance costs decreased 19.8% from RMB1,679 million in 2004 to RMB1,346 million in 2005. This decrease was primarily due to the decrease in short-term borrowings and the repayment of US\$690 million convertible notes due on November 3, 2005. In 2005, the average interest rate that we paid on our outstanding borrowings was approximately 3.3%.

**Profit before Tax.** As a result of the foregoing, profit before tax increased 28.4% from RMB60,951 million in 2004 to RMB78,264 million in 2005.

**Taxation.** Our income tax expense increased 28.7% from RMB19,180 million in 2004 to RMB24,675 million in 2005. This increase was primarily due to an increase in our profit before tax. Our effective tax rate was 31.3% in 2004 and 31.5% in 2005, respectively.

**Profit attributable to equity shareholders.** As a result of the foregoing and after taking into account minority interests, profit attributable to equity shareholders increased 28.3% from RMB41,749 million in 2004 to RMB53,549 million in 2005. This increase was primarily due to our organic growth and the full-year effect of our acquisition of the ten regional mobile telecommunications companies and other telecommunications assets in July 2004. Net profit margin (profit attributable to equity shareholders as a percentage of operating revenue) increased from 21.7% in 2004 to 22.0% in 2005.



**Table of Contents****Liquidity and Capital Resources*****Liquidity***

Our principal source of liquidity is cash generated from our operations. As of December 31, 2006, we had a working capital (current assets minus current liabilities) surplus of RMB30,900 million (US\$3,960 million) compared to a working capital surplus of RMB11,122 million as of December 31, 2005 and a working capital deficit of RMB17,757 million as of 2004. The substantial improvement in our working capital position in 2006 and 2005 was mainly due to a significant increase in deposits with banks and cash and cash equivalent generated as a result of our business development and the continued expansion of our subscriber base in recent years. As of December 31, 2004, 2005 and 2006, accounts receivable totaled RMB6,553 million, RMB6,603 million and RMB7,153 million (US\$917 million), respectively. Short-term bank and other loans (including the current portion of long-term loans, convertible notes, bonds and capital lease obligations) as of December 31, 2004, 2005 and 2006 totaled RMB8,248 million, RMB68 million and RMB3,064 million (US\$393 million), respectively.

The following table summarizes certain cash flow information for the periods indicated.

|   | Year ended December 31, |          |           |
|---|-------------------------|----------|-----------|
|   | 2004                    | 2005     | 2006      |
|   | (in millions of RMB)    |          |           |
| Net cash from operating activities        | 103,779                 | 131,709  | 149,346   |
| Net cash used in investing activities     | (73,302)                | (87,116) | (118,841) |
| Net cash used in financing activities     | (24,457)                | (25,173) | (23,587)  |
| Net increase in cash and cash equivalents | 6,020                   | 19,420   | 6,918     |

Net cash from operating activities increased 13.4% from RMB131,709 million in 2005 to RMB149,346 million in 2006, reflecting the growth in operating revenue due to the increase in our subscriber base through the continued growth and economies of scale. Net cash from operating activities increased 26.9% from RMB103,779 million in 2004 to RMB131,709 million in 2005, reflecting the growth in operating revenue due to the increase in our subscriber base through the continued organic growth, economies of scale and the full year effect of our acquisition of the ten regional mobile telecommunications companies and other telecommunications assets in July 2004.

Net cash used in investing activities increased 36.4% from RMB87,116 million in 2005 to RMB118,841 million in 2006. This increase was primarily due to the increases in deposits with banks and capital expenditures. Net cash used in investing activities increased 18.8% from RMB73,302 million in 2004 to RMB87,116 million in 2005. This increase was primarily due to the increases in deposits with banks and capital expenditures.

Net cash used in financing activities decreased 6.3% from RMB25,173 million in 2005 to RMB23,587 million in 2006. This decrease was primarily due to the redemption in 2005 of convertible notes issued on November 3, 2000 and the repayment of bank and other loans in 2005 that, combined together, had resulted in higher net cash used in financing activities in 2005 as compared to 2006. The slight increase in net cash used in financing activities in 2005 as compared to 2004 was mainly due to a larger dividend payment to shareholders in 2005 compared to 2004.

***Capital Expenditures***

Capital expenditures incurred during 2004, 2005 and 2006 were RMB61,398 million, RMB71,453 million and RMB86,988 million (US\$11,146 million), respectively. We incurred capital expenditures principally for the construction of our GSM networks, support systems, transmission facilities and structural facilities and the development of new technologies and new businesses. The increase in our capital expenditures was primarily due to increased demand on our network services resulting from the continued expansion of our subscriber base, growth in voice usage volume and rapid development of our value-added business.

We estimate that we will spend approximately RMB99.8 billion (US\$12.79 billion) in 2007, RMB98.0 billion (US\$12.56 billion) in 2008 and RMB96.0 billion (US\$12.30 billion) in 2009 in capital expenditures. These amounts do not include specific capital expenditures that would be required for the construction of 3G networks. The required funding will be sourced largely from cash generated from our operating activities. We expect to incur these expenditures primarily for the purpose of:

further expanding our GSM network capacity and coverage;

increasing our efforts in improving our support systems;

building our own transmission facilities where economically advantageous; and

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developing and providing new technologies and new businesses.

Following our initial public offering, we have funded our capital requirements primarily with cash generated from operations, proceeds from equity and debt offerings and, to the extent necessary, short-term and long-term borrowings. We believe our available cash and cash generated from future operations will be sufficient to fund most of the capital expenditures and working capital necessary for the planned network expansion and continued growth of our mobile telecommunications operations through the end of 2008.

Moreover, we believe that to the extent we are granted any 3G license by the Ministry of Information Industry and our 3G networks are constructed, GSM and 3G will co-exist in our networks over an extended period of time. In that case, the capital expenditures for our existing GSM networks are expected to be reduced, and the extent of such reduction depends primarily on when we will be granted a 3G license and what 3G-based technology standard we will be required to adopt.

We may seek to obtain additional sources of financing to fund our network expansion and possible future acquisitions, to the extent necessary.

### ***Contractual Obligations and Commitments***

#### **Indebtedness**

As of December 31, 2004, 2005 and 2006, we did not have any long-term bank and other loans and obligations under capital leases (excluding current portions), and our short-term bank and other loans (including the current portion of long-term loans, convertible notes, bonds and capital lease obligations) totaled RMB8,248 million, RMB68 million and RMB3,064 million (US\$393 million), respectively. Our short-term loans increased in 2006 primarily due to the inclusion of bonds that are due within one year. Our short-term loans decreased in 2005 primarily due to our redemption of convertible notes, with an aggregate principal amount of US\$690 million, on November 3, 2005. Capital lease obligations totaled RMB68 million and RMB68 million (US\$9 million) as of December 31, 2005 and 2006, respectively.

On November 3, 2000, we issued unsecured convertible notes with a principal amount of US\$690 million due on November 3, 2005. The notes bear interest at the rate of 2.25% per annum and such interest is payable semi-annually on May 3 and November 3 of each year, commencing May 3, 2001. We fully redeemed these unsecured convertible notes on November 3, 2005.

On June 18, 2001, Guangdong Mobile, one of our wholly-owned subsidiaries, issued bonds with a principal amount RMB5,000 million at a floating rate due June 18, 2011. Guangdong Mobile's payment obligations under the bonds are guaranteed in full by us, and our guarantee is further guaranteed by CMCC.

On October 28, 2002, Guangdong Mobile, one of our wholly-owned subsidiaries, issued RMB3,000 million five-year guaranteed bonds and RMB5,000 million fifteen-year guaranteed bonds. Guangdong Mobile's payment obligations under these two bonds are guaranteed in full by us, and our guarantee obligation is further guaranteed by CMCC.

The deferred consideration of US\$2,800 million for our acquisition of the eight regional mobile telecommunications companies in 2002 and the deferred consideration of US\$1,650 million for our acquisition of the ten regional mobile telecommunications companies and other telecommunications assets in 2004 are subordinated to other senior debt owed by us from time to time. In addition, these deferred considerations are payable by the fifteenth anniversary of the date of the completion of the respective acquisitions, and we may make an early payment of all or part of these deferred considerations at any time without penalty. We are required to pay interest semi-annually on the actual amount of these deferred considerations unpaid from the date of completion of the respective acquisitions. Interest is calculated at the two-year US dollar London Inter-Bank Offered Rate, or LIBOR, swap rate at 11:00 a.m. (New York City time) on the second business day next preceding the date of the respective acquisition agreements for the first two years after completion of the respective acquisitions. Thereafter, the interest rate will be adjusted every two years to equal the two-year US dollar LIBOR swap rate prevailing at 11:00 a.m. (New York City time) on the relevant interest determination dates. The payment of the deferred considerations and the interest payments can be made in Hong Kong dollars, RMB or US dollars (or other agreed currencies). Any payment made in currencies other than US dollars will be accounted for based on the exchange rates between US dollars and such currencies prevailing at 12:00 noon (New York City time) on the day which is two business days next preceding the date of the respective acquisition agreements. We used the entire proceeds from the RMB3,000 million guaranteed bonds due 2007 and RMB5,000 million guaranteed bonds due 2017, both issued on October 28, 2002 by Guangdong Mobile, our wholly-owned subsidiary, to pay a portion of the US\$2,800 million deferred consideration for our acquisition of the eight regional mobile telecommunications companies in 2002.

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Our corporate credit rating was raised to A2/Positive Outlook by Moody's and to A/Outlook Stable by Standard & Poor's in July 2006, which is equivalent to China's sovereign credit rating. Any downgrade in our credit rating will not trigger any events of default on our outstanding bonds or loans or our existing credit facilities. Our management currently believes that a downgrade below A2/Positive Outlook or A/Outlook Stable is not likely.

For a discussion of our interest rate risk, please see Item 11. Quantitative and Qualitative Disclosures About Market Risk.

**Other Contractual Obligations and Commitments**

As of December 31, 2006, we had various contractual obligations and commitments which are more fully disclosed in the notes to our consolidated financial statements. The principal components of these obligations and commitments include:

our short-term and long-term debts (in addition to the bonds and notes described under **Indebtedness** above), which includes capital leases;

operating leases; and

capital commitments.

In the ordinary course of our business, we routinely enter into commercial commitments for various aspects of our operations, such as repair and maintenance. However, we believe that those commitments will not have a material effect on our financial condition, results of operations or cash flows.

For further disclosure regarding leases and other commitments, please see notes 27 and 28 to our consolidated financial statements included elsewhere in this annual report on Form 20-F.

The following table sets forth certain information regarding our contractual obligations to make future payments (including relevant estimated interest payment) as of December 31, 2006:

|                               |         | Payments Due by Period |            |           |         |
|-------------------------------|---------|------------------------|------------|-----------|---------|
|                               |         | Over                   |            | Over      |         |
|                               |         | 1 year but             | 3 year but |           |         |
|                               |         | Less Than              | less than  | less than | After   |
| Contractual Obligations       | Total   | 1 year                 | 3 years    | 5 years   | 5 years |
|                               |         | (in millions of RMB)   |            |           |         |
| Bills Payable                 | 2,212   | 2,212                  |            |           |         |
| Deferred Payable              | 38,539  | 1,279                  | 2,558      | 2,558     | 32,144  |
| Long-Term Debt                | 16,594  | 3,552                  | 931        | 5,801     | 6,310   |
| Capital Lease Obligations     | 68      | 68                     |            |           |         |
| Trade Payable                 | 57,240  | 57,240                 |            |           |         |
| Total Contractual Obligations | 114,653 | 64,351                 | 3,489      | 8,359     | 38,454  |

The following table sets forth certain information regarding our other commercial commitments as of December 31, 2006:





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|                              | Amount of Commitment |                       |            |           |         |
|------------------------------|----------------------|-----------------------|------------|-----------|---------|
|                              | Total                | Expiration Per Period |            | Over      |         |
|                              |                      | Over                  |            | Over      |         |
|                              |                      | 1 year but            | 3 year but |           |         |
|                              | Amount               | Less Than             | less than  | less than | After   |
| Other Commercial Commitments | Committed            | 1 year                | 3 years    | 5 years   | 5 years |
|                              |                      | (in millions of RMB)  |            |           |         |
| Operating Lease Commitments  | 13,672               | 4,644                 | 4,524      | 2,447     | 2,057   |
| Capital Commitments          | 68,772               | 68,772                |            |           |         |
| Total Commercial Commitments | 82,444               | 73,416                | 4,524      | 2,447     | 2,057   |

**Off-Balance Sheet Arrangements**

As of December 31, 2006, we did not have any off-balance sheet arrangements or any written options on non-financial assets.

**Foreign Exchange**

We maintain our accounts in Renminbi and substantially all of our revenue and expenses are denominated in Renminbi. Our capital expenditures totaled the equivalent of RMB61,398 million, RMB71,453 million and RMB86,988 million (US\$11,146 million) in 2004, 2005 and 2006, respectively.

All of our current operating subsidiaries are incorporated in Mainland China, except for Peoples, which became our wholly-owned operating subsidiary as of March 28, 2006. Under the current foreign exchange system in Mainland China, our subsidiaries in Mainland China may not be able to hedge effectively against currency risk, including any possible future Renminbi devaluation. See Item 3. Key Information Risk Factors Fluctuations in exchange rates could materially and adversely affect our financial results and Item 10. Additional Information Exchange Controls .

Each of our operating subsidiaries in Mainland China is able to purchase foreign exchange for settlement of current account transactions, as defined in applicable regulations, in order to satisfy its foreign exchange requirements.

**U.S. GAAP Reconciliation**

Our consolidated financial statements are prepared in accordance with Hong Kong GAAP, which differ in certain significant respects from U.S. GAAP. The following table sets forth a comparison of our profit attributable to equity shareholders and shareholders' equity in accordance with Hong Kong GAAP and U.S. GAAP.

|   | As of or for the year ended |         |         |
|---|-----------------------------|---------|---------|
|   | December 31                 |         |         |
|   | 2004                        | 2005    | 2006    |
|   | (in millions of RMB)        |         |         |
| Profit for the year attributable to equity shareholders in accordance with: |                             |         |         |
| Hong Kong GAAP  | 41,749                      | 53,549  | 66,026  |
| U.S. GAAP   | 45,061                      | 54,504  | 65,074  |
| Shareholders' equity in accordance with:                                    |                             |         |         |
| Hong Kong GAAP  | 233,161                     | 272,824 | 319,002 |
| U.S. GAAP   | 198,119                     | 237,252 | 282,690 |

Under Hong Kong GAAP, we adopted the purchase accounting method to account for our acquisitions of the eight regional mobile telecommunications companies in July 2002, our acquisition of the ten regional mobile telecommunications companies and other telecommunications assets in July 2004 and our acquisition of Peoples in 2006. Under the purchase accounting method, the acquired results of

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these companies were included in the results of operations from the respective dates of acquisition. Goodwill is the excess of the cost over the fair value of our share of the identifiable assets and liabilities acquired. In prior years, goodwill arising on the date of our acquisition of the eight regional mobile telecommunications companies in July 2002 and our acquisition of the ten

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regional mobile telecommunications companies and other telecommunications assets in July 2004 is amortized to the consolidated statements of income on a straight line of twenty years. Effective January 1, 2005, we no longer amortize goodwill due to the adoption of HKFRS 3. See Special Note on Our Financial Information and Certain Statistical Information Presented in This Annual Report .

Under U.S. GAAP, because we and the companies acquired from our immediate holding company were deemed to be under common control prior to the acquisitions, the acquisitions were considered a combination of entities under common control . Under U.S. GAAP, combinations of entities under common control are accounted for under the as if pooling-of-interests method, whereby assets and liabilities are accounted for at historical cost and our consolidated financial statements are adjusted retrospectively to include the financial statements of these previously separate companies for all periods presented. The consideration we paid or payable in each acquisition was treated as an equity transaction in the respective years of each acquisition, and goodwill amortization recognized under Hong Kong GAAP in 2004 was reversed for U.S. GAAP purposes.

In addition, there are other differences between Hong Kong GAAP and U.S. GAAP for the periods presented, which relate primarily to:

the computation of capitalized interest;

the revaluation of property, plant and equipment and land lease prepayments of the acquired companies under Hong Kong GAAP;

the recognition of deferred income taxes;

the non-recognition under Hong Kong GAAP of certain of our employee housing scheme costs;

the treatment of share options we grant to directors and employees;

the recognition as revenue of connection fees and telephone number selection fees; and

the net savings arising from interconnection, roaming and leased line agreements.

Disclosure relating to these differences can be found in note 40 to our consolidated financial statements. In addition, our condensed consolidated balance sheets as of December 31, 2005 and 2006 and our condensed consolidated statements of income, shareholders' equity and comprehensive income and cash flows for the years ended December 31, 2004, 2005 and 2006 prepared and presented under U.S. GAAP have been included in note 40 to our consolidated financial statements to reflect the impact of the significant differences between Hong Kong GAAP and U.S. GAAP.

## **Item 6. Directors, Senior Management and Employees.**

### **Directors and Senior Management**

The following table sets forth certain information concerning our directors and senior management as of May 31, 2007.

| <b>Name</b>       | <b>Age</b> | <b>Position</b>  |
|-------------------|------------|--|
| Mr. WANG Jianzhou | 58         | Executive Director, Chairman and Chief Executive Officer       |
| Mr. LI Yue        | 48         | Executive Director and Vice President                          |
| Mr. LU Xiangdong  | 47         | Executive Director and Vice President                          |
| Mr. XUE Taohai    | 51         | Executive Director, Vice President and Chief Financial Officer |

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|                          |    |                                       |
|--------------------------|----|---------------------------------------|
| Mr. ZHANG Chenshuang     | 55 | Executive Director and Vice President |
| Mr. SHA Yuejia           | 49 | Executive Director and Vice President |
| Mr. LIU Aili             | 43 | Executive Director and Vice President |
| Madam XIN Fanfei         | 50 | Executive Director and Vice President |
| Mr. XU Long              | 50 | Executive Director                    |
| Mr. Paul Michael DONOVAN | 48 | Non-Executive Director                |
| Dr. LO Ka Shui           | 60 | Independent Non-Executive Director    |
| Mr. Frank K.S. WONG      | 59 | Independent Non-Executive Director    |
| Mr. Moses M.C. CHENG     | 57 | Independent Non-Executive Director    |

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Mr. WANG Jianzhou has served as our Executive Director, Chairman and Chief Executive Officer since November 2004. Mr. Wang is in charge of our overall management. He is also the President of CMCC, the ultimate controlling shareholder of the Company, and the Chairman of CMC. Prior to joining us, Mr. Wang served as Deputy Director General and Director General of the Posts and Telecommunications Bureau of Hangzhou City, Deputy Director General of the Posts and Telecommunications Administration of Zhejiang Province, Director General of the Department of Planning and Construction of the Ministry of Posts and Telecommunications, Director General of the Department of General Planning of the Ministry of Information Industry, and Director, Executive Vice President, President and Chairman of China United Telecommunications Corporation, Executive Director, President, Chairman and Chief Executive Officer of China Unicom Limited, and Chairman and President of China United Telecommunications Corporation Limited. Mr. Wang graduated in 1985 from the Department of Management Engineering of Zhejiang University with a Master's Degree in Engineering, and holds a doctoral degree in business administration from Hong Kong Polytechnic University. Mr. Wang is a professor-level senior engineer with extensive knowledge and has over 29 years of experience in the telecommunications industry.

Mr. LI Yue has served as our Executive Director and Vice President since March 2003. Mr. Li assists the Chief Executive Officer in relation to our network, planning, development strategy and management information systems. He has been serving as Vice President of CMCC since April 2000. Mr. Li is also a director of CMC. Mr. Li previously served as the Deputy Director General of the Tianjin Posts and Telecommunications Administration and the President of Tianjin Mobile Communications Company. Mr. Li graduated from Tianjin University with a Master's Degree, and holds a doctoral degree in business administration from Hong Kong Polytechnic University. Mr. Li is a professor-level senior engineer with over 31 years of experience in the telecommunications industry.

Mr. LU Xiangdong has served as our Executive Director and Vice President since March 2003. Mr. Lu assists the Chief Executive Officer principally with respect to our marketing, data and corporate customer matters. He has been serving as Vice President of CMCC since April 2000. Mr. Lu is also a director of CMC, Chairman of Aspire Holdings Limited and a director of Phoenix Satellite Television Holdings Limited. He previously served as the Director General of Fujian Wireless Telecommunications Administration and the Deputy Director General of the Mobile Telecommunications Bureau of the Ministry of Posts and Telecommunications. Mr. Lu graduated from the Academy of Posts and Telecommunications of the Ministry of Posts and Telecommunications with a Master's Degree in wireless telecommunications, and holds a doctoral degree in economics from Peking University. Mr. Lu is a professor-level senior engineer with nearly 25 years of experience in the telecommunications industry.

Mr. XUE Taohai has served as our Executive Director, Vice President and Chief Financial Officer since July 2002. Mr. Xue assists the Chief Executive Officer in relation to our corporate finance and human resources remuneration. Mr. Xue is also Vice President of CMCC and a director of CMC. Mr. Xue previously served as the Deputy Director General of the Finance Department of the former Ministry of Posts and Telecommunications, Deputy Director General of the Department of Financial Adjustment and Clearance of the Ministry of Information Industry and Deputy Director General of the former Directorate General of Telecommunications. He graduated from Henan University and received an EMBA degree from Peking University. He is a senior accountant with over 27 years of experience in the telecommunications industry and financial management.

Mr. ZHANG Chenshuang has served as our Executive Director and Vice President since July 2004. Mr. Zhang assists the Chief Executive Officer in relation to our corporate affairs. Mr. Zhang has been serving as Vice President of CMCC since April 2001. Mr. Zhang is also a director of CMC. Mr. Zhang previously served as the Deputy Director General of the Office of the Ministry of Posts and Telecommunications, the Director General of the Neimenggu Posts and Telecommunications Administration, and the Assistant to the President of CMCC. He graduated from the Party School of the CPC and received an MBA degree from Hong Kong Polytechnic University. He is a senior economist with over 27 years of experience in the telecommunications industry.

Mr. SHA Yuejia has served as our Executive Director and Vice President since March 2006. Mr. Sha assists the Chief Executive Officer in relation to our business support, technology and research & development. He is also a Vice President of CMCC and a director of CMC since May 2005. He previously served as Director of the Engineering Construction Department IV Division of Beijing Telecommunications Administration, President of Beijing Telecommunications Planning Design Institute, Deputy Director General of Beijing Telecommunications Administration, Vice President of Beijing Mobile Communications Company, and Director

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and Vice President, Chairman and President of Beijing Mobile. Mr. Sha graduated from Beijing University of Posts and Telecommunications, and received a Master's Degree from the Academy of Posts and Telecommunications of the Ministry of Posts and Telecommunications and a doctoral degree in business administration from Hong Kong Polytechnic University. He is a professor-level senior engineer with over 24 years of experience in the telecommunications industry.

Mr. LIU Aili has served as our Executive Director and Vice President since March 2006. Mr. Liu assists the Chief Executive Officer in relation to our business expansion. He is also a Vice President of CMCC, a director of CMC and Chairman of CMPak Limited. He previously served as Deputy Director General of Shandong Mobile Telecommunications Administration, Director General of Shandong Mobile Telecommunications Administration and General Manager of Shandong Mobile Communications Enterprises, Vice President of Shandong Mobile Communications Company, Director-General of Network Department of China Mobile Communications Corporation, and Chairman and President of Shandong Mobile and Zhejiang Mobile. Mr. Liu graduated from Heilongjiang Posts and Telecommunications School with an associate degree and completed a post-graduate program in economics at Shandong University. Mr. Liu also received a Master of Management degree from Norwegian School of Management BI and a doctoral degree in business administration from Hong Kong Polytechnic University. He is a professor-level senior engineer with over 24 years of experience in the telecommunications industry.

Madam XIN Fanfei has served as our Executive Director and Vice President since January 2006. Madam Xin assists the Chief Executive Officer in relation to our general administration and investor and media relations. She is also Chairwoman of Peoples. She previously served as Deputy Director of the Foreign Affairs Division, Deputy Director of the Planning Division and Chief of the Planning Office, Director of the Planning Division, Director of the Department of Planning and Construction of Tianjin Posts and Telecommunications Administration, Assistant to the Director General and Director of the Department of Planning and Construction of Tianjin Mobile Telecommunications Administration, Vice President of Tianjin Mobile Communications Company, Vice President of Tianjin Mobile, President of Heilongjiang Mobile Communications Company, and Chairwoman and President of Heilongjiang Mobile. Madam Xin graduated from Xidian University and received an EMBA degree from Peking University. She is currently pursuing a doctoral degree in business administration from Hong Kong Polytechnic University. Madam Xin is a professor-level senior engineer with many years of experience in the telecommunications industry.

Mr. XU Long has served as our Executive Director since August 1999. He is also the Chairman and President of Guangdong Mobile, responsible for the mobile telecommunications operations in Guangdong Province. He previously served as Deputy Director of Shaoxing Posts and Telecommunications Bureau, President of Zhejiang Nantian Posts and Telecommunications Group Company, Director of the General Office and Deputy Director General of the Posts and Telecommunications Administration in Zhejiang Province, and Chairman and President of Zhejiang Mobile. He graduated from Zhejiang Radio and Television University in 1985, and holds a doctoral degree in business administration from Hong Kong Polytechnic University. Mr. Xu is a senior economist with 29 years of experience in the telecommunications industry.

Mr. Paul Michael DONOVAN has served as our Non-Executive Director since June 2006. Mr. Donovan is Chief Executive Officer for Central Europe, Middle East, Asia-Pacific and Affiliates (EMAPA) of Vodafone. Mr. Donovan is also a member of the Executive Committee of Vodafone, a director of Vodafone's operating companies located in Turkey, Hungary, Australia, New Zealand, Egypt, Czech Republic and Romania and also a director of certain other subsidiaries of Vodafone. Prior to his appointment as the Chief Executive Officer of the EMAPA division, Mr. Donovan was Chief Executive Officer of the Other Vodafone Subsidiaries, which included 14 of Vodafone's operating subsidiaries. Mr. Donovan joined Vodafone UK in 1999 as Managing Director - Commercial, and in 2001 was appointed the Chief Executive Officer of Vodafone Ireland. In 2004 he assumed the additional role of Global Director of Business Integration, leading One Vodafone, Vodafone's business transformation program. Mr. Donovan began his career in FMCG sales and marketing at the Mars Group, before becoming Marketing Director at Coca-Cola and Schweppes Beverages in 1989. He holds a Bachelor of Arts Degree in Scandinavian Studies from University College London and a Master's Degree in Business Administration from Bradford University Management Centre, and has over 15 years experience in the telecommunications and information technology industries, gained at Apple Computer, BT and Cable and Wireless subsidiary One2One as Commercial Director, and as Chief Commercial Officer at Australian telecommunications provider Optus Communications. His other directorships held in listed public companies in the last three years include Vodafone Libertel NV, Vodafone Egypt Telecommunications S.A.E., Vodafone-PanafonHellenic Telecommunications Company S.A. and Bharti Tele-Ventures Limited.

Dr. LO Ka Shui has served as our independent Non-Executive Director since April 2001. Dr. Lo is the Chairman and Managing Director of Great Eagle Holdings Limited, and is the non-executive chairman of Eagle Asset Management (CP) Limited (manager of Hong Kong listed Champion Real Estate Investment Trust). He is also a non-executive Director of The Hongkong and Shanghai Banking Corporation Limited, Shanghai Industrial Holdings Limited, Phoenix Satellite Television Holdings Limited, City e-Solutions Limited, Melco International Development Limited, The HSBC China Fund Limited, Tom Online Inc. and Winsor

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Properties Holdings Limited. He was also a director of Hong Kong Exchanges and Clearing Limited. Apart from the aforesaid, he did not hold any other directorships in other listed public companies in the last three years. He is also a Vice President of the Real Estate Developers Association of Hong Kong, a Trustee of the Hong Kong Centre for Economic Research and a Member of the Airport Authority. Dr. Lo graduated with a Bachelor of Science Degree from McGill University in Canada and a Doctorate degree in medicine from Cornell University in the United States. He is board certified in cardiology. He has more than 27 years of experience in property and hotel development and investment both in Hong Kong and overseas.

Mr. Frank K.S. WONG has served as our independent Non-Executive Director since August 2002. Mr. Wong is currently Vice Chairman of DBS Bank, Chief Operating Officer and a member of the boards of DBS Bank and DBS Group Holdings, and Chairman of DBS Bank (Hong Kong). Mr. Wong is also a director of the Singapore Tourism Board, National Healthcare Group Pte Ltd and Mapletree Investments Pte Ltd, and is a member of the University Court of The University of Hong Kong. He previously held a series of progressively senior positions with regional responsibility at Citibank, JP Morgan and NatWest from 1967 to 1999. Mr. Wong has also served in various positions with Hong Kong's government bodies including the Chairman of the Hong Kong Futures Exchange. Mr. Wong has many years of finance and commercial management experience.

Mr. Moses M.C. CHENG has served as our independent Non-Executive Director since March 2003. Mr. Cheng is a practicing solicitor and the senior partner of Messrs. P.C. Woo & Co. Mr. Cheng was a member of the Legislative Council of Hong Kong between 1991 and 1995. He is the Founder Chairman of the Hong Kong Institute of Directors of which he currently is the Honorary President and Chairman Emeritus. His other directorships held in listed public companies in the last three years include Beijing Capital International Airport Company Limited, City Telecom (HK) Limited, China COSCO Holdings Company Limited, China Resources Enterprise Limited, Guangdong Investment Limited, Kader Holdings Company Limited, Galaxy Entertainment Group Limited (formerly known as K. Wah Construction Materials Limited), Liu Chong Hing Investment Limited, Shui On Construction and Materials Limited, Tian An China Investments Company Limited and Hong Kong Exchanges and Clearing Limited.

## **Compensation**

The aggregate amount of compensation that we paid to our directors and executive officers in 2006 for services performed as directors, officers or employees was approximately HK\$63 million (US\$8.2 million).

We adopted a share option scheme on October 8, 1997, or the Old Scheme, pursuant to which our directors may, at their discretion, invite our employees, including executive directors, or employees of our subsidiaries, to take up options to subscribe for ordinary shares up to a maximum aggregate number of ordinary shares equal to 10% of our total issued share capital.

Pursuant to a resolution passed at the annual general meeting held on June 24, 2002, the Old Scheme was terminated and a new share option scheme, or the Current Scheme, was adopted. The purpose of the Current Scheme is to provide the Company with a flexible and effective means of remunerating and providing benefits to the employees, the executive directors and the non-executive directors of the Company, any of its holdings companies and their respective subsidiaries and any entity in which the Company or any of its subsidiaries holds any equity interest, thereby providing incentives to these participants. Under the Current Scheme, the directors of the Company may, at their discretion, invite the plan participants to take up options to subscribe for the ordinary shares of the Company.

The maximum aggregate number of ordinary shares which can be subscribed pursuant to options that are or may be granted under the above schemes equals to 10% of the total issued share capital of the Company as at the date of adoption of the Current Scheme. Options lapsed or cancelled in accordance with the terms of the Old Scheme or the Current Scheme will not be counted for the purpose of calculating this 10% limit.

As the Old Scheme was terminated with effect on June 24, 2002, no further options were granted under the Old Scheme thereafter. As at December 31, 2006, the total number of ordinary shares which may be issued on the exercise of the outstanding options granted under the Old Scheme is 14,401,300. As at the same date, the total number of ordinary shares which may be issued on the exercise of the outstanding options granted or to be granted under the Current Scheme is 1,559,974,404. No share options were granted under the Current Scheme during the year ended December 31, 2006.

The consideration payable for the grant of option under each of the Old Scheme and the Current Scheme is HK\$1.00. For options granted before September 1, 2001 under the Old Scheme, the exercise price of the options was determined by the directors of the Company at their discretion provided that such price may not be set below a minimum price which is the higher of:

- (i) the nominal value of a share; and



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- (ii) 80% of the average of the closing price of the ordinary share on the Hong Kong Stock Exchange on the five trading days immediately preceding the date on which the option was granted.

For options granted under the Current Scheme, the exercise price of the options are determined by the directors of the Company at their discretion provided that such price may not be set below a minimum price which is the highest of:

- (i) the nominal value of an ordinary share;
- (ii) the closing price of the ordinary shares on the Hong Kong Stock Exchange on the date on which the option was granted; and
- (iii) the average closing price of the ordinary shares on the Hong Kong Stock Exchange for the five trading days immediately preceding the date on which the option was granted.

Under both the Old Scheme and the Current Scheme, the term of the option is determined by the directors at their discretion, provided that all options shall be exercised within 10 years after the adoption of the scheme (in the case of the Old Scheme) and within 10 years after the date on which the option is granted (in the case of the Current Scheme).

As of December 31, 2006, the directors and employees of the Company had options to subscribe for the ordinary shares of the Company granted under both the Old Scheme and, from June 24, 2002 onwards, the Current Scheme. In 2006, 132,654,741 of these options had been exercised. See Share Ownership below for details on options granted to our directors.

## **Board Practices**

To enhance our corporate governance, we have three principal board committees, the audit committee, the remuneration committee and the nomination committee. The audit committee, the remuneration committee and the nomination committee are all comprised solely of independent non-executive directors.

### ***Audit Committee***

The members of our audit committee are Dr. Lo Ka Shui, as chairman of the committee, Mr. Frank K.S. Wong and Mr. Moses M.C. Cheng. The audit committee's major responsibilities include:

to review the financial reports, the related report of independent registered public accounting firm and management's responses to the reports;

to discuss the audit procedures with the independent registered public accounting firm as well as any issues arising out of such procedures;

to review the appointment of the independent registered public accounting firm, the audit and non-audit fees and any matters relating to the termination or resignation of the independent registered public accounting firm; and

to examine the effectiveness of our internal controls, to review our internal audit plan and to submit relevant reports and recommendations to our Board on a regular basis.

The audit committee usually meets four times each year.

### ***Remuneration Committee***

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The members of our remuneration committee are Dr. Lo Ka Shui, as chairman of the committee, Mr. Frank K.S. Wong and Mr. Moses M.C. Cheng. The remuneration committee's major responsibilities include:

to advise the Board in relation to the remuneration structure and payments of our executive directors and executives; and

to represent the Board in confirming the individual remuneration packages and employment terms of executive directors and approving their related employment contracts.

Meetings of the remuneration committee are held at least once a year.

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### ***Nomination Committee***

The members of our nomination committee are Dr. Lo Ka Shui, as chairman of the committee, Mr. Frank K.S. Wong and Mr. Moses M.C. Cheng. The primary responsibilities of the nomination committee include:

to review, advise and make recommendations to the board on the matters in relation to the appointment and re-appointment of board members; and

to ensure the proper and transparent procedures for the appointment and re-appointment of directors.  
Meetings of the nomination committee are held at least once a year.

As a foreign private issuer (as defined in Rule 3b-4 under the Securities Exchange Act of 1934, as amended), we are permitted to follow home country practices in lieu of some of the corporate governance practices required to be followed by U.S. companies listed on the New York Stock Exchange. As a result, our corporate governance practices differ in some respects from those required to be followed by U.S. companies listed on the New York Stock Exchange.

### **Employees**

See Item 4. Information on the Company Business Overview Employees .

### **Share Ownership**

As of December 31, 2006, the following directors and members of our senior management had interests in our share capital:

Under our Memorandum and Articles of Association, our directors and senior management do not have different voting rights when compared to other holders of shares in the same class.

As of December 31, 2006, options exercisable for an aggregate of 9,258,950 shares had been granted to the following directors and members of our senior management under our share option scheme and were outstanding. As of the same date, none of these options had been exercised.

The following options are exercisable at a price of HK\$45.04 per share through October 7, 2007.

|  | <b>Number of shares</b>   |
|--|---------------------------|
| <b>Director</b>  | <b>covered by options</b> |
| Xu Long  | 1,000,000                 |
| The following options are exercisable at a price of HK\$32.10 per share through October 7, 2007. |                           |

|   | <b>Number of shares</b>   |
|---|---------------------------|
| <b>Director</b>   | <b>covered by options</b> |
| Sha Yuejia  | 250                       |
| The following options are exercisable at a price of HK\$22.85 per share from July 3, 2007 through July 2, 2012. |                           |

|                 | Number of shares          |
|-----------------|---------------------------|
| <b>Director</b> | <b>covered by options</b> |
| Xue Taohai      | 100,000                   |
| Sha Yuejia      | 90,000                    |
| Liu Aili        | 90,000                    |
| Xu Long         | 90,000                    |

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The following options are exercisable at a price of HK\$22.75 per share through October 27, 2014:

|                  | Number of shares          |
|------------------|---------------------------|
| <b>Director</b>  | <b>covered by options</b> |
| Li Yue           | 58,000                    |
| Lu Xiangdong     | 58,000                    |
| Xue Taohai       | 58,000                    |
| Zhang Chenshuang | 68,000                    |
| Sha Yuejia       | 27,550                    |
| Liu Aili         | 27,550                    |
| Xu Long          | 39,000                    |

The following options are exercisable at a price of HK\$22.75 per share from October 28, 2007 through October 27, 2014:

|                  | Number of shares          |
|------------------|---------------------------|
| <b>Director</b>  | <b>covered by options</b> |
| Li Yue           | 96,000                    |
| Lu Xiangdong     | 96,000                    |
| Xue Taohai       | 96,000                    |
| Zhang Chenshuang | 96,000                    |
| Sha Yuejia       | 55,050                    |
| Liu Aili         | 55,050                    |
| Xu Long          | 78,000                    |

The following options are exercisable at a price of HK\$26.75 per share through December 20, 2014:

|                 | Number of shares          |
|-----------------|---------------------------|
| <b>Director</b> | <b>covered by options</b> |
| Wang Jianzhou   | 335,000                   |

The following options are exercisable at a price of HK\$26.75 per share from December 21, 2007 through December 20, 2014:

|                 | Number of shares          |
|-----------------|---------------------------|
| <b>Director</b> | <b>covered by options</b> |
| Wang Jianzhou   | 180,000                   |

The following options are exercisable at a price of HK\$34.87 per share through November 7, 2015:

|                 | Number of shares          |
|-----------------|---------------------------|
| <b>Director</b> | <b>covered by options</b> |
| Wang Jianzhou   | 388,000                   |
| Li Yue          | 312,000                   |
| Lu Xiangdong    | 312,000                   |
| Xue Taohai      | 312,000                   |

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|                  |         |
|------------------|---------|
| Zhang Chenshuang | 312,000 |
| Sha Yuejia       | 312,000 |
| Liu Aili         | 51,200  |
| Xu Long          | 92,000  |
| Lo Ka Shui       | 160,000 |
| Frank K.S. Wong  | 160,000 |
| Moses M.C. Cheng | 160,000 |

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The following options are exercisable at a price of HK\$34.87 per share from November 8, 2007 through November 7, 2015:

| <b>Director</b>  | <b>Number of shares<br/>covered by options</b> |
|------------------|--|
| Wang Jianzhou    | 291,000  |
| Li Yue           | 234,000  |
| Lu Xiangdong     | 234,000  |
| Xue Taohai       | 234,000  |
| Zhang Chenshuang | 234,000  |
| Sha Yuejia       | 234,000  |
| Liu Aili         | 45,150   |
| Xu Long          | 81,000   |
| Lo Ka Shui       | 120,000  |
| Frank K.S. Wong  | 120,000  |
| Moses M.C. Cheng | 120,000  |

The following options are exercisable at a price of HK\$34.87 per share from November 8, 2008 through November 7, 2015:

| <b>Director</b>  | <b>Number of shares<br/>covered by options</b> |
|------------------|--|
| Wang Jianzhou    | 291,000  |
| Li Yue           | 234,000  |
| Lu Xiangdong     | 234,000  |
| Xue Taohai       | 234,000  |
| Zhang Chenshuang | 234,000  |
| Sha Yuejia       | 234,000  |
| Liu Aili         | 45,150   |
| Xu Long          | 81,000   |
| Lo Ka Shui       | 120,000  |
| Frank K.S. Wong  | 120,000  |
| Moses M.C. Cheng | 120,000  |

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### **Item 7. Major Shareholders and Related Party Transactions.**

#### **Major Shareholders**

As of May 31, 2007, approximately 74.46% of our outstanding shares were held by China Mobile Hong Kong (BVI) Limited, a wholly-owned subsidiary of China Mobile (Hong Kong) Group Limited. CMCC, a state-owned company, holds all of the voting shares and economic interest in China Mobile (Hong Kong) Group Limited. No other persons own 5% or more of our ordinary shares. Between our initial public offering and May 31, 2007, our majority shareholders held, directly or indirectly, between approximately 74.46% and 76.5% of equity interest in us, except for brief periods following our equity offerings in 1999 and 2000 but before the issuance of consideration shares to our direct shareholder, China Mobile Hong Kong (BVI) Limited, for the related acquisitions, during which periods the shareholding was temporarily lower. See Item 4. Information on the Company Industry Restructuring and Changes in Our Shareholding Structure for changes during the past three years with respect to our majority shareholders. Under our Memorandum and Articles of Association, our major shareholders do not have different voting rights when compared to other holders of shares in the same class.

We are not aware of any arrangement which may at a subsequent date result in a change of control over us.

#### **Related Party Transactions**

As of May 31, 2007, CMCC indirectly owned an aggregate of approximately 74.46% of our issued and outstanding share capital.

We and each of our subsidiaries have entered into various related party transactions. The principal terms of the agreements for these related party transactions are described below.

Certain charges for the services under these agreements are based on tariffs set by the PRC regulatory authorities. Those transactions where the charges are not set by PRC regulatory authorities are based on commercial negotiation between the parties, in each case on an arm's length basis.

#### ***International Roaming Arrangements***

Prior to July 1, 2004, international roaming and international long distance calling charges incurred by an international mobile telecommunications services subscriber making or receiving a call while roaming in Mainland China were collected for us and credited to us by CMCC, and we would make the necessary settlement with the relevant telecommunications operators in Mainland China. CMCC also collected a 15% handling charge on the roaming and international long distance calling charges from the international mobile telecommunications operators and shared such handling charge equally with us. When our subscribers roamed internationally, we would collect the roaming and international long distance calling charges together with a 15% handling charge from our subscribers and would pay the roaming and international long distance calling charges together with half of the handling charge collected to CMCC, which would make the necessary settlement with the international mobile telecommunications operators concerned. Where long distance charges could not be distinguished from base roaming charges, such long distance charges were grouped under roaming charges.

Following the completion of our acquisition of the telecommunication assets from our parent company in July 2004, CMCC no longer provides mobile telecommunications services in Mainland China other than through us. As a result, we no longer have inter-provincial roaming and interconnection arrangement with CMCC and the handling charge with respect to roaming and international long distance calling charges are no longer shared between CMCC and us. In addition, pursuant to an agreement we entered into with CMCC on July 1, 2004 (the International Roaming Settlement Agreement), CMCC maintains the existing settlement arrangements with respect to international interconnection and roaming with the relevant telecommunications services providers in foreign countries and regions, and collects the relevant usage fees and other fees from us and pays the same to the relevant mobile telecommunication service providers in foreign countries and regions.



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### ***Licensing of Trademark***

CMCC is the owner of the CHINA MOBILE name and logo, a registered trademark in Mainland China, Hong Kong, Macau, Taiwan, Brunei, Cambodia, Indonesia, New Zealand, South Korea, Thailand and the United States. In addition, it has filed applications in Bangladesh, Canada, India, Malaysia and Philippines to register the CHINA MOBILE name and logo as a trademark for certain goods and services. In July 2002, we entered into a licensing agreement (the Trademark Licensing Agreement) with CMCC for, among other things, the use of the CHINA MOBILE name and logo by us and our operating subsidiaries. This licensing agreement replaces the previous licensing agreements entered into with CMCC in October 1999 and the supplemental licensing agreement entered into in September 2000. In addition, each of the companies that we acquired in July 2004, other than Jingyi, has entered into a licensing agreement with CMCC (together with the Trademark Licensing Agreement, the Trademark Licensing Agreements) for the use of the CHINA MOBILE name and logo. Under these agreements, no license fee is payable until December 31, 2007.

### ***Spectrum Fees and Numbering Resources***

The Ministry of Information Industry and the Ministry of Finance jointly determine the standardized spectrum fees payable to the Ministry of Information Industry by all mobile telecommunications operators in Mainland China, including us. In accordance with a joint circular from the National Development and Reform Commission and the Ministry of Finance, CMCC entered into an agreement with us that specifies the amount of fees to be paid to the Ministry of Information Industry for spectrum usage by each mobile telecommunications network operator based on the bandwidth of the frequency used and the number of base stations within the relevant operator's networks. In October 1999, we entered into an agreement with CMCC (as supplemented by two supplemental agreements entered into in September 2000 and April 2002), under which we have been granted the exclusive right to use the frequency spectrum and telephone numbers allocated to CMCC in Mainland China. For the usage of the 800/900 MHz and the 1800 MHz frequency bands, the charges will be shared between our operating subsidiaries and CMCC's operating subsidiaries. Sixty percent of the charges will be shared on the basis of the number of base stations at the end of the previous year and 40% of the charges will be shared on the basis of the bandwidth of the spectrum used. The agreement is valid for one year and will be automatically renewed on an annual basis unless either party notifies the other of its intention to terminate at least three months prior to the expiration of the term.

On May 2, 2002, the relevant regulatory authorities in China informed us that the standard spectrum usage fees for GSM networks will be adjusted progressively over a period of three years, and the adjustments will be effective from July 1, 2002 for a period of five years. For the first year, spectrum usage fees for GSM networks will be charged at the annual rate of RMB7.5 million per MHz frequency. For the second year, the annual fee will be RMB11.25 million per MHz frequency and from the third year onward, the annual fee will be RMB15 million per MHz frequency. All adjusted annual fees are charged on the basis that upward and downward frequencies are separately charged. The allocation of spectrum usage fees between CMCC and us remains the same under our existing agreement.

Following the completion of our acquisition of the telecommunications assets from our direct parent company in July 2004, we entered into an agreement with CMCC on July 1, 2004 (the Spectrum and Numbering Resources Agreement), pursuant to which CMCC will collect usage fees from us relating to spectrum frequency and numbering resources and make payment to the Ministry of Information Industry. In addition to transferring to us all existing frequency spectrum and numbering resources allocated to it by the Ministry of Information Industry, CMCC has also agreed to apply for new frequency spectrum and numbering resources upon our request or notice from time to time and transfer the relevant new frequency spectrum and numbering resources to us.

### ***Sharing of Inter-Provincial Transmission Line Leasing Fees***

Following the completion of our acquisition of the telecommunications assets from our direct parent company in July 2004, we entered into an agreement with CMCC on July 1, 2004 (the Inter-Provincial Transmission Line Leasing Settlement Agreement), pursuant to which CMCC maintains the existing settlement arrangements with respect to inter-provincial transmission line leasing with the relevant transmission line providers in Mainland China, and collects inter-provincial transmission line leasing fees from us and pay the same to the transmission line providers in respect of the inter-provincial transmission lines we lease from such providers.

### ***Platform Development***

Aspire is 66.41% owned by us, and it is a joint venture with Vodafone and Hewlett-Packard Company. It entered into a platform development master agreement (the Platform Development Agreement) with CMCC on January 10, 2001. Under the Platform Development Agreement, Aspire (or its subsidiaries) provides technology platform development and maintenance services to CMCC and its then subsidiaries. These services include system and gateway integration services, hardware, software and system development (including development of applications), technical support and major overhaul services for a standardized, nation-wide platform for wireless data.



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Under the Platform Development Agreement, CMCC will pay Aspire equipment charges, systems integration fees, software licensing fees, technical support fees and/or major overhaul charges, which will be determined according to standards laid down by the relevant governmental departments and/or by reference to market rates.

### ***Miscellaneous***

In 2006, there was no consideration passed through CMCC and us under the International Roaming Settlement Agreement, the Trademark Licensing Agreements, the Spectrum and Numbering Resources Agreement and the Inter-Provincial Transmission Line Leasing Settlement Agreement.

The transactions contemplated under the Platform Development Agreement have been entered into in the ordinary course of business and on normal commercial terms. Under the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Hong Kong Listing Rules"), such transactions are considered to be connected transactions and would normally require full disclosure and, in certain circumstances, prior independent shareholders' approval on each occasion they arise. As the transactions contemplated under the Platform Development Agreement are expected to be continued in the normal course of business, our directors consider that such disclosure and approval would be impractical. Accordingly, our directors have requested the Hong Kong Stock Exchange to grant, and the Hong Kong Stock Exchange has granted, waiver from compliance with the normal approval and disclosure requirements related to connected transactions under the Hong Kong Listing Rules which were in force prior to March 31, 2004, which waiver was effective until December 31, 2006, upon the following conditions:

- (1) the transactions as well as the Platform Development Agreement will be (a) entered into in the ordinary and usual course of business on terms that are fair and reasonable so far as our independent shareholders are concerned, and (b) on normal commercial terms and in accordance with the terms of the Platform Development Agreement;
- (2) details of the transactions, as required by rule 14.25(1)(A) to (D) of the Listing Rules, which were in force prior to March 31, 2004, shall be disclosed in our Hong Kong annual report;
- (3) our independent non-executive directors shall review annually the transactions and confirm in our Hong Kong annual report and financial statements for the relevant year that the transactions have been conducted in the manner stated in paragraph (1) above and within the upper limit stated below;
- (4) our auditors shall review annually the transactions and provide our directors with a letter, details of which will be set out in our Hong Kong annual report, stating that the transactions:

received the approval of our board of directors;

are in accordance with the pricing policies as stated in our annual report;

have been conducted in the manner as stated in (1)(b) above; and

have not exceeded the upper limit as set forth in paragraph (7) below;

(5)

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details of the transactions are disclosed to our independent shareholders who shall have voted in favor of an ordinary resolution to approve the connected transaction and the upper limit set out below at our extraordinary general meeting;

(6) CMCC has undertaken to us that our auditors will be granted access to such of its and its associates' accounting records for the purposes of reviewing the transactions mentioned above; and

(7) payments payable by CMCC to Aspire or its subsidiaries in respect of platform development charges in any fiscal year shall not exceed 3% of our consolidated net tangible assets as of the end of such year.

Our independent shareholders approved the connected transactions contemplated under the Platform Development Agreement and the related upper limit at our extraordinary general meeting held on May 15, 2003.

Following the completion of our acquisition of the telecommunications assets from CMCC in July 2004, CMCC no longer provides mobile telecommunications services in Mainland China other than through us. Therefore, the transactions previously entered into between our subsidiaries and prior subsidiaries of CMCC which have been acquired by us no longer constitute connected transactions under the Hong Kong Listing Rules beginning on July 1, 2004 since such prior subsidiaries of CMCC became part of us on July 1, 2004. Only those transactions between us and CMCC or its subsidiaries (which have not been acquired by us) remain as connected transactions under the Hong Kong Listing Rules. In December 2004, in order to streamline the management of the connected transactions, we consolidated the agreements between us and CMCC into two agreements:

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- (i) the Property Leasing Agreement pursuant to which we rent from CMCC various properties for use as business premises and offices, retail outlets and warehouses and CMCC and its subsidiaries provide to us property management services. Under this agreement, for properties owned by CMCC or its subsidiaries, the charges are determined with reference to market rates. For properties leased by CMCC or its subsidiaries from third parties and sublet to us, the charges are determined according to the actual rent payable by CMCC or its subsidiaries together with any tax payable. The payments payable by us to CMCC and its subsidiaries shall not exceed RMB800 million, RMB900 million and RMB1,000 million for the fiscal years ending December 31, 2005, 2006 and 2007, respectively; and
- (ii) the Telecommunications Services Agreement pursuant to which our subsidiaries obtain telecommunications project planning, design and construction services, telecommunications line and pipeline construction services and telecommunications line maintenance services from CMCC and its subsidiaries. Pursuant to the Telecommunications Services Agreement, subsidiaries of CMCC sell transmission towers and spare parts and provide related installation and maintenance services to our subsidiaries. Under this agreement, the charges and prices payable are generally determined with reference to and cannot exceed relevant standards set by and revised from time to time by relevant governmental authorities in Mainland China. Where there are no such standards, the charges and prices are determined with reference to market rates. The payments payable to CMCC and its subsidiaries by us shall not exceed RMB2,500 million for each of the three fiscal years ending December 31, 2007.

The transactions relating to platform development between CMCC and Aspire remain as connected transactions under the Hong Kong Listing Rules, and the charges paid by CMCC to Aspire or its subsidiaries have not exceeded 3% of our consolidated net tangible assets as of December 31, 2006. The platform development charges payable were determined according to standards laid down by the relevant government departments and/or by reference to market rates, and the waiver granted by the Hong Kong Stock Exchange as mentioned in sub-paragraph (7) above that is related to such transactions was effective until December 31, 2006.

We expect that the consideration payable by CMCC to Aspire (or its subsidiaries) under the Platform Development Agreement for the year ending December 31, 2007 will not exceed the de minimis threshold under Rule 14A.33 of the Hong Kong Listing Rules. Accordingly, the Platform Development Agreement is exempt from the reporting, announcement and independent shareholders' approval requirements under Chapter 14A of the Hong Kong Listing Rules.

In February 2007, CMCC, our parent company, acquired 88.86% of the outstanding shares of Paktel Limited, a mobile telecommunications operator in Pakistan, from Millicom International Cellular S.A. Paktel Limited was subsequently renamed CMPak Limited. In May 2007, CMCC acquired the remaining 11.14% of the outstanding shares of CMPak Limited from the minority shareholders of CMPak Limited and, as a result, CMPak Limited became a wholly-owned subsidiary of CMCC. CMCC has indicated that to the extent it decides to transfer or otherwise dispose of its interests in CMPak Limited in the future, it may give us preferential consideration as a potential transferee.

## **Item 8. Financial Information.**

### **Consolidated Financial Statements**

Our audited consolidated financial statements are set forth beginning on page F-1. Other than as disclosed elsewhere in this annual report on Form 20-F, no significant change has occurred since the date of the annual financial statements.

### **Legal Proceedings**

We are not involved in any material litigation, arbitration or administrative proceedings, and, so far as we are aware, we do not have any pending or threatened litigation, arbitration or administrative proceeding that is expected to have a material effect on our financial conditions and results of operation.

### **Policy on Dividend Distributions**

We hold in the highest regard the interests of our shareholders and the returns achieved for them, especially our minority shareholders. In consideration of our favorable operating results in 2006 and our long-term development in the future, and in accordance with our dividend payout plan for the full year of 2006, our board of directors recommended payment of an ordinary final dividend of HK\$0.763 per share for the financial year ended December 31, 2006. This, together with the ordinary interim dividend of HK\$0.62 per share paid during 2006, amounted to an aggregate ordinary dividend payment of HK\$1.383 per share for the full financial year of 2006, representing an increase of 35.6% over the annual dividend of HK\$1.02 per share for the full year of 2005.



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The dividend payout ratio for the year 2006 was 42%. In addition, while the profit and dividend per share for the year 2006 continued to maintain a favorable growth, our board of directors, having taken into full account the interests of our shareholders, recommended payment of a special final dividend in 2006 of HK\$0.069 per share to cater for the effect of our revised depreciation policy on the profit attributable to shareholders. This, together with the special interim dividend of HK\$0.09 per share paid during 2006, amounted to an aggregate special dividend payment of HK\$0.159 per share for the full financial year of 2006. Having taken into account various relevant factors, such as our overall financial condition, our cash flow generating capabilities and our future continuing development needs, we plan that our dividend payout ratio for the full financial year of 2007 will be 43%. In addition, we will consider distributing a special dividend for the year 2007 to cater for the effect of the revision of our depreciation policy in 2007 on the profit attributable to shareholders. Our board of directors believes that our strong free cash flow will be capable of supporting the investments required to maintain our sustained stable growth, while also providing our shareholders with a favorable cash return. We will continue our efforts to achieve a sustainable, steadily increasing dividend over the longer term, with a view to generating the best possible returns for our shareholders.

**Item 9. The Offer and Listing.**

In connection with our initial public offering, our American depositary shares, or ADSs, each representing twenty ordinary shares, were listed and commenced trading on the New York Stock Exchange on October 22, 1997 under the symbol **CHL**. Effective from July 5, 2000, our ADS-to-share ratio has been changed to one-to-five. Our shares were listed and commenced trading on the Hong Kong Stock Exchange on October 23, 1997. Prior to these listings, there was no public market for our equity securities. The New York Stock Exchange and the Hong Kong Stock Exchange are the principal trading markets for our ADSs and ordinary shares, which are not listed on any other exchanges in or outside the United States.

As of December 31, 2006 and May 31, 2007, there were 19,967,815,140 and 19,997,027,813, respectively, ordinary shares issued and outstanding. As of December 31, 2006 and May 31, 2007, there were, respectively, 123 and 133 registered holders of American depositary receipts evidencing 82,182,807 and 100,509,981 ADSs. Since certain of the ADSs are held by nominees, the above number may not be representative of the actual number of U.S. beneficial holders of ADSs or the number of ADSs beneficially held by U.S. persons. The depositary for the ADSs is The Bank of New York.

The high and low closing sale prices of the shares on the Hong Kong Stock Exchange and of the ADSs on the NYSE for the periods indicated are as follows.

|                | Price per Share (HK\$) |       | Price per ADS (US\$) |       |
|----------------|------------------------|-------|----------------------|-------|
|                | High                   | Low   | High                 | Low   |
| <b>2002</b>    | 28.40                  | 17.80 | 17.87                | 11.30 |
| <b>2003</b>    | 23.90                  | 14.85 | 15.54                | 9.30  |
| <b>2004</b>    | 27.85                  | 19.25 | 18.07                | 12.31 |
| <b>2005</b>    | 39.80                  | 23.45 | 25.66                | 14.91 |
| First Quarter  | 26.65                  | 23.45 | 17.10                | 14.91 |
| Second Quarter | 29.70                  | 25.10 | 19.17                | 16.20 |
| Third Quarter  | 38.25                  | 27.55 | 24.86                | 17.93 |
| Fourth Quarter | 39.80                  | 33.80 | 25.66                | 21.70 |
| <b>2006</b>    |                        |       |                      |       |
| First Quarter  | 41.65                  | 35.60 | 26.91                | 22.82 |
| Second Quarter | 46.75                  | 39.45 | 30.93                | 24.76 |
| Third Quarter  | 55.65                  | 44.10 | 36.25                | 27.94 |
| Fourth Quarter | 69.40                  | 55.95 | 44.96                | 35.48 |
| December       | 67.95                  | 61.15 | 44.16                | 39.50 |
| <b>2007</b>    |                        |       |                      |       |
| January        | 77.50                  | 64.70 | 50.65                | 41.85 |
| February       | 79.35                  | 72.40 | 51.39                | 44.16 |
| March          | 73.65                  | 67.00 | 47.08                | 42.59 |
| First Quarter  | 79.35                  | 64.70 | 51.39                | 41.85 |
| April          | 75.70                  | 70.25 | 48.64                | 45.01 |

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|                       |       |       |       |       |
|-----------------------|-------|-------|-------|-------|
| May                   | 74.65 | 70.95 | 48.20 | 44.94 |
| June (through June 6) | 72.85 | 72.20 | 46.51 | 45.96 |



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We may conduct in the future a public offering and listing of our A shares in the PRC, which will be a separate class of our ordinary shares denominated in Renminbi and listed on a PRC stock exchange, although there are no definitive plans for a transaction at this point in time and there is no specific timetable for the offering. We believe that an A share offering would provide us with better access to the capital markets in the PRC and enable our subscribers in the PRC to have an opportunity to become our shareholders. A decision to proceed with such an offering, as well as the precise timing of such an offering, would depend on a number of factors, including the receipt of relevant regulatory approvals and market conditions.

### **Item 10. Additional Information.**

#### **Memorandum and Articles of Association**

Under Section 3 of our Memorandum of Association, we have the capacity and the rights, powers and privileges of a natural person and, in addition and without limit, we may do anything which it is permitted or required to do by any enactment or rule of law.

#### ***Directors***

***Material Interests.*** A director who is in any way directly or indirectly interested in a contract or proposed contract with us shall declare the nature of his interest in accordance with the provisions of the Companies Ordinance (Chapter 32) of Hong Kong and the Articles of Association. A director shall not vote, or be counted in the quorum, on any resolution of the board in respect of any contract or arrangement or proposal in which he or any of his Associates (as such term is defined in the Listing Rules of the Hong Kong Stock Exchange), is to his knowledge, materially interested, and if he shall do so his vote shall not be counted or counted in the quorum for that resolution. The above prohibition shall not apply to any contract, arrangement or proposal:

for the giving by us of any security or indemnity to the director or his Associates in respect of money lent or obligations incurred or undertaken by him or any of them at the request of, or for, our or any of our subsidiaries' benefit;

for the giving by us of any security to a third party in respect of our or any of our subsidiaries' debt or obligation for which the director or his Associates has himself or themselves assumed responsibility or guaranteed or secured in whole or in part whether alone or jointly;

concerning an offer of the shares or debentures or other securities of or by us or any other company which we may promote or be interested in for subscription or purchase where the director or his Associates are, or are to be, interested as a participant in the underwriting or sub-underwriting of the offer;

in which the director or his Associates are interested in the same manner as other holders of our shares or debentures or other securities by virtue only of his or their interest in our shares or debentures or other securities;

concerning any other company in which the director or his Associates are interested, directly or indirectly, as an officer or a shareholder or in which the director or his Associates are beneficially interested in shares of that company other than a company in which the director and any of his Associates, are beneficially interested in five percent or more of the issued shares of any class of the equity share capital of such company (or of any third company through which his interest or that of his Associates is derived) or of the voting rights (excluding for the purpose of calculating such five percent interest any indirect interest of such director or his Associates by virtue of our interest in such company);

for the benefit of our or any of our subsidiaries' employees, including the adoption, modification or operation of a pension fund or retirement, death or disability benefit scheme which relates to both our, or any of our subsidiaries', directors and employees and such directors' Associates and does not give the director or his Associates any privilege not generally accorded to the class of persons to

whom such scheme or fund relates; and

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concerning the adoption, modification or operation of any employees' share scheme involving the issue or grant of options over shares or other securities by us to, or for the benefit of, our or any of our subsidiaries' employees under which the director or his Associates may benefit.

***Compensation and Pension.*** The directors are entitled to receive by way of remuneration for their services such sum as we may determine from time to time in general meeting. The directors are also entitled to be repaid their reasonable traveling, hotel and other expenses incurred by them in or about the performance of their duties as directors. The directors may award special remuneration out of our funds, by way of salary, commission or otherwise as the directors may determine, to any director who performs services which, in the opinion of the directors, are outside the scope of the ordinary duties of a director.

The board may establish and maintain any contributory or non-contributory pension or superannuation funds for the benefit of, or give donations, gratuities, pensions, allowances or emoluments to any persons (1) who are or were at any time in employment or service of our company (or any of our subsidiaries) or are allied or associated with us or any of our subsidiaries, or (2) who are or were at any time our (or any of our subsidiaries') directors or officers, and who are holding or have held any salaried employment or office in our company or any of our subsidiaries, and the wives, widows, families and dependants of any of these persons. Any director holding any such employment or office is entitled to participate in, and retain for his own benefit, any such donation, gratuity, pension, allowance or emolument.

***Borrowing Powers.*** The directors may exercise all the powers of our company to borrow money and to mortgage or charge all or any part of our undertaking, property and assets (present and future) and uncalled capital and to issue debentures, debenture stocks, bonds and other securities, whether outright or as collateral security for the debt, liability or obligation of our company or any third party.

***Qualification; Retirement.*** A director need not hold any of our shares to qualify as a director. There is no age limit requirement for a director's retirement or non-retirement.

Each director is subject to retirement by rotation at least once every three years. The directors to retire in every year shall be those who have been longest in office since their last election, but as between persons who became directors on the same day shall be determined by lot unless they otherwise agree between themselves. The retiring directors shall be eligible for re-election.

### ***Rights Attaching to Ordinary Shares***

The section entitled "Description of Share Capital" in our Registration Statement on Form F-3 (File No. 333-47256), as filed with the Securities and Exchange Commission on October 30, 2000, is incorporated by reference into this annual report on Form 20-F.

Pursuant to ordinary resolutions passed at our extraordinary general meeting held on November 10, 2000, our authorized share capital was increased, by the creation of an additional 14,000,000,000 ordinary shares of HK\$0.10 each, which rank pari passu with the existing ordinary shares, to a total of HK\$3,000,000,000 divided into 30,000,000,000 ordinary shares.

### ***Annual General Meetings and Extraordinary General Meetings***

We must hold, in each year, a general meeting as our annual general meeting in addition to any other meetings in that year. The annual general meeting must be held at such time (which shall be within a period of not more than 15 months, or such longer period as the Registrar of Companies may authorize in writing, after the holding of the last preceding annual general meeting) and place as may be determined by the directors. All other general meetings are extraordinary meetings. The directors may proceed to convene an extraordinary general meeting whenever they think fit, in accordance with the Companies Ordinance.

In general, an annual general meeting and a meeting called for the passing of a special resolution shall be called by not less than 21 days' notice in writing, and any other general meeting shall be called by not less than 14 days' notice in writing. The notice must specify the place, date and time of the meeting and, in the case of special business, the general nature of that business.

### ***Miscellaneous***

We keep our share register with our share registrar, which is Hong Kong Registrars Limited, Shops 1712-1716, 17th Floor, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong. In addition, we also file certain documents with the Registrar of Companies, Hong Kong, China, in accordance with the requirements of the Companies Ordinance. Our company number is 622909.



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### **Material Contracts**

See Item 7. Major Shareholders and Related Party Transactions Related Party Transactions for certain arrangements we have entered into with CMCC.

### ***Interconnection Arrangements***

Each of our operating subsidiaries has entered into interconnection agreements with other operators in its network area. The economic terms of the interconnection arrangements are described under Item 4. Information on the Company Business Overview Interconnection .

### ***Aspire Business Alliance with Vodafone***

On January 9, 2002, Vodafone Americas Asia Inc., a subsidiary of Vodafone, and Aspire entered into a business alliance agreement under which Aspire will engage Vodafone Global Platform and Internet Services, a unit of Vodafone Americas Asia Inc., as a preferred provider of wireless data applications software in relation to the Aspire Mobile Information Service Center Platform, provided that software supplied to Aspire has at least equivalent technical specifications on the same or better commercial terms. Aspire and Vodafone Global Platform and Internet Services also agreed to use their reasonable efforts to coordinate the development of their respective wireless data platforms with the intention of providing a seamless delivery of wireless data services for their respective customers and enabling content and application providers to use a single application programming interface.

### **Exchange Controls**

The Renminbi currently is not a freely convertible currency. The Renminbi is currently freely convertible under the current account , which includes dividends, trade and service-related foreign currency transactions, but not under the capital account , which includes foreign direct investment, unless the prior approval of the State Administration of Foreign Exchange is obtained. The State Administration of Foreign Exchange, under the authority of the People's Bank of China, controls the conversion of Renminbi into foreign currency. In the event of shortages of foreign currencies, we may be unable to convert sufficient Renminbi into a foreign currency to meet our foreign currency obligations or to pay dividends in a foreign currency.

The value of the Renminbi is subject to changes in PRC government policies and to international economic and political developments. Since 1994, the conversion of the Renminbi into foreign currencies, including U.S. dollars, has been based on rates set by the People's Bank of China, which are set daily based on the previous business day's inter-bank foreign exchange market rates and current exchange rates on the world financial markets. From 1994 to July 20, 2005, the official exchange rate for the conversion of the Renminbi to foreign currencies was generally stable. On July 21, 2005, the PRC government introduced a managed floating exchange rate system to allow the value of the Renminbi to fluctuate within a regulated band based on market supply and demand and by reference to a basket of currencies. The PRC government has since made and in the future may make further adjustments to the exchange rate system.

There are no limitations on the right of non-resident or foreign owners to remit dividends or to hold or vote the ordinary shares or the ADSs imposed by Hong Kong law or by our memorandum and articles of association or other constituent documents.

### **Taxation Hong Kong**

The taxation of income and capital gains of holders of ordinary shares or ADSs is subject to the laws and practices of Hong Kong and of jurisdictions in which holders of ordinary shares or ADSs are resident or otherwise subject to tax. The following summary of certain relevant taxation provisions under Hong Kong law is based on current law and practice, is subject to changes therein and does not constitute legal or tax advice. The discussion does not deal with all possible tax consequences relating to an investment in the ordinary shares or ADSs. Accordingly, each prospective investor (particularly those subject to special tax rules, such as banks, dealers, insurance companies, tax-exempt entities and holders of 10% or more of our voting capital stock) should consult its own tax advisor regarding the tax consequences of an investment in the ordinary shares and ADSs. The discussion is based upon laws and relevant interpretations thereof in effect as of the date of this annual report on Form 20-F, all of which are subject to change. There is no reciprocal tax treaty in effect between Hong Kong and the United States.

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### ***Tax on Dividends***

Under the current practices of the Hong Kong Inland Revenue Department, no tax is payable in Hong Kong in respect of dividends paid by us unless such dividends are attributable to a trade, profession or business carried on in Hong Kong.

### ***Profits Tax***

No tax is imposed in Hong Kong in respect of capital gains from the sale of property (such as the ordinary shares and ADSs). Trading gains from the sale of property by persons carrying on a trade, profession or business in Hong Kong where such gains are derived from or arise in Hong Kong from such trade, profession or business will be chargeable to Hong Kong profits tax, which is currently imposed at the rate of 17.5% on corporations and at a maximum rate of 16% on individuals. Gains from sales of the ordinary shares effected on the Hong Kong Stock Exchange may be considered to be derived from or arise in Hong Kong. Liability for Hong Kong profits tax may thus arise in respect of trading gains from sales of ordinary shares or ADSs realized by persons carrying on a business or trading or dealing in securities in Hong Kong.

### ***Stamp Duty***

Hong Kong stamp duty, currently charged at the rate of HK\$1 per HK\$1,000 or part thereof on the higher of the consideration for or the value of the ordinary shares, will be payable by the purchaser on every purchase and by the seller on every sale of ordinary shares (i.e., a total of HK\$2 per HK\$1,000 or part thereof is currently payable on a typical sale and purchase transaction involving ordinary shares). In addition, a fixed duty of HK\$5 is currently payable on any instrument of transfer of ordinary shares. The withdrawal of ordinary shares upon the surrender of ADSs, and the issuance of ADSs upon the deposit of ordinary shares, will also attract stamp duty at the rate described above for sale and purchase transactions unless the withdrawal or deposit does not result in a change in the beneficial ownership of the ordinary shares under Hong Kong law, in which case only a fixed duty of HK\$5 is payable on the transfer. The issuance of the ADSs upon the deposit of ordinary shares issued directly to the depositary or for the account of the depositary does not attract stamp duty. No Hong Kong stamp duty is payable upon the transfer of ADSs outside Hong Kong.

### ***Estate Duty***

The Revenue (Abolition of Estate Duty) Ordinance 2005 came into effect on February 11, 2006 in Hong Kong. No Hong Kong estate duty is payable and no estate duty clearance papers are needed for an application for a grant of representation in respect of holders of ordinary shares whose death occurs on or after February 11, 2006.

## **Taxation United States Federal Income Taxation**

This section describes the material United States federal income tax consequences of the ownership and disposition of our shares or ADSs. This section applies to you only if you are a U.S. holder, as defined below, and you hold your shares or ADSs as capital assets for United States federal income tax purposes. This section does not apply to you if you are a member of a special class of holders subject to special rules, including:

a dealer in securities;

a trader in securities that elects to use a mark-to-market method of accounting for your securities holdings;

a tax-exempt organization;

a life insurance company;

a person liable for alternative minimum tax;

a person that actually or constructively owns 10% or more of our voting stock;

a person that holds shares or ADSs as part of a straddle or a hedging or conversion transaction; or

a person whose functional currency is not the U.S. dollar.

This section is based on the Internal Revenue Code of 1986, as amended, its legislative history, existing and proposed regulations, published rulings and court decisions, all as currently in effect. These laws are subject to change, possibly on a retroactive basis. In addition, this section is based in part upon the representations of The Bank of New York, as depositary, and the assumption that each obligation in the Deposit Agreement among us, The Bank of New York, as depositary, and owners and beneficial owners of ADRs issued thereunder, and any related agreement will be performed in accordance with its terms.

You are a U.S. holder if you are a beneficial owner of shares or ADSs and you are:

a citizen or resident of the United States;

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a domestic corporation;

an estate whose income is subject to United States federal income tax regardless of its source; or

a trust if a United States court can exercise primary supervision over the trust's administration and one or more United States persons are authorized to control all substantial decisions of the trust.

*You should consult your own tax advisor regarding the United States federal, state and local and other tax consequences of owning and disposing of shares or ADSs in your particular circumstances.*

In general, and taking into account the earlier assumptions, for United States federal income tax purposes, if you hold ADRs evidencing ADSs, you will be treated as the owner of the shares represented by those ADRs. Exchanges of shares for ADRs, and ADRs for shares, generally will not be subject to the United States federal income tax.

### ***Taxation of Dividends***

Under the United States federal income tax laws, and subject to the passive foreign investment company, or PFIC, rules discussed below, if you are a U.S. holder, the gross amount of any dividend we pay out of our current or accumulated earnings and profits (as determined for United States federal income tax purposes) is subject to United States federal taxation. If you are a noncorporate U.S. holder, dividends paid to you in taxable years beginning before January 1, 2011 that constitute qualified dividend income will be taxable to you at a maximum tax rate of 15% provided that you hold the shares or ADSs for more than 60 days during the 121-day period beginning 60 days before the ex-dividend date and meet other holding period requirements.

The dividend is taxable to you when you, in the case of shares, or The Bank of New York, as depositary, in the case of ADSs, receive the dividend, actually or constructively. The dividend will not be eligible for the dividends-received deduction generally allowed to United States corporations in respect of dividends received from other United States corporations. The amount of the dividend distribution that you must include in your income will be the U.S. dollar value of the Hong Kong dollar payments made, determined at the spot Hong Kong dollar/U.S. dollar rate on the date the dividend distribution is includible in your income, regardless of whether the payment is in fact converted into U.S. dollars. Generally, any gain or loss resulting from currency exchange fluctuations during the period from the date you include the dividend payment in income to the date you convert the payment into U.S. dollars will be treated as ordinary income or loss and will not be eligible for the special tax rate applicable to qualified dividend income. This gain or loss generally will be from sources within the United States for foreign tax credit limitation purposes. Distributions in excess of current and accumulated earnings and profits (as determined for United States federal income tax purposes) will be treated as a non-taxable return of capital to the extent of your basis in the shares or ADSs and thereafter as capital gain. Dividends will be income from sources outside the United States, but dividends paid in taxable years beginning before January 1, 2007 generally will be passive or financial services income, and dividends paid in taxable years beginning after December 31, 2006 will, depending on your circumstances, be passive or general income which, in either case, is treated separately from other types of income for purposes of computing the foreign tax credit allowable to you.

### ***Taxation of Capital Gains***

Subject to the PFIC rules discussed below, if you are a U.S. holder and you sell or otherwise dispose of your shares or ADSs, you will recognize capital gain or loss for United States federal income tax purposes equal to the difference between the U.S. dollar value of the amount that you realize and your tax basis, determined in U.S. dollars, in your shares or ADSs. Capital gain of a noncorporate U.S. holder that is recognized in taxable years beginning before January 1, 2011 is generally taxed at a maximum rate of 15% where the property is held more than one year. The deductibility of capital losses is subject to limitations. The gain or loss will generally be from sources within the United States for foreign tax credit limitation purposes.

### ***PFIC Rules***

We believe that shares or ADSs should not be treated as stock of a PFIC for United States federal income tax purposes, but this conclusion is a factual determination that is made annually and thus may be subject to change. In general, if you are a U.S. holder, we will be a PFIC with respect to you if for any taxable year in which you held our shares or ADSs:



at least 75% of our gross income for the taxable year is passive income; or

at least 50% of the value, determined on the basis of a quarterly average, of our assets is attributable to assets that produce or are held for the production of passive income.

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Passive income generally includes dividends, interest, royalties, rents (other than certain rents and royalties derived in the active conduct of a trade or business), annuities and gains from assets that produce passive income. If a foreign corporation owns at least 25% by value of the stock of another corporation, the foreign corporation is treated for purposes of the PFIC tests as owning its proportionate share of the assets of the other corporation, and as receiving directly its proportionate share of the other corporation's income.

If we are treated as a PFIC, and you are a U.S. holder that did not make a mark-to-market election, as described below, you will be subject to special rules with respect to:

any gain you realize on the sale or other disposition of your shares or ADSs; and

any excess distribution that we make to you (generally, any distributions to you during a single taxable year that are greater than 125% of the average annual distributions received by you in respect of the shares or ADSs during the three preceding taxable years or, if shorter, your holding period for the shares or ADSs).

Under these rules:

the gain or excess distribution will be allocated ratably over your holding period for the shares or ADSs;

the amount allocated to the taxable year in which you realized the gain or excess distribution will be taxed as ordinary income;

the amount allocated to each prior year, with certain exceptions, will be taxed at the highest tax rate in effect for that year; and

the interest charge generally applicable to underpayments of tax will be imposed in respect of the tax attributable to each such year. If you own shares or ADSs in a PFIC that are treated as marketable stock, you may make a mark-to-market election. If you make this election, you will not be subject to the PFIC rules described above. Instead, in general, you will include as ordinary income each year the excess, if any, of the fair market value of your shares or ADSs at the end of the taxable year over your adjusted basis in your shares or ADSs. These amounts of ordinary income will not be eligible for the favorable tax rates applicable to qualified dividend income on long-term capital gains. You will also be allowed to take an ordinary loss in respect of the excess, if any, of the adjusted basis of your shares or ADSs over their fair market value at the end of the taxable year (but only to the extent of the net amount of previously included income as a result of the mark-to-market election). Your basis in the shares or ADSs will be adjusted to reflect any such income or loss amounts.

In addition, notwithstanding any election you make with regard to the shares or ADSs, dividends that you receive from us will not constitute qualified dividend income to you if we are a PFIC either in the taxable year of the distribution or the preceding taxable year. Moreover, your shares or ADSs will be treated as stock in a PFIC if we were a PFIC at any time during your holding period in your shares or ADSs, even if we are not currently a PFIC. For purposes of this rule, if you make a mark-to-market election with respect to your shares or ADSs, you will be treated as having a new holding period in your shares or ADSs beginning on the first day of the first taxable year beginning after the last taxable year for which the mark-to-market election applies. Dividends that you receive that do not constitute qualified dividend income are not eligible for taxation at the 15% maximum rate applicable to qualified dividend income. Instead, you must include the gross amount of any such dividend paid by us out of our accumulated earnings and profits (as determined for United States federal income tax purposes) in your gross income, and it will be subject to tax at rates applicable to ordinary income.

If you own shares or ADSs during any year that we are a PFIC, you must file Internal Revenue Service Form 8621.

## **Documents on Display**

You may read and copy documents referred to in this annual report on Form 20-F that have been filed with the SEC at the SEC's public reference room located at 100 F Street, N.E., Room 1580, Washington, D.C. 20549. Please call the SEC at 1-800-SEC-0330 for further information on the

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public reference room and its copy charges. The SEC also maintains a web site at [www.sec.gov](http://www.sec.gov) that contains reports, proxy statements and other information regarding registrants that file electronically with the SEC.

The SEC allows us to incorporate by reference the information we file with the SEC. This means that we can disclose important information to you by referring you to another document filed separately with the SEC. The information incorporated by reference is considered to be part of this annual report on Form 20-F.

**Table of Contents****Item 11. Quantitative and Qualitative Disclosures About Market Risk.**

We are subject to market rate risks due to fluctuations in interest rates. The majority of our debt is in the form of long-term loans with original maturities ranging from one to fifteen years. Accordingly, fluctuations in interest rates can lead to significant fluctuations in the fair value of these debt instruments. From time to time, we may enter into interest rate swap agreements designed to mitigate our exposure to interest rate risks, although we did not consider it necessary to do so in 2006.

We are also exposed to foreign currency risk as a result of our telecommunications equipment being sourced substantially from overseas suppliers. Specifically, our foreign currency exposure relates primarily to our firm purchase commitments and, to a limited extent, cash and cash equivalents denominated in foreign currencies. We have entered into foreign exchange forward contracts designed to mitigate our exposure to foreign currency risks. As of December 31, 2006, we had no foreign exchange forward contracts outstanding. Our foreign currency hedging activity generally is expected to be limited to hedging of specific future commitments in foreign currencies.

The following table provides information regarding our interest rate-sensitive financial instruments, which consist of fixed and variable rate short-term and long-term debt obligations, as of December 31, 2006 and 2005.

|   | Expected Maturity Date |      |      |      |       |            | As of December 31, |        | As of December 31, |            |
|---|------------------------|------|------|------|-------|------------|--------------------|--------|--------------------|------------|
|   |                        |      |      |      |       |            | 2006               |        | 2005               |            |
|   |                        |      |      |      |       |            | Total              |        | Total              |            |
|   |                        |      |      |      |       |            | Recorded           | Fair   | Recorded           | Fair       |
|   | 2007                   | 2008 | 2009 | 2010 | 2011  | Thereafter | Amount             | Value  | Amount             | Fair Value |
| (RMB equivalent in millions, except interest rates) |                        |      |      |      |       |            |                    |        |                    |            |
| Debt:   |                        |      |      |      |       |            |                    |        |                    |            |
| Obligations under capital leases                    | 68                     |      |      |      |       |            | 68                 | 68     | 68                 | 68         |
| Average interest rate                               | 4.96%                  |      |      |      |       |            | 4.96%              |        | 4.96%              |            |
| Bonds   | 2,996                  |      |      |      | 4,967 | 4,974      | 12,937             | 13,218 | 12,912             | 13,685     |
| Average interest rate                               | 3.50%                  |      |      |      | 4.81% | 4.50%      | 4.13%              |        | 3.97%              |            |
| Deferred payable                                    |                        |      |      |      |       | 23,633     | 23,633             | 23,633 | 23,633             | 23,633     |
| Average interest rate                               |                        |      |      |      |       | 5.41%      | 4.11%              |        | 2.74%              |            |

The following table provides information regarding our foreign currency-sensitive financial instruments and transactions, which consist of deposits with banks and cash and cash equivalents as of December 31, 2006 and 2005.

|   | Expected Maturity Date |       |      |      |      |            | As of December 31, |       | As of December 31, |       |
|---|------------------------|-------|------|------|------|------------|--------------------|-------|--------------------|-------|
|   |                        |       |      |      |      |            | 2006               |       | 2005               |       |
|   |                        |       |      |      |      |            | Total              |       | Total              |       |
|   |                        |       |      |      |      |            | Recorded           | Fair  | Recorded           | Fair  |
|   | 2007                   | 2008  | 2009 | 2010 | 2011 | Thereafter | Amount             | Value | Amount             | Value |
| (RMB equivalent in millions, except interest rates) |                        |       |      |      |      |            |                    |       |                    |       |
| On-balance sheet financial instruments              |                        |       |      |      |      |            |                    |       |                    |       |
| Deposits with banks:                                |                        |       |      |      |      |            |                    |       |                    |       |
| in U.S. dollars                                     |                        | 276   |      |      |      |            | 276                | 276   | 17                 | 17    |
| in Hong Kong dollars                                |                        |       |      |      |      |            |                    |       | 134                | 134   |
| Cash and cash equivalents:                          |                        |       |      |      |      |            |                    |       |                    |       |
| in U.S. dollars                                     |                        | 511   |      |      |      |            | 511                | 511   | 567                | 567   |
| in Hong Kong dollars                                |                        | 5,091 |      |      |      |            | 5,091              | 5,091 | 4,266              | 4,266 |

**Item 12. Description of Securities Other than Equity Securities.**

Not Applicable.

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**PART II**

**Item 13. Defaults, Dividend Arrearages and Delinquencies.**

None.

**Item 14. Material Modifications to the Rights of Security Holders and Use of Proceeds.**

None.

**Item 15. Controls and Procedures.**

*Disclosure Controls and Procedures.* As of December 31, 2006, an evaluation was carried out by our management, with the participation of our Chief Executive Officer and Chief Financial Officer, of the effectiveness of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934, as amended). Based on that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that, as of the end of the period covered by this annual report on Form 20-F, our disclosure controls and procedures were effective at a reasonable assurance level.

*Management's Annual Report on Internal Control Over Financial Reporting.* Management's Report on Internal Control Over Financial Reporting is set forth below.

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**Management's Report on Internal Control Over Financial Reporting**

Management of China Mobile Limited (together with its consolidated subsidiaries, the Company) is responsible for establishing and maintaining adequate internal control over financial reporting (as defined in Rule 13a-15(f) under the Securities Exchange Act of 1934, as amended). The Company's internal control over financial reporting is a process designed under the supervision of the Company's Chief Executive Officer and Chief Financial Officer to provide reasonable assurance regarding the reliability of financial reporting and the preparation of the Company's financial statements for external reporting purposes in accordance with Hong Kong Financial Reporting Standards and the required reconciliation to U.S. generally accepted accounting principles.

As of December 31, 2006, the Company's management conducted an assessment of the effectiveness of the Company's internal control over financial reporting based on the framework established in Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on this assessment, the Company's management has concluded that the Company's internal control over financial reporting as of December 31, 2006 was effective.

Management's assessment of the effectiveness of the Company's internal control over financial reporting as of December 31, 2006 has been audited by KPMG, an independent registered public accounting firm, as stated in their report appearing on page 70, which expresses unqualified opinions on management's assessment and on the effectiveness of the Company's internal control over financial reporting as of December 31, 2006.

/s/ WANG Jianzhou  
Name: WANG Jianzhou  
Title: Chairman and Chief Executive Officer

/s/ XUE Taohai  
Name: XUE Taohai  
Title: Executive Director, Vice President and  
Chief Financial Officer

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**Attestation Report of Independent Registered Public Accounting Firm**

The Board of Directors and Shareholders of

China Mobile Limited:

We have audited management's assessment, included in the accompanying Management's Report on Internal Control Over Financial Reporting, that China Mobile Limited maintained effective internal control over financial reporting as of December 31, 2006, based on criteria established in Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). China Mobile Limited's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management's assessment and an opinion on the effectiveness of the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, evaluating management's assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that: (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, management's assessment that China Mobile Limited maintained effective internal control over financial reporting as of December 31, 2006 is fairly stated, in all material respects, based on criteria established in Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Also, in our opinion, China Mobile Limited maintained, in all material respects, effective internal control over financial reporting as of December 31, 2006, based on criteria established in Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of China Mobile Limited and subsidiaries as of December 31, 2005 and 2006, and consolidated statements of income, equity and cash flows for each of the years in the three-year period ended December 31, 2006, and our report dated June 8, 2007 expressed an unqualified opinion on those consolidated financial statements.

/s/ KPMG

Hong Kong

June 8, 2007



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*Changes in Internal Control Over Financial Reporting.* During 2006, no change to our internal control over financial reporting occurred that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

**Item 16A. Audit Committee Financial Expert.**

All members of our audit committee have extensive management experience. In particular, one of the members has many years of finance and commercial management experience and expertise. However, members of our audit committee do not possess direct experience or expertise in respect of the reconciliation of financial statements with U.S. GAAP and the evaluation of reports filed with the SEC by SEC-reporting issuers. Our board of directors has determined that we do not currently have an audit committee financial expert, as defined in Item 16A(b) of Form 20-F, serving on our audit committee. Our audit committee may consider appointing, from time to time, an external financial expert as a consultant.

**Item 16B. Code of Ethics.**

We have adopted a code of ethics that applies to our Chief Executive Officer, Chief Financial Officer, Deputy Chief Financial Officer, Assistant Chief Financial Officer and our other designated senior officers. A copy of our Code of Ethics for Covered Officers was filed as Exhibit 11.1 to our annual report on Form 20-F for the fiscal year ended December 31, 2003, and may also be downloaded from our website at [www.ChinaMobileLtd.com/images/pdf/terms/CodeofEthics\\_eng.pdf](http://www.ChinaMobileLtd.com/images/pdf/terms/CodeofEthics_eng.pdf). Information contained on that website is not a part of this annual report on Form 20-F. Copies of our Code of Ethics for Covered Officers may also be obtained at no charge by writing to our investor relations department at 60/F, The Center, 99 Queen's Road Central, Hong Kong.

**Item 16C. Principal Accountant Fees and Services.**

The following table sets forth the aggregate audit fees, audit-related fees, tax fees of our principal accountants and all other fees billed for products and services provided by our principal accountants other than the audit fees, audit-related fees and tax fees for each of the years ended December 31, 2005 and 2006:

|      | Audit Fees                     | Audit-Related Fees | Tax Fees    | All Other Fees                |
|------|--------------------------------|--------------------|-------------|-------------------------------|
| 2005 | US\$ 7,606,000                 |                    | US\$ 3,000  | US\$ 77,000                   |
| 2006 | US\$ 10,254,000 <sup>(1)</sup> |                    | US\$ 19,000 | US\$ 4,510,000 <sup>(2)</sup> |

(1) Includes the fees for services rendered in connection with the audit of internal control over financial reporting as required by Section 404 of the Sarbanes-Oxley Act of 2002.

(2) Includes the fees for Sarbanes-Oxley Act of 2002 advisory services provided to us.

Before our principal accountants were engaged by us or our subsidiaries to render audit or non-audit services, the engagement was approved by our audit committee as required by applicable rules and regulations of the SEC.

**Item 16D. Exemptions from the Listing Standards for Audit Committees.**

Not applicable.

**Item 16E. Purchases of Equity Securities by the Issuer and Affiliated Purchasers.**

None.

**Table of Contents****PART III****Item 17. Financial Statements.**

The Company has elected to provide the financial statements and related information specified in Item 18 in lieu of Item 17.

**Item 18. Financial Statements.**

The following financial statements are filed as part of this annual report on Form 20-F.

**China Mobile Limited:**

|   |      |
|---|------|
| <u>Index to Consolidated Financial Statements</u>   | F-1  |
| <u>Report of Independent Registered Public Accounting Firm</u>  | F-2  |
| <u>Consolidated Statements of Income for Each of the Three Years Ended December 31, 2004, 2005 and 2006</u>     | F-3  |
| <u>Consolidated Balance Sheets as of December 31, 2005 and 2006</u>   | F-5  |
| <u>Consolidated Statements of Cash Flows for Each of the Three Years Ended December 31, 2004, 2005 and 2006</u> | F-7  |
| <u>Consolidated Statements of Equity for Each of the Three Years Ended December 31, 2004, 2005 and 2006</u>     | F-11 |
| <u>Notes to Consolidated Financial Statements</u>   | F-12 |

**Item 19. Exhibits.**

(a) See Item 18 for a list of the financial statements filed as part of this annual report on Form 20-F.

(b) Exhibits to this annual report on Form 20-F:

| <b>Exhibit Number</b> | <b>Description of Exhibit</b>  |
|-----------------------|--|
| 1.1                   | Memorandum and Articles of Association (as amended). <sup>(1)</sup>  |
| 2.1                   | We agree to provide the SEC, upon request, copies of instruments defining the rights of holders of our long-term debt.   |
| 2.2                   | Guarantee from China Mobile Communications Corporation for the RMB5,000 million guaranteed bonds due 2011 issued by Guangdong Mobile. <sup>(2)</sup>   |
| 2.3                   | Letter of Guarantee from China Mobile Communications Corporation for the RMB3,000 million guaranteed bonds due 2007 and RMB5,000 million guaranteed bonds due 2017, both issued by Guangdong Mobile in 2002 (with English translation). <sup>(3)</sup>   |
| 4.1                   | Agreement regarding Settlement of Interconnection and Roaming, Transmission Line Leasing, Usage of Spectrum Frequency and Numbering Resources, dated July 1, 2004, between China Mobile (Hong Kong) Limited and China Mobile Communications Corporation (with English translation). <sup>(4)</sup> |
| 4.2                   | Tax Indemnity, dated July 1, 2004, among China Mobile Hong Kong (BVI) Limited, China Mobile (Hong Kong) Limited and China Mobile Communications Corporation. <sup>(4)</sup>  |
| 4.3                   | Agreement on Use of Premises and Related Management Services, dated December 30, 2004, between China Mobile (Hong Kong) Limited and China Mobile Communications Corporation (with English translation). <sup>(4)</sup>   |
| 4.4                   | Telecommunications Services Agreement, dated December 30, 2004, between China Mobile (Hong Kong) Limited and China Mobile Communications Corporation (with English translation). <sup>(4)</sup>  |

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### **Exhibit**

| <b>Number</b> | <b>Description of Exhibit</b>  |
|---------------|--|
| 4.5           | Conditional Sale and Purchase Agreement, dated April 28, 2004 between China Mobile (Hong Kong) Limited, China Mobile Hong Kong (BVI) Limited and China Mobile Communications Corporation. <sup>(5)</sup>   |
| 4.6           | Asset Injection Agreement, dated April 9, 2004, between China Mobile Communications Corporation, Neimenggu Mobile and Neimenggu Communication Service Company (with English translation and schedule). <sup>(5)</sup>  |
| 4.7           | Asset Injection Agreement, dated April 9, 2004, between China Mobile Communications Corporation, China Mobile Group Design Institute Co., Ltd. and Beijing P&T Consulting & Design Institute (with English translation). <sup>(5)</sup>  |
| 4.8           | Asset Injection Agreement, dated April 9, 2004, between China Mobile Communications Corporation and China Mobile Communication Company Limited (with English translation). <sup>(5)</sup>  |
| 4.9           | Agreement on the Confirmation of Rights and Obligations, dated April 9, 2004, between China Mobile Communications Corporation, Neimenggu Mobile and Neimenggu Communication Service Company (with English translation and schedule). <sup>(5)</sup>  |
| 4.10          | Agreement on the Confirmation of Rights and Obligations, dated April 9, 2004, between China Mobile Communications Corporation, China Mobile Group Design Institute Co., Ltd. and Beijing P&T Consulting & Design Institute (with English translation). <sup>(5)</sup>  |
| 4.11          | Consent Letter to the Substitution of Borrowers under the Consigned Loan Agreement, dated February 13, 2004, between China Mobile Communications Corporation, Neimenggu Mobile, Neimenggu Communication Service Company and Beijing Chang an Sub-branch of Industrial and Commercial Bank of China (with English translation and schedule). <sup>(5)</sup> |
| 4.12          | Agreement on Sharing of Administrative Services and Administrative Costs, dated April 27, 2004, between China Mobile Communication Co., Ltd. and China Mobile Communications Corporation (with English translation). <sup>(5)</sup>  |
| 4.13          | Trademark Licensing Agreement, dated April 23, 2004, between China Mobile Communications Corporation and China Mobile Communication Co., Ltd. (with English translation). <sup>(5)</sup>   |
| 4.14          | Trademark License Agreement, dated July 18, 2002, between China Mobile Communications Corporation and China Mobile (Hong Kong) Limited (with English translation). <sup>(3)</sup>  |
| 4.15          | Tax Indemnity dated July 1, 2002 between China Mobile Hong Kong (BVI) Limited, China Mobile (Hong Kong) Limited and China Mobile Communications Corporation. <sup>(3)</sup>  |
| 4.16          | Co-operation Framework Agreement in respect of Indirect Loan dated May 10, 2002 between China Mobile Communications Corporation and China Mobile (Hong Kong) Limited (with English translation). <sup>(3)</sup>  |
| 4.17          | Agreement on the Sales and Maintenance of Masts and Maintenance of Antennas and Feeder Lines, dated August 1, 2000, between Hebei Mobile and Hebei Provincial Posts and Telecommunications Equipment and Machinery Plant. <sup>(6)</sup>   |
| 8.1           | List of Major Subsidiaries.  |
| 11.1          | Code of Ethics. <sup>(5)</sup>   |
| 12.1          | Certification of Chief Executive Officer pursuant to Rule 13a-14(a).   |
| 12.2          | Certification of Chief Financial Officer pursuant to Rule 13a-14(a).   |
| 13.1          | Certification of Chief Executive Officer pursuant to Rule 13a-14(b).   |
| 13.2          | Certification of Chief Financial Officer pursuant to Rule 13a-14(b).   |

---

(1) Incorporated by reference to our Annual Report on Form 20-F for the fiscal year ended December 31, 2005 (File No. 1-14696), filed with the SEC on June 9, 2006.

(2) Incorporated by reference to our Annual Report on Form 20-F for the fiscal year ended December 31, 2000 (File No. 1-14696), filed with the SEC on June 26, 2001.

(3) Incorporated by reference to our Annual Report on Form 20-F for the fiscal year ended December 31, 2002 (File No. 1-14696), filed with the SEC on June 17, 2003.



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- (4) Incorporated by reference to our Annual Report on Form 20-F for the fiscal year ended December 31, 2004 (File No. 1-14696), filed with the SEC on June 13, 2005.
- (5) Incorporated by reference to our Annual Report on Form 20-F for the fiscal year ended December 31, 2003 (File No. 1-14696), filed with the SEC on June 17, 2004.
- (6) Incorporated by reference to our Registration Statement on Form F-3 (File No. 333-47256), filed with the SEC on October 30, 2000.

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**SIGNATURES**

The registrant hereby certifies that it meets all of the requirements for filing on Form 20-F and that it has duly caused and authorized the undersigned to sign this annual report on Form 20-F on its behalf.

**CHINA MOBILE LIMITED**

By: /s/ WANG Jianzhou

Name: WANG Jianzhou

Title: Chairman and Chief Executive Officer

Date: June 12, 2007

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**Exhibit Index**

**Exhibit**

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| <u>Consolidated Balance Sheets as of December 31, 2005 and 2006</u>   | F-5                    |
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| <u>Consolidated Statements of Equity for Each of the Three Years Ended December 31, 2004, 2005 and 2006</u>     | F-11                   |
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Report of Independent Registered Public Accounting Firm

The Board of Directors and Shareholders of

China Mobile Limited:

We have audited the accompanying consolidated balance sheets of China Mobile Limited (the Company) and subsidiaries (together referred to as the Group) as of December 31, 2005 and 2006 and the related consolidated statements of income, equity, and cash flows for each of the years in the three-year period ended December 31, 2006, all expressed in Renminbi. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States) and generally accepted auditing standards in Hong Kong. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Group as of December 31, 2005 and 2006, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2006 in conformity with accounting principles generally accepted in Hong Kong.

Accounting principles generally accepted in Hong Kong vary in certain material respects from accounting principles generally accepted in the United States of America. Information relating to the nature and effect of such differences is presented in note 40 to the consolidated financial statements.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of China Mobile Limited's internal control over financial reporting as of December 31, 2006, based on criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated June 8, 2007 expressed an unqualified opinion on management's assessment of, and the effective operation of, internal control over financial reporting.

/s/ KPMG

Hong Kong

June 8, 2007

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## Consolidated Statements of Income

*(Amounts in millions, except share data)*

|                                    |             | <i>Year ended December 31,</i> |             |             |
|------------------------------------|-------------|--------------------------------|-------------|-------------|
|                                    | <i>Note</i> | <i>2004</i>                    | <i>2005</i> | <i>2006</i> |
|                                    |             | <b>RMB</b>                     | <b>RMB</b>  | <b>RMB</b>  |
| <b>Operating revenue</b>           |             |                                |             |             |
| Usage fees                         |             | 128,534                        | 156,710     | 189,710     |
| Monthly fees                       |             | 24,760                         | 25,055      | 21,629      |
| Value-added services fees          |             | 30,236                         | 50,187      | 69,309      |
| Other operating revenue            |             | 8,851                          | 11,089      | 14,710      |
| <b>Total operating revenue</b>     | 4           | 192,381                        | 243,041     | 295,358     |
| <b>Operating expenses</b>          |             |                                |             |             |
| Leased lines                       |             | 3,861                          | 3,224       | 2,451       |
| Interconnection                    |             | 12,072                         | 15,309      | 18,783      |
| Depreciation                       |             | 44,186                         | 56,368      | 64,574      |
| Personnel                          |             | 9,972                          | 14,200      | 16,853      |
| Other operating expenses           |             | 62,811                         | 80,254      | 100,772     |
| <b>Total operating expenses</b>    | 5           | 132,902                        | 169,355     | 203,433     |
| <b>Profit from operations</b>      |             | 59,479                         | 73,686      | 91,925      |
| <b>Amortization of goodwill</b>    |             | (1,930)                        |             |             |
| <b>Other net income</b>            | 6           | 3,167                          | 3,284       | 2,872       |
| <b>Non-operating net income</b>    | 7           | 900                            | 1,025       | 1,017       |
| <b>Interest income</b>             |             | 1,014                          | 1,615       | 2,604       |
| <b>Finance costs</b>               | 8           | (1,679)                        | (1,346)     | (1,510)     |
| <b>Profit before tax</b>           |             | 60,951                         | 78,264      | 96,908      |
| <b>Income tax</b>                  | 11          | (19,180)                       | (24,675)    | (30,794)    |
| <b>Profit for the year</b>         |             | 41,771                         | 53,589      | 66,114      |
| <b>Attributable to:</b>            |             |                                |             |             |
| Equity shareholders of the Company |             | 41,749                         | 53,549      | 66,026      |
| Minority interests                 |             | 22                             | 40          | 88          |
| <b>Profit for the year</b>         |             | 41,771                         | 53,589      | 66,114      |

See accompanying notes to consolidated financial statements.

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## Consolidated Statements of Income (continued)

*(Amounts in millions, except share data)*

|   |             | <i>Year ended December 31,</i> |             |             |
|---|-------------|--------------------------------|-------------|-------------|
|   | <i>Note</i> | <i>2004</i>                    | <i>2005</i> | <i>2006</i> |
|   |             | <b>RMB</b>                     | <b>RMB</b>  | <b>RMB</b>  |
| <b>Dividends payable to equity shareholders of the Company attributable to the year:</b>              |             |                                |             |             |
| Ordinary interim dividend declared and paid during the year   | 12          | 4,175                          | 9,259       | 12,612      |
| Special interim dividend declared and paid during the year  | 12          |                                |             | 1,831       |
| Ordinary final dividend proposed after the balance sheet date   | 12          | 9,614                          | 11,767      | 15,327      |
| Special final dividend proposed after the balance sheet date  | 12          |                                |             | 1,386       |
|   |             | 13,789                         | 21,026      | 31,156      |
| <b>Basic net income per share</b>   | 2(v)        | RMB2.12                        | RMB2.71     | RMB3.32     |
| <b>Weighted average number of shares used in calculating basic net income per share (thousands)</b>   |             | 19,673,185                     | 19,738,229  | 19,892,968  |
| <b>Diluted net income per share</b>   | 2(v)        | RMB2.12                        | RMB2.70     | RMB3.29     |
| <b>Weighted average number of shares used in calculating diluted net income per share (thousands)</b> |             | 19,774,093                     | 19,892,163  | 20,078,549  |

See accompanying notes to consolidated financial statements.

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## Consolidated Balance Sheets

*(Amounts in millions)*

|  | <i>Note</i> | <i>December 31,</i><br><b>2005</b> | <b>2006</b>    |
|--|-------------|------------------------------------|----------------|
|  |             | <b>RMB</b>                         | <b>RMB</b>     |
| <b>Assets</b>                            |             |                                    |                |
| Current assets                           |             |                                    |                |
| Cash and cash equivalents                |             | 64,461                             | 71,167         |
| Deposits with banks                      |             | 41,925                             | 82,294         |
| Tax recoverable                          |             | 165                                | 468            |
| Amount due from ultimate holding company | 13          | 63                                 | 305            |
| Prepayments and other current assets     |             | 3,583                              | 4,613          |
| Other receivables                        | 14          | 1,911                              | 2,500          |
| Accounts receivable                      | 15          | 6,603                              | 7,153          |
| Inventories                              | 16          | 2,365                              | 3,007          |
| <b>Total current assets</b>              |             | <b>121,076</b>                     | <b>171,507</b> |
| Property, plant and equipment            | 17          | 216,505                            | 218,274        |
| Construction in progress                 |             | 34,201                             | 52,436         |
| Land lease prepayments                   |             | 7,243                              | 7,675          |
| Goodwill                                 | 18          | 35,300                             | 36,894         |
| Other intangible assets                  | 19          |                                    | 700            |
| Interest in associates                   | 20          |                                    |                |
| Other financial assets                   | 21          | 77                                 | 77             |
| Deferred tax assets                      | 22          | 6,625                              | 7,113          |
| <b>Total assets</b>                      |             | <b>421,027</b>                     | <b>494,676</b> |

See accompanying notes to consolidated financial statements.

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## Consolidated Balance Sheets (continued)

(Amounts in millions)

|   | <i>Note</i> | <i>December 31,</i><br><b>2005</b><br><b>RMB</b> | <b>2006</b><br><b>RMB</b> |
|---|-------------|--|---------------------------|
| <b>Liabilities and equity</b>               |             |  |                           |
| Current liabilities                         |             |  |                           |
| Accounts payable                            | 23          | 41,931   | 57,240                    |
| Bills payable                               |             | 1,359  | 2,212                     |
| Deferred revenue – current portion          | 24          | 16,975   | 21,823                    |
| Accrued expenses and other payables         | 25          | 40,007   | 46,130                    |
| Amount due to immediate holding company     | 13          | 96   | 186                       |
| Amount due to ultimate holding company      | 13          | 269  | 129                       |
| Interest-bearing borrowings                 | 26          |  | 2,996                     |
| Obligations under capital lease             | 27          | 68   | 68                        |
| Current taxation                            |             | 9,249  | 9,823                     |
| Total current liabilities                   |             | 109,954  | 140,607                   |
| Deferred tax liabilities                    | 22          | 97   | 192                       |
| Interest-bearing borrowings                 | 26          | 36,545   | 33,574                    |
| Deferred revenue, excluding current portion | 24          | 1,324  | 930                       |
| <b>Total liabilities</b>                    |             | <b>147,920</b>                                   | <b>175,303</b>            |
| <b>Total equity attributable to:</b>        |             |  |                           |
| Equity shareholders of the Company          |             | 272,824  | 319,002                   |
| Minority interests                          |             | 283  | 371                       |
| <b>Total liabilities and equity</b>         |             | <b>421,027</b>                                   | <b>494,676</b>            |

See accompanying notes to consolidated financial statements.

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## Consolidated Statements of Cash Flows

(Amounts in millions)

|   | Year ended December 31, |                |                |
|---|-------------------------|----------------|----------------|
| Note  | 2004                    | 2005           | 2006           |
|   | RMB                     | RMB            | RMB            |
| <b>Operating activities</b>   |                         |                |                |
| Profit before tax   | 60,951                  | 78,264         | 96,908         |
| <i>Adjustments for:</i>   |                         |                |                |
| - Depreciation of property, plant and equipment                     | 44,186                  | 56,368         | 64,574         |
| - Amortization of land lease prepayments                            | 134                     | 169            | 176            |
| - Amortization of goodwill  | 1,930                   |                |                |
| - Amortization of other intangible assets                           |                         |                | 203            |
| - Loss on disposal of property, plant and equipment                 | 535                     | 411            | 46             |
| - Write-off of property, plant and equipment                        | 5,900                   | 5,645          | 2,857          |
| - Allowance for doubtful accounts                                   | 2,273                   | 2,968          | 3,852          |
| - Amortization of deferred expenses                                 | 47                      |                |                |
| - Interest income   | (1,014)                 | (1,615)        | (2,604)        |
| - Interest expense  | 1,679                   | 1,346          | 1,510          |
| - Dividend income   | (84)                    | (51)           | (39)           |
| - Equity-settled share-based payment expenses                       | 255                     | 1,553          | 2,264          |
| - Unrealized exchange loss, net                                     | 24                      | 108            | 212            |
| <b>Profit from operations before changes in working capital</b>     | <b>116,816</b>          | <b>145,166</b> | <b>169,959</b> |
| (Increase)/decrease in inventories                                  | (106)                   | 134            | (626)          |
| Decrease in amount due from fellow subsidiaries                     | 896                     |                |                |
| Decrease/(increase) in amount due from ultimate holding company     | 662                     | 293            | (242)          |
| Increase in accounts receivable                                     | (2,082)                 | (3,037)        | (4,310)        |
| Decrease/(increase) in other receivables                            | 377                     | 134            | (313)          |
| Increase in prepayments and other current assets                    | (555)                   | (609)          | (1,030)        |
| Decrease in amount due to fellow subsidiaries                       | (4,661)                 |                |                |
| Decrease in amount due to ultimate holding company                  | (1,257)                 | (190)          | (140)          |
| Increase in accounts payable  | 2,707                   | 2,303          | 6,556          |
| Increase/(decrease) in bills payable                                |                         | 11             | (3)            |
| Increase in accrued expenses and other payables                     | 6,365                   | 7,670          | 6,033          |
| Increase in deferred revenue  | 2,724                   | 4,419          | 4,455          |
| <b>Cash generated from operations</b>                               | <b>121,886</b>          | <b>156,294</b> | <b>180,339</b> |
| Tax paid  |                         |                |                |
| - Hong Kong profits tax paid  |                         |                | (21)           |
| - PRC enterprise income tax paid                                    | (18,107)                | (24,585)       | (30,972)       |
| <b>Net cash generated from operating activities carried forward</b> | <b>103,779</b>          | <b>131,709</b> | <b>149,346</b> |

See accompanying notes to consolidated financial statements.



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## Consolidated Statements of Cash Flows (continued)

(Amounts in millions)

|   |             | <i>Year ended December 31,</i> |             |             |
|---|-------------|--------------------------------|-------------|-------------|
|   | <i>Note</i> | <i>2004</i>                    | <i>2005</i> | <i>2006</i> |
|   |             | <b>RMB</b>                     | <b>RMB</b>  | <b>RMB</b>  |
| <b>Net cash generated from operating activities brought forward</b>                 |             | 103,779                        | 131,709     | 149,346     |
| <b>Investing activities</b>   |             |                                |             |             |
| Payment for acquisition of subsidiaries (net of cash and cash equivalents acquired) | (b)         | (12,238)                       |             | (3,410)     |
| Capital expenditure   |             | (58,367)                       | (66,027)    | (76,969)    |
| Land lease prepayments  |             | (776)                          | (1,079)     | (597)       |
| Payment for purchase of other intangible assets                                     |             |                                |             | (45)        |
| Proceeds from disposal of property, plant and equipment                             |             | 93                             | 132         | 80          |
| Increase in deposits with banks   |             | (3,037)                        | (21,661)    | (40,369)    |
| Interest received   |             | 939                            | 1,468       | 2,430       |
| Dividends received  |             | 84                             | 51          | 39          |
| <b>Net cash used in investing activities</b>  |             | (73,302)                       | (87,116)    | (118,841)   |
| <b>Financing activities</b>   |             |                                |             |             |
| Proceeds from issue of shares under share option scheme                             |             | 703                            | 3,422       | 4,093       |
| Redemption of convertible notes   |             |                                | (5,611)     |             |
| Redemption of fixed rate notes  |             | (4,978)                        |             |             |
| Repayments of interest-bearing borrowings   |             | (9,783)                        | (2,455)     | (104)       |
| Capital elements of capital leases rentals paid                                     |             | (10)                           |             |             |
| Interest paid   |             | (2,040)                        | (1,635)     | (1,414)     |
| Dividends paid  |             | (8,349)                        | (18,894)    | (26,162)    |
| <b>Net cash used in financing activities</b>  |             | (24,457)                       | (25,173)    | (23,587)    |
| <b>Net increase in cash and cash equivalents</b>                                    |             | 6,020                          | 19,420      | 6,918       |
| <b>Cash and cash equivalents at beginning of year</b>                               |             | 39,129                         | 45,149      | 64,461      |
| <b>Effect of changes in foreign exchange rate</b>                                   |             |                                | (108)       | (212)       |
| <b>Cash and cash equivalents at end of year</b>                                     |             | 45,149                         | 64,461      | 71,167      |
| <b>Analysis of the balances of cash and cash equivalents</b>                        |             |                                |             |             |
| Deposits with banks maturing within three months when placed                        |             | 7,100                          | 11,069      | 9,703       |
| Cash and bank balances  |             | 38,049                         | 53,392      | 61,464      |
|   |             | 45,149                         | 64,461      | 71,167      |

See accompanying notes to consolidated financial statements.

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## Consolidated Statements of Cash Flows (continued)

(Amounts in millions)

*(a) Acquisition of subsidiaries*

|  | <i>Year ended December 31,</i> |             |             |
|--|--------------------------------|-------------|-------------|
|  | <i>2004</i>                    | <i>2005</i> | <i>2006</i> |
|  | <b>RMB</b>                     | <b>RMB</b>  | <b>RMB</b>  |
| <i>Net assets acquired:</i>              |                                |             |             |
| Property, plant and equipment            | 33,584                         |             | 1,146       |
| Construction in progress                 | 3,806                          |             | 9           |
| Land lease prepayments                   | 1,210                          |             | 11          |
| Other intangible assets                  |                                |             | 859         |
| Deferred tax assets                      | 193                            |             |             |
| Inventories                              | 343                            |             | 17          |
| Amount due from ultimate holding company | 256                            |             |             |
| Amount due from fellow subsidiaries      | 896                            |             |             |
| Accounts receivable                      | 589                            |             | 91          |
| Other receivables                        | 417                            |             | 103         |
| Prepayments and other current assets     | 291                            |             |             |
| Cash and cash equivalents                | 4,315                          |             | 178         |
| Bills payable                            | (31)                           |             | (44)        |
| Amount due to ultimate holding company   | (364)                          |             |             |
| Amount due to fellow subsidiaries        | (4,661)                        |             |             |
| Accounts payable                         | (4,272)                        |             | (96)        |
| Obligations under capital leases         | (10)                           |             |             |
| Accrued expenses and other payables      | (4,263)                        |             | (96)        |
| Interest-bearing borrowings              | (3,460)                        |             | (104)       |
| Current taxation                         | (490)                          |             |             |
| Deferred revenue                         | (992)                          |             |             |
| Deferred tax liabilities                 | (4)                            |             | (80)        |
|  | 27,353                         |             | 1,994       |
| Goodwill arising on acquisition          | 2,857                          |             | 1,594       |
|  | 30,210                         |             | 3,588       |
| Satisfied by: Cash consideration         | 30,210                         |             | 3,588       |

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## Consolidated Statements of Cash Flows (continued)

*(Amounts in millions)****(b) Analysis of net outflow of cash and cash equivalents in respect of the acquisition of subsidiaries***

|  | <i>Year ended December 31,</i> |             |             |
|--|--------------------------------|-------------|-------------|
|  | <b>2004</b>                    | <b>2005</b> | <b>2006</b> |
|  | <b>RMB</b>                     | <b>RMB</b>  | <b>RMB</b>  |
| Cash consideration   | 30,210                         |             | 3,588       |
| Cash and bank balances acquired  | (4,315)                        |             | (178)       |
| Amount due to immediate holding company  | (13,657)                       |             |             |
| Net outflow of cash and cash equivalents in respect of acquisition of subsidiaries | 12,238                         |             | 3,410       |

***(c) Significant non-cash transactions:***

The Group incurred payables of RMB36,851 and RMB2,143 to equipment suppliers and banks respectively for additions of construction in progress during the year ended December 31, 2006.

The Group incurred payables of RMB28,176 and RMB1,332 to equipment suppliers and banks respectively for additions of construction in progress during the year ended December 31, 2005.

The Group incurred payables of RMB23,584 and RMB1,660 to equipment suppliers and banks respectively for additions of construction in progress during the year ended December 31, 2004.

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## Consolidated Statements of Equity

(Amounts in millions, except share data)

*Statements of equity for the years:*

|   |                           | Attributable to equity shareholders of the Company |                   |                     |                     |                      |                            |                       |           | Minority interest | Total equity |
|---|---------------------------|--|-------------------|---------------------|---------------------|----------------------|----------------------------|-----------------------|-----------|-------------------|--------------|
|   | Number of ordinary shares | Share capital RMB                                  | Share premium RMB | Capital reserve RMB | General reserve RMB | Exchange reserve RMB | PRC statutory reserves RMB | Retained earnings RMB | Total RMB | RMB               | RMB          |
| Equity at January 1, 2004                                   | 19,671,653,899            | 2,099  | 374,579           | (295,665)           | 72                  |                      | 32,686                     | 85,032                | 198,803   | 182               | 198,985      |
| Transfer from statements of income                          |                           |  |                   |                     |                     |                      |                            | 41,749                | 41,749    | 22                | 41,771       |
| Dividends approved in respect of previous year              |                           |  |                   |                     |                     |                      |                            | (4,174)               | (4,174)   |                   | (4,174)      |
| Dividends declared in respect of current year               |                           |  |                   |                     |                     |                      |                            | (4,175)               | (4,175)   |                   | (4,175)      |
| Shares issued under share option scheme                     | 28,985,500                | 3  | 700               |                     |                     |                      |                            |                       | 703       |                   | 703          |
| Equity settled share-based transactions                     |                           |  |                   | 255                 |                     |                      |                            |                       | 255       |                   | 255          |
| Appropriation   |                           |  |                   |                     |                     |                      | 9,591                      | (9,591)               |           |                   |              |
| Minority interests arising from acquisition of a subsidiary |                           |  |                   |                     |                     |                      |                            |                       |           | 39                | 39           |
| Equity at December 31, 2004                                 | 19,700,639,399            | 2,102  | 375,279           | (295,410)           | 72                  |                      | 42,277                     | 108,841               | 233,161   | 243               | 233,404      |
| Equity at January 1, 2005                                   |                           |  |                   |                     |                     |                      |                            |                       |           |                   |              |
| Before opening balance adjustment                           | 19,700,639,399            | 2,102  | 375,279           | (295,410)           | 72                  |                      | 42,277                     | 108,841               | 233,161   | 243               | 233,404      |
| Opening balance adjustment in                               |                           |  |                   |                     |                     |                      |                            | 33                    | 33        |                   | 33           |

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Standard 39

|  |                |         |           |           |        |          |          |         |                     |
|--|----------------|---------|-----------|-----------|--------|----------|----------|---------|---------------------|
| After opening balance adjustment               | 2,102          | 375,279 | (295,410) | 72        | 42,277 | 108,874  | 233,194  | 243     | 233,437             |
| Transfer from statements of income             |                |         |           |           |        | 53,549   | 53,549   | 40      | 53,589              |
| Dividends approved in respect of previous year |                |         |           |           |        | (9,635)  | (9,635)  |         | (9,635)             |
| Dividends declared in respect of current year  |                |         |           |           |        | (9,259)  | (9,259)  |         | (9,259)             |
| Shares issued under share option scheme        | 134,521,000    | 14      | 3,961     | (553)     |        |          | 3,422    |         | 3,422               |
| Equity settled share-based transactions        |                |         | 1,553     |           |        |          | 1,553    |         | 1,553               |
| Appropriation                                  |                |         |           |           | 11,118 | (11,118) |          |         |                     |
| Equity at December 31, 2005                    | 19,835,160,399 | 2,116   | 379,240   | (294,410) | 72     | 53,395   | 132,411  | 272,824 | 283 273,107         |
| Equity at January 1, 2006                      | 19,835,160,399 | 2,116   | 379,240   | (294,410) | 72     | 53,395   | 132,411  | 272,824 | 283 273,107         |
| Transfer from statements of income             |                |         |           |           |        | 66,026   | 66,026   | 88      | 66,114              |
| Dividends approved in respect of previous year |                |         |           |           |        | (11,719) | (11,719) |         | (11,719)            |
| Dividends declared in respect of current year  |                |         |           |           |        | (14,443) | (14,443) |         | (14,443)            |
| Shares issued under share option scheme        | 132,654,741    | 14      | 4,567     | (488)     |        |          | 4,093    |         | 4,093               |
| Equity settled share-based transactions        |                |         | 2,264     |           |        |          | 2,264    |         | 2,264               |
| Appropriation                                  |                |         |           |           | 13,566 | (13,566) |          |         |                     |
| Exchange difference                            |                |         |           |           | (43)   |          | (43)     |         | (43)                |
| Equity at December 31, 2006                    | 19,967,815,140 | 2,130   | 383,807   | (292,634) | 72     | (43)     | 66,961   | 158,709 | 319,002 371 319,373 |

See accompanying notes to consolidated financial statements.

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Notes to Consolidated Financial Statements

*(Amounts in millions, except share data)*

### **1 Organization, principal activities and basis of presentation**

China Mobile Limited (formerly China Mobile (Hong Kong) Limited) (the Company) and its subsidiaries (hereinafter collectively referred to as the Group) are principally engaged in the provision of mobile telecommunications and related services in thirty-one provinces, autonomous regions, and municipalities and Hong Kong Special Administrative Region in the People's Republic of China (PRC) and market their services under the China Mobile logo, which is a registered trademark owned by China Mobile Communications Corporation (CMCC), a company incorporated in the PRC in July 1999 to hold and operate the mobile telecommunications networks nationwide as a result of restructuring of the telecommunications industry in the PRC. The telecommunications operations in the PRC previously controlled by the Ministry of Information Industry (MII) have been separated into four business lines: fixed line communications, mobile communications, paging services and satellite communications. Since then, the MII act exclusively as the industry regulator and are not involved in managing the day-to-day operations of telecommunications service providers in the PRC.

Prior to the restructuring (as described below, the Restructuring), the Group's Total Access Communications Systems (TACS) and Global System for Mobile Communications (GSM) networks in Guangdong were owned by Guangdong Mobile Communication Corporation (together with the successor wholly-owned foreign enterprise formed in connection with the Restructuring, Guangdong Mobile), an enterprise formed in September 1988 and wholly owned by the MII on behalf of the State. Prior to the Restructuring, the Group's GSM network in Zhejiang was owned by Zhejiang GSM Mobile Communication Company Limited (together with the successor sino-foreign joint venture company formed in connection with the Restructuring, Zhejiang Mobile), a company formed in February 1996 and 98.55% owned by the Zhejiang Provincial Posts and Telecommunications Administrations (PTA) (Zhejiang PTA), while the Group's TACS networks in Zhejiang were owned and operated directly by the Zhejiang PTA.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **1 Organization, principal activities and basis of presentation (continued)**

#### *Restructuring*

Pursuant to the Restructuring, the Company was established as a wholly-owned subsidiary of China Mobile Hong Kong (BVI) Limited ( CMHK (BVI) ), a company incorporated with limited liability in the British Virgin Islands. CMHK (BVI) is controlled by China Mobile (Hong Kong) Group Limited ( CMHKG ), which in turn is 51% owned by Telpo Communications (Group) Limited ( Telpo ), a Hong Kong company wholly owned by the MII, and as to 49% by the China Telecommunications Corporation (previously known as the Directorate General of Telecommunications, or the DGT). At December 31, 1999, the percentages of equity interests of CMHK (BVI), which in turn were owned by Telpo and DGT were changed to 57% and 43%, respectively. On May 12, 2000, CMCC acquired a 100% controlling interest in CMHKG. As a result of this, CMCC indirectly holds approximately 75% equity interest in the Company. China Mobile Group Guangdong Co., Ltd. (formerly Guangdong Mobile Communication Company Limited ) was formed as a wholly foreign-owned enterprise whereas China Mobile Group Zhejiang Co., Ltd (formerly Zhejiang Mobile Communication Company Limited ) was formed as a sino-foreign joint venture company. The Company is the sole equity owner in Guangdong Mobile and was initially the 99.63% joint venture partner in Zhejiang Mobile, with the remaining interests held by various local investors. The Company acquired the remaining 0.37% interest in Zhejiang Mobile in April 1999. Subsequent to the acquisition, Zhejiang Mobile became a wholly foreign-owned enterprise.

In connection with the Restructuring and in anticipation of the initial offering of the Company's ordinary shares, the property, plant and equipment of Guangdong Mobile and Zhejiang Mobile were revalued as of May 31, 1997, by a firm of independent valuers and approved by the China State-owned Assets Administration Bureau. The value of property, plant and equipment and land lease prepayments of Guangdong Mobile and Zhejiang Mobile pursuant to the valuation, based on a depreciated replacement cost basis, was determined at RMB15,630. Upon the transfer of interests in Guangdong Mobile and Zhejiang Mobile by the MII and the DGT to the Company, 9,010,000,000 ordinary shares of HK\$0.10 each were issued by the Company to CMHK (BVI) for consideration valued at RMB19,466. Such amount was based on the net asset value of Guangdong Mobile and Zhejiang Mobile at May 31, 1997, the effective date of the Restructuring, adjusted for additional earnings to September 26, 1997, the completion date of the Restructuring, of RMB1,135, which is reflected as capital reserve.



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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **1 Organization, principal activities and basis of presentation (continued)**

#### *Equity offering*

Subsequent to the Restructuring, in October 1997, the Company completed an initial public offering (the Offering) of an aggregate of 2,770,788,000 ordinary shares. Net proceeds to the Company for the Offering, after deduction of offering expenses, were approximately RMB33,570.

#### *Acquisition of China Mobile Group Jiangsu Co., Ltd. (formerly Jiangsu Mobile Communication Company Limited) (Jiangsu Mobile)*

Pursuant to the ordinary resolution passed by the Company's shareholders on June 3, 1998, the Company acquired the entire issued share capital of China Telecom Jiangsu Mobile (BVI) Limited (subsequently renamed as Jiangsu Mobile (BVI) Limited) (Jiangsu Mobile BVI) from CMHK (BVI) by a total cash consideration of HK\$22,475 (RMB equivalent 24,120) (hereinafter referred to as the First Acquisition).

The only asset of Jiangsu Mobile BVI is its interest in the entire equity of Jiangsu Mobile. Subsequent to the First Acquisition, Jiangsu Mobile became a wholly foreign-owned enterprise.

In connection with the First Acquisition, the property, plant and equipment and land lease prepayments of Jiangsu Mobile were revalued as of December 31, 1997, by a firm of independent valuers and approved by the China State-owned Assets Administration Bureau. The value of property, plant and equipment of Jiangsu Mobile pursuant to the valuation, based on a depreciated replacement cost basis, was determined at RMB7,879.

In prior years, goodwill arising from the First Acquisition (RMB15,569), being the excess of the cost of investments (RMB24,120) over the fair value of the Group's share of the separable net assets acquired (RMB8,551), was eliminated against reserves immediately on acquisition. The fair value of the Group's share of the separable net assets acquired was based on the net asset value of Jiangsu Mobile at December 31, 1997 (RMB8,065), adjusted for additional earnings to June 3, 1998, the completion date of the First Acquisition, of RMB489. With effect from January 1, 2005, in order to comply with Hong Kong Financial Reporting Standard (HKFRS) 3 Business combinations and Hong Kong Accounting Standard (HKAS) 36 Impairment of assets, the Group has changed its accounting policies relating to goodwill. In accordance with the transitional arrangements under HKFRS 3, goodwill which had previously been taken into reserve will not be recognized in the consolidated statements of income on disposal or impairment of the acquired business, or under any other circumstances.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **1 Organization, principal activities and basis of presentation (continued)**

*Acquisition of China Mobile Group Fujian Co., Ltd. (formerly Fujian Mobile Communication Company Limited ) ( Fujian Mobile ), China Mobile Group Henan Co., Ltd. (formerly Henan Mobile Communication Company Limited ) ( Henan Mobile ) and China Mobile Group Hainan Co., Ltd. (formerly Hainan Mobile Communication Company Limited ) ( Hainan Mobile )*

Pursuant to an ordinary resolution passed by the Company's shareholders on November 11, 1999, the Company acquired the entire issued share capital of Fujian Mobile (BVI) Limited ( Fujian Mobile BVI ), Henan Mobile (BVI) Limited ( Henan Mobile BVI ) and Hainan Mobile (BVI) Limited ( Hainan Mobile BVI ) from CMHK (BVI) for a total consideration of HK\$49,715 (RMB equivalent 52,953) (hereinafter referred to as the Second Acquisition ). The consideration was satisfied by cash of HK\$19,031 (RMB equivalent 20,268) and an allotment of 1,273,195,021 ordinary shares of HK\$0.10 each to CMHK (BVI) amounting to HK\$30,684 (RMB equivalent 32,685). The only assets of each of Fujian Mobile BVI, Henan Mobile BVI and Hainan Mobile BVI are their interests in the entire equity of Fujian Mobile, Henan Mobile and Hainan Mobile, respectively.

In connection with the Second Acquisition, the property, plant and equipment and land lease prepayments of Fujian Mobile, Henan Mobile and Hainan Mobile were revalued as of June 30, 1999, by a firm of independent valuers and approved by the Ministry of Finance. The value of property, plant and equipment and land lease prepayments of Fujian Mobile, Henan Mobile and Hainan Mobile pursuant to the valuation, based on a depreciated replacement cost basis, was determined at RMB10,684.

In prior years, goodwill arising from the Second Acquisition (RMB42,340), being the excess of the cost of investments (RMB52,953) over the fair value of the Group's share of the separable net assets acquired (RMB10,613), was eliminated against reserves immediately on acquisition. The fair value of the Group's share of the separable net assets acquired was based on the net assets of Fujian Mobile, Henan Mobile and Hainan Mobile at June 30, 1999 (RMB9,624), adjusted for additional earnings to November 11, 1999, the completion date of the Second Acquisition, of RMB989. With effect from January 1, 2005, in order to comply with HKFRS 3 and HKAS 36, the Group has changed its accounting policies relating to goodwill. In accordance with the transitional arrangements under HKFRS 3, goodwill which had previously been taken into reserve will not be recognized in the consolidated statements of income on disposal or impairment of the acquired business, or under any other circumstances.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **1 Organization, principal activities and basis of presentation (continued)**

#### *Equity offering and debt offering*

In order to finance the acquisition consideration, the Company completed an international offering of an aggregate of 644,804,000 ordinary shares and debt offering with a principal amount of US\$600 with maturity due on November 2, 2004. Further, the Company issued 1,273,195,021 consideration shares to CMHK (BVI), credited as fully paid as part of the acquisition consideration. Net proceeds to the Company for such equity offering and debt offering, after deduction of offering expenses and discount, were approximately RMB16,134 and RMB4,899, respectively.

*Acquisition of China Mobile Group Beijing Co., Ltd. (formerly Beijing Mobile Communication Company Limited) (Beijing Mobile), China Mobile Group Shanghai Co., Ltd. (formerly Shanghai Mobile Communication Company Limited) (Shanghai Mobile), China Mobile Group Tianjin Co., Ltd. (formerly Tianjin Mobile Communication Company Limited) (Tianjin Mobile), China Mobile Group Hebei Co., Ltd. (formerly Hebei Mobile Communication Company Limited) (Hebei Mobile), China Mobile Group Liaoning Co., Ltd. (formerly Liaoning Mobile Communication Company Limited) (Liaoning Mobile), China Mobile Group Shandong Co., Ltd. (formerly Shandong Mobile Communication Company Limited) (Shandong Mobile) and China Mobile Group Guangxi Co., Ltd. (formerly Guangxi Mobile Communication Company Limited) (Guangxi Mobile)*

Pursuant to an ordinary resolution passed by the Company's shareholders on November 10, 2000, the Company acquired the entire issued share capital of Beijing Mobile (BVI) Limited (Beijing Mobile BVI), Shanghai Mobile (BVI) Limited (Shanghai Mobile BVI), Tianjin Mobile (BVI) Limited (Tianjin Mobile BVI), Hebei Mobile (BVI) Limited (Hebei Mobile BVI), Liaoning Mobile (BVI) Limited (Liaoning Mobile BVI), Shandong Mobile (BVI) Limited (Shandong Mobile BVI) and Guangxi Mobile (BVI) Limited (Guangxi Mobile BVI) from CMHK (BVI) for a total consideration of HK\$256,021 (RMB equivalent 271,485) (hereinafter referred to as the Third Acquisition). The consideration was satisfied by cash of HK\$74,609 (RMB equivalent 79,116) and an allotment of 3,779,407,375 ordinary shares of HK\$0.10 each to CMHK (BVI) amounting to HK\$181,412 (RMB equivalent 192,369). The only assets of each of Beijing Mobile BVI, Shanghai Mobile BVI, Tianjin Mobile BVI, Hebei Mobile BVI, Liaoning Mobile BVI, Shandong Mobile BVI and Guangxi Mobile BVI are their interests in the entire equity of Beijing Mobile, Shanghai Mobile, Tianjin Mobile, Hebei Mobile, Liaoning Mobile, Shandong Mobile and Guangxi Mobile, respectively.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **1 Organization, principal activities and basis of presentation (continued)**

In connection with the Third Acquisition, the property, plant and equipment and land lease prepayments of Beijing Mobile, Shanghai Mobile, Tianjin Mobile, Hebei Mobile, Liaoning Mobile, Shandong Mobile and Guangxi Mobile were revalued as of June 30, 2000, by a firm of independent valuers and approved by the Ministry of Finance. The value of property, plant and equipment and land lease prepayments of Beijing Mobile, Shanghai Mobile, Tianjin Mobile, Hebei Mobile, Liaoning Mobile, Shandong Mobile and Guangxi Mobile pursuant to the valuation, based on a depreciated replacement cost basis, was determined at RMB37,252.

In prior years, goodwill arising from the Third Acquisition (RMB238,891), being the excess of the cost of investments (RMB271,485) over the fair value of the Group's share of the separable net assets acquired (RMB32,594), was eliminated against reserves immediately on acquisition. The fair value of the Group's share of the separable net assets acquired was based on the net assets of Beijing Mobile, Shanghai Mobile, Tianjin Mobile, Hebei Mobile, Liaoning Mobile, Shandong Mobile and Guangxi Mobile at June 30, 2000 (RMB29,966), adjusted for additional earnings to November 12, 2000, the completion date of the Third Acquisition, of RMB2,628. With effect from January 1, 2005, in order to comply with HKFRS 3 and HKAS 36, the Group has changed its accounting policies relating to goodwill. In accordance with the transitional arrangements under HKFRS 3, goodwill which had previously been taken into reserve will not be recognized in the consolidated statements of income on disposal or impairment of the acquired business, or under any other circumstances.

#### *Equity offering and debt offering*

In order to finance the acquisition consideration, the Company completed an international offering of an aggregate of 1,115,643,845 ordinary shares and debt offering with a principal amount of US\$690 with maturity due on November 3, 2005. Further the Company issued 3,779,407,375 consideration shares to CMHK (BVI), credited as fully paid as part of the acquisition consideration. Net proceeds to the Company for such equity offering and debt offering, after deduction of offering expenses and discount, were approximately RMB55,723 and RMB5,580, respectively.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **1 Organization, principal activities and basis of presentation (continued)**

*Acquisition of China Mobile Group Anhui Co., Ltd. (formerly Anhui Mobile Communication Company Limited) (Anhui Mobile), China Mobile Group Jiangxi Co., Ltd. (formerly Jiangxi Mobile Communication Company Limited) (Jiangxi Mobile), China Mobile Group Chongqing Co., Ltd. (formerly Chongqing Mobile Communication Company Limited) (Chongqing Mobile), China Mobile Group Sichuan Co., Ltd. (formerly Sichuan Mobile Communication Company Limited) (Sichuan Mobile), China Mobile Group Hubei Co., Ltd. (formerly Hubei Mobile Communication Company Limited) (Hubei Mobile), China Mobile Group Hunan Mobile Communication Co., Ltd. (formerly Hunan Mobile Communication Company Limited) (Hunan Mobile), China Mobile Group Shaanxi Mobile Communication Co., Ltd. (formerly Shaanxi Mobile Communication Company Limited) (Shaanxi Mobile) and China Mobile Group Shanxi Mobile Communication Co., Ltd. (formerly Shanxi Mobile Communication Company Limited) (Shanxi Mobile)*

Pursuant to a resolution passed at the extraordinary general meeting held on June 24, 2002, the Company acquired the entire issued share capital of Anhui Mobile BVI Limited (Anhui Mobile BVI), Jiangxi Mobile BVI Limited (Jiangxi Mobile BVI), Chongqing Mobile BVI Limited (Chongqing Mobile BVI), Sichuan Mobile BVI Limited (Sichuan Mobile BVI), Hubei Mobile BVI Limited (Hubei Mobile BVI), Hunan Mobile BVI Limited (Hunan Mobile BVI), Shaanxi Mobile BVI Limited (Shaanxi Mobile BVI) and Shanxi Mobile Communication BVI Limited (Shanxi Mobile BVI) from CMHK (BVI). The acquisition was completed on July 1, 2002 for a total consideration of US\$8,573 (RMB equivalent 70,959) (hereinafter referred to as the Fourth Acquisition). The consideration was satisfied by cash of RMB49,248 and an allotment of 827,514,446 ordinary shares of HK\$0.10 each to CMHK (BVI) amounting to HK\$20,458 (RMB equivalent 21,711). The only assets of each of Anhui Mobile BVI, Jiangxi Mobile BVI, Chongqing Mobile BVI, Sichuan Mobile BVI, Hubei Mobile BVI, Hunan Mobile BVI, Shaanxi Mobile BVI and Shanxi Mobile BVI are their interests in the entire equity of Anhui Mobile, Jiangxi Mobile, Chongqing Mobile, Sichuan Mobile, Hubei Mobile, Hunan Mobile, Shaanxi Mobile and Shanxi Mobile, respectively.

In connection with the Fourth Acquisition, the property, plant and equipment and land lease prepayments of Anhui Mobile, Jiangxi Mobile, Chongqing Mobile, Sichuan Mobile, Hubei Mobile, Hunan Mobile, Shaanxi Mobile and Shanxi Mobile were revalued as of December 31, 2001, by a firm of independent valuers and approved by the Ministry of Finance. The value of property, plant and equipment and land lease prepayments of Anhui Mobile, Jiangxi Mobile, Chongqing Mobile, Sichuan Mobile, Hubei Mobile, Hunan Mobile, Shaanxi Mobile and Shanxi Mobile pursuant to the valuation, based on a depreciated replacement cost basis, was determined at RMB39,499.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **1 Organization, principal activities and basis of presentation (continued)**

In prior years, positive goodwill arising from the Fourth Acquisition (RMB37,159), being the excess of the cost of investments (RMB70,959) over the fair value of the Group's share of the separable net assets acquired (RMB33,800), is amortized to the consolidated statements of income on a straight-line basis over 20 years. Positive goodwill is stated in the consolidated balance sheet at cost less accumulated amortization and any impairment losses. The fair value of the Group's share of the separable net assets acquired was based on the net assets of Anhui Mobile, Jiangxi Mobile, Chongqing Mobile, Sichuan Mobile, Hubei Mobile, Hunan Mobile, Shaanxi Mobile and Shanxi Mobile at December 31, 2001 (RMB30,982), adjusted for additional earnings to June 30, 2002, the completion date of the Fourth Acquisition, of RMB2,818. With effect from January 1, 2005, in order to comply with HKFRS 3 and HKAS 36, the Group has changed its accounting policies relating to goodwill. Under the new policy, the Group no longer amortizes positive goodwill but tests it at least annually for impairment.

#### *Equity offering and debt offering*

In order to finance the acquisition consideration, the Company issued 236,634,212 new shares to Vodafone Holdings (Jersey) Limited at HK\$5,850 (RMB equivalent 6,205). Further, the Company issued 827,514,446 consideration shares to CMHK (BVI), credited as fully paid as part of the acquisition consideration. Net proceeds to the Company for the equity offering, after deduction of offering expenses, was approximately RMB5,946. In addition, Guangdong Mobile issued five-year guaranteed bonds and fifteen-year guaranteed bonds, with a principal amount of RMB3,000 and RMB5,000 respectively, at an issue price equal to the face value of the bonds. Net proceeds to the Group for the debt offering, after deduction of offering expenses, was approximately RMB7,947.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **1 Organization, principal activities and basis of presentation (continued)**

*Acquisition of China Mobile Group Neimenggu Co., Ltd. (formerly Neimenggu Mobile Communication Company Limited ) ( Neimenggu Mobile ), China Mobile Group Jilin Co., Ltd. (formerly Jilin Mobile Communication Company Limited ) ( Jilin Mobile ), China Mobile Group Heilongjiang Co., Ltd. (formerly Heilongjiang Mobile Communication Company Limited ) ( Heilongjiang Mobile ), China Mobile Group Guizhou Co., Ltd. (formerly Guizhou Mobile Communication Company Limited ) ( Guizhou Mobile ), China Mobile Group Yunnan Co., Ltd. (formerly Yunnan Mobile Communication Company Limited ) ( Yunnan Mobile ), China Mobile Group Xizang Co., Ltd. (formerly Xizang Mobile Communication Company Limited ) ( Xizang Mobile ), China Mobile Group Gansu Co., Ltd. (formerly Gansu Mobile Communication Company Limited ) ( Gansu Mobile ), China Mobile Group Qinghai Co., Ltd. (formerly Qinghai Mobile Communication Company Limited ) ( Qinghai Mobile ), China Mobile Group Ningxia Co., Ltd. (formerly Ningxia Mobile Communication Company Limited ) ( Ningxia Mobile ), China Mobile Group Xinjiang Co., Ltd. (formerly Xinjiang Mobile Communication Company Limited ) ( Xinjiang Mobile ), China Mobile Group Design Institute Co., Ltd. (formerly Beijing P&T Consulting & Design Institute Company Limited ) ( Jingyi Design Institute ) and China Mobile Communication Co., Ltd. ( CMC ).*

Pursuant to a resolution passed at the extraordinary general meeting held on June 16, 2004, the Company acquired the entire issued share capital of Neimenggu Mobile (BVI) Limited ( Neimenggu Mobile BVI ), Jilin Mobile (BVI) Limited ( Jilin Mobile BVI ), Heilongjiang Mobile (BVI) Limited ( Heilongjiang Mobile BVI ), Guizhou Mobile (BVI) Limited ( Guizhou Mobile BVI ), Yunnan Mobile (BVI) Limited ( Yunnan Mobile BVI ), Xizang Mobile (BVI) Limited ( Xizang Mobile BVI ), Gansu Mobile (BVI) Limited ( Gansu Mobile BVI ), Qinghai Mobile BVI Limited ( Qinghai Mobile BVI ), Ningxia Mobile (BVI) Limited ( Ningxia Mobile BVI ), Xinjiang Mobile (BVI) Limited ( Xinjiang Mobile BVI ), Beijing P&T Consulting & Design Institute (BVI) Limited ( Zhongjing Design Institute BVI ) and China Mobile Communication (BVI) Limited ( CMC BVI ) from CMHK (BVI). The acquisition was completed on July 1, 2004 for a total consideration of US\$3,650 (RMB equivalent 30,210) (hereinafter referred to as the Fifth Acquisition ). The consideration was satisfied by cash. The only assets of each of Neimenggu Mobile BVI, Jilin Mobile BVI, Heilongjiang Mobile BVI, Guizhou Mobile BVI, Yunnan Mobile BVI, Xizang Mobile BVI, Gansu Mobile BVI, Qinghai Mobile BVI, Ningxia Mobile BVI, Xinjiang Mobile BVI, Zhongjing Design Institute BVI and CMC BVI are their interests in the entire equity of Neimenggu Mobile, Jilin Mobile, Heilongjiang Mobile, Guizhou Mobile, Yunnan Mobile, Xizang Mobile, Gansu Mobile, Qinghai Mobile, Ningxia Mobile, Xinjiang Mobile, Jingyi Design Institute and CMC, respectively.

## **Table of Contents**

Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **1 Organization, principal activities and basis of presentation (continued)**

In connection with the Fifth Acquisition, the property, plant and equipment and land lease prepayments of Neimenggu Mobile, Jilin Mobile, Heilongjiang Mobile, Guizhou Mobile, Yunnan Mobile, Xizang Mobile, Gansu Mobile, Qinghai Mobile, Ningxia Mobile, Xinjiang Mobile, Jingyi Design Institute and CMC were revalued as of December 31, 2003, by a firm of independent valuers and approved by the State-owned Assets Supervision and Administration Commission of the State Council ( SASACSC ). The value of property, plant and equipment and land lease prepayments of Neimenggu Mobile, Jilin Mobile, Heilongjiang Mobile, Guizhou Mobile, Yunnan Mobile, Xizang Mobile, Gansu Mobile, Qinghai Mobile, Ningxia Mobile, Xinjiang Mobile, Jingyi Design Institute and CMC pursuant to the valuation, based on a depreciated replacement cost basis, was determined at RMB33,996.

In prior years, positive goodwill arising from the Fifth Acquisition (RMB2,857), being the excess of the cost of investments (RMB30,210) over the fair value of the Group's share of the separable net assets acquired (RMB27,353), was amortized to the consolidated statements of income on a straight-line basis over 20 years. Positive goodwill was stated in the consolidated balance sheet at cost less accumulated amortization and any impairment losses. The fair value of the Group's share of the separable net assets acquired was based on the net assets of Neimenggu Mobile, Jilin Mobile, Heilongjiang Mobile, Guizhou Mobile, Yunnan Mobile, Xizang Mobile, Gansu Mobile, Qinghai Mobile, Ningxia Mobile, Xinjiang Mobile, Jingyi Design Institute and CMC at December 31, 2003 (RMB25,766), adjusted for additional earnings to June 30, 2004, the completion date of the Fifth Acquisition, of RMB1,587. With effect from January 1, 2005, in order to comply with HKFRS 3 and HKAS 36, the Group has changed its accounting policies relating to goodwill. Under the new policy, the Group no longer amortizes positive goodwill but tests it at least annually for impairment.

*Acquisition of China Resources Telephone Company Limited (currently known as China Mobile Peoples Telephone Company Limited , or Peoples Telephone )*

On November 10, 2005, the Group through Fit Best Limited, a company incorporated in the British Virgin Islands which is a wholly-owned subsidiary of the Company, made a voluntary conditional cash offer to acquire all the issued shares of Peoples Telephone, a mobile telecommunications services provider based in Hong Kong with its shares listed on the Stock Exchange of Hong Kong Limited (the SEHK ). The offer became unconditional in all respects on December 29, 2005.



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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

**1 Organization, principal activities and basis of presentation (continued)**

On January 5, 2006, Fit Best Limited successfully acquired 736,221,101 shares of Peoples Telephone, representing 99% of the issued shares of Peoples Telephone. Up to January 12, 2006, the Company received additional valid acceptance in respect of the voluntary conditional cash offer to acquire 5,073,500 shares of Peoples Telephone, representing 0.68% of the issued shares of Peoples Telephone. On the same day, the Company applied the provisions of the Hong Kong Companies Ordinance to compulsorily acquire any remaining issued shares of Peoples Telephone.

On March 28, 2006, the compulsory acquisition of all the issued and outstanding shares of Peoples Telephone was completed at a total cash consideration of HK\$3,384 (approximately RMB3,520) and the listing of the shares of Peoples Telephone on the SEHK was withdrawn with effect from March 29, 2006.

The newly acquired subsidiary has contributed profit for the year of RMB159 (equivalent to HK\$155). If the acquisition had occurred on January 1, 2006, the estimated Group revenue and profit for the year would not have been significantly different to the actual result.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***1 Organization, principal activities and basis of presentation (continued)**

The acquisition has the following effect on the Group's assets and liabilities:

|   | <i>Recognized<br/>values on<br/>acquisition<br/>RMB</i> |
|---|---|
| Property, plant and equipment             | 1,146   |
| Construction in progress                  | 9   |
| Land lease prepayments                    | 11  |
| Other intangible assets                   | 859   |
| Inventories                               | 17  |
| Accounts receivable and other receivables | 194   |
| Cash and cash equivalents                 | 178   |
| Bills payable                             | (44)  |
| Accounts payable and other payables       | (192)   |
| Interest-bearing borrowings               | (104)   |
| Deferred tax liabilities                  | (80)  |
| Net identified assets and liabilities     | 1,994   |
| Goodwill on acquisition                   | 1,594   |
|   | 3,588   |
| Cost of acquisition                       |   |
| Purchase consideration, satisfied in cash | 3,520   |
| Other directly attributable costs         | 68  |
|   | 3,588   |
| Cash acquired                             | (178)   |
| Net cash outflow                          | 3,410   |

Apart from other intangible assets, the acquiree's book value of net assets acquired at the date of acquisition approximates its fair value as disclosed above.

The goodwill is attributable to the synergies expected to arise after the Group's acquisition of Peoples Telephone. In order to comply with HKFRS 3 and HKAS 36, the Group does not amortize positive goodwill but tests it at least annually for impairment.

The acquired other intangible assets include brand name of RMB184, customer base of RMB516 and others of RMB159. All other intangible assets acquired, other than brand name, are deemed to be of finite life, with a weighted-average amortization period of 5 years, comprising customer base of 3 years and others of 9 years.



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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **1 Organization, principal activities and basis of presentation (continued)**

#### *Basis of preparation*

The consolidated financial statements have been prepared on a consolidated basis to reflect the financial position and results of operations of the Company, Guangdong Mobile and Zhejiang Mobile from the date of the Restructuring and of Jiangsu Mobile, Fujian Mobile, Henan Mobile, Hainan Mobile, Beijing Mobile, Shanghai Mobile, Tianjin Mobile, Hebei Mobile, Liaoning Mobile, Shandong Mobile, Guangxi Mobile, Anhui Mobile, Jiangxi Mobile, Chongqing Mobile, Sichuan Mobile, Hubei Mobile, Hunan Mobile, Shaanxi Mobile, Shanxi Mobile, Neimenggu Mobile, Jilin Mobile, Heilongjiang Mobile, Guizhou Mobile, Yunnan Mobile, Xizang Mobile, Gansu Mobile, Qinghai Mobile, Ningxia Mobile, Xinjiang Mobile, Peoples Telephone, Jingyi Design Institute and CMC from their respective dates of acquisition.

The consolidated statement of income for the year ended December 31, 2006 includes the results of the Company, the mobile telecommunications subsidiaries in each of the thirty-one provinces, autonomous regions and municipalities in Mainland China, Jingyi Design Institute and CMC for the year ended December 31, 2006 and the post-acquisition results of and Peoples Telephone from January 5, 2006 to December 31, 2006.

The consolidated statement of income for the year ended December 31, 2005 includes the results of the Company, the mobile telecommunications subsidiaries in each of the thirty-one provinces, autonomous regions and municipalities in Mainland China, Jingyi Design Institute and CMC for the year ended December 31, 2005.

The consolidated statement of income for the year ended December 31, 2004 includes the results of the Company, Guangdong Mobile, Zhejiang Mobile, Jiangsu Mobile, Fujian Mobile, Henan Mobile, Hainan Mobile, Beijing Mobile, Shanghai Mobile, Tianjin Mobile, Hebei Mobile, Liaoning Mobile, Shandong Mobile, Guangxi Mobile, Anhui Mobile, Jiangxi Mobile, Chongqing Mobile, Sichuan Mobile, Hubei Mobile, Hunan Mobile, Shaanxi Mobile, Shanxi Mobile for the year ended December 31, 2004 and the post-acquisition results of Neimenggu Mobile, Jilin Mobile, Heilongjiang Mobile, Guizhou Mobile, Yunnan Mobile, Xizang Mobile, Gansu Mobile, Qinghai Mobile, Ningxia Mobile, Xinjiang Mobile, Jingyi Design Institute and CMC for the period from July 1, 2004 to December 31, 2004.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **1 Organization, principal activities and basis of presentation (continued)**

The financial statements have been prepared in accordance with all applicable HKFRSs, which collective term includes all applicable individual Hong Kong Financial Reporting Standards, HKASs and Interpretations issued by the Hong Kong Institute of Certified Public Accountants ( HKICPA ), accounting principles generally accepted in Hong Kong ( HK GAAP ). Significant differences between HK GAAP and accounting principles generally accepted in the United States ( US GAAP ) are set forth in note 40.

The HKICPA has issued certain new and revised HKFRSs that are effective or available for early adoption for the current accounting period of the Group. Management has assessed and determined in the preparation of this annual consolidated financial statements that the new and revised HKFRSs have no significant impact on the Group's current and prior accounting periods' financial position and results of operations.

### **2 Principal accounting policies**

#### ***(a) Basis of consolidation***

The consolidated financial statements include the financial statements of the Company and all of its subsidiaries (see note 36 for details of the Company's principal subsidiaries). The results of subsidiaries are included in the consolidated statements of income, and the minority interests in the results of the Group are presented on the face of the consolidated statements of income as an allocation of the total profit or loss for the year between minority interests and the equity shareholders of the Company. All significant inter-company balances and transactions have been eliminated.

#### ***(b) Cash and cash equivalents***

Cash and cash equivalents comprise cash at bank and on hand, demand deposits with banks, and short-term, highly liquid investments that are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value, having been within three months of maturity at acquisition.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **2 Principal accounting policies (continued)**

#### ***(c) Associates***

An associate is an entity in which the Group has significant influence, but not control or joint control, over its management, including participation in the financial and operating policy decisions.

An investment in an associate is accounted for in the consolidated financial statements under the equity method and is initially recorded at cost and adjusted thereafter for the post acquisition change in the Group's share of the associate's net assets. The consolidated statements of income include the Group's share of the post-acquisition, post-tax results of the associates for the year.

When the Group's share of losses exceeds its interest in the associates, the Group's interest is reduced to nil and recognition of further losses is discontinued except to the extent that the Group has incurred legal or constructive obligations or made payments on behalf of the associates. For this purpose, the Group's interest in the associate is the carrying amount of the investment under the equity method together with the Group's long-term interests that in substance form part of the Group's net investment in the associate.

Unrealized profits and losses resulting from transactions between the Group and its associates are eliminated to the extent of the Group's interest in the associates, except where unrealized losses provide evidence of an impairment of the asset transferred, in which case they are recognized immediately in the consolidated statements of income.

#### ***(d) Goodwill***

Goodwill represents the excess of the cost of a business combination over the Group's interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities.

Goodwill is stated at cost less accumulated impairment losses. Goodwill is allocated to cash-generating units and is tested annually for impairment (see note 2(i)).

Any excess of the Group's interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities over the cost of a business combination is recognized immediately in the consolidated statements of income.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **2 Principal accounting policies (continued)**

#### ***(d) Goodwill (continued)***

On disposal of a cash generating unit, any attributable amount of purchased goodwill is included in the calculation of the gain or loss on disposal.

#### ***(e) Intangible assets (other than goodwill)***

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

Intangible assets with indefinite useful lives are tested for impairment annually either individually or at the cash-generating unit level. Such intangible assets are not amortized. The useful life of an intangible asset with an indefinite life is reviewed annually to determine whether indefinite life assessment continues to be supportable. If not, the change in useful life assessment from indefinite to finite is accounted for prospectively from the date of change and in accordance with the policy for amortization of intangible assets with finite lives as set out above.

##### **(i) Brand name**

The Group's brand name are stated at cost less any impairment losses (see note 2(i)) on an individual basis.

##### **(ii) Customer base, license and contract-based agreement**

The Group's customer base, license and contract-based agreement are stated at cost less any impairment losses (see note 2(i)) and are amortized using straight-line basis over the estimated useful lives from 2 to 15 years.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **2 Principal accounting policies (continued)**

#### ***(f) Other investments in equity securities***

The Group's policies for investments in equity securities, other than investments in subsidiaries and associates, are as follows:

Investments in equity securities that do not have a quoted market price in an active market and whose fair value cannot be reliably measured are recognized in the consolidated balance sheet at cost less impairment losses (see note 2(i)).

Investments are recognized/derecognized on the date the Group commits to purchase/sell the investments or they expire.

#### ***(g) Property, plant and equipment***

Property, plant and equipment are stated in the consolidated balance sheet at cost less accumulated depreciation and impairment losses (see note 2(i)). The circumstances and basis under which the revalued amount (including the revalued amount of land lease prepayments) is arrived at are set out in details in note 17.

The cost of property, plant and equipment comprises the purchase price and any directly attributable costs of bringing the asset to its working condition and location for its intended use. Subsequent expenditure relating to an item of property, plant and equipment that has already been recognized is added to the carrying amount of the asset when it is probable that future economic benefits, in excess of the originally assessed standard of performance of the existing asset, will flow to the enterprise. All other subsequent expenditure is recognized as an expense in the period in which it is incurred.

Gains or losses arising from the retirement or disposal of an item of property, plant and equipment are determined as the difference between the net disposal proceeds and the carrying amount of the item and are recognized in the consolidated statements of income on the date of retirement or disposal.



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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **2 Principal accounting policies (continued)**

#### ***(g) Property, plant and equipment (continued)***

Depreciation is calculated to write off the cost of items of property, plant and equipment, less their estimated residual value, if any, using the straight-line method over their estimated useful lives as follows:

|  |              |
|--|--------------|
| Buildings  | 8 - 35 years |
| Telecommunications transceivers, switching centers, transmission and other network equipment | 5 - 10 years |
| Office equipment, furniture and fixtures and others  | 4 - 18 years |

Where parts of an item of property, plant and equipment have different useful lives, the cost of the item is allocated on a reasonable basis between the parts and each part is depreciated separately. Both the useful life of an asset and its residual value, if any, are reviewed annually.

During the year, management reviewed the estimated useful lives of all the property, plant and equipment and changed the estimated useful lives of certain network equipment from 7 years to 5 years. The effect of such change in accounting estimate is set out in note 17.

#### ***(h) Leased assets***

An arrangement, comprising a transaction or a series of transactions, is or contains a lease if management determines that the arrangement conveys a right to use a specific asset or assets for an agreed period of time in return for a payment or a series of payments. Such a determination is made on an evaluation of the substance of the arrangement and is regardless of whether the arrangement takes the legal form of a lease.

#### ***(i) Classification of assets leased to the Group***

Assets that are held by the Group under leases which transfer to the Group substantially all the risks and rewards of ownership are classified as being held under capital leases. Leases which do not transfer substantially all the risks and rewards of ownership to the Group are classified as operating leases.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

**2 Principal accounting policies (continued)**

***(h) Leased assets (continued)***

***(ii) Assets acquired under capital leases***

Where the Group acquires the use of assets under capital leases, the amounts representing the fair value of the leased asset, or, if lower, the present value of the minimum lease payments, of such assets are included in property, plant and equipment and the corresponding liabilities, net of finance charges, are recorded as obligations under capital leases. Depreciation is provided at rates which write off the cost of the assets over the term of the relevant lease or, where it is likely the Group will obtain ownership of the asset, the life of the asset, as set out in note 2(g). Impairment losses are accounted for in accordance with the accounting policy as set out in note 2(i). Finance charges implicit in the lease payments are charged to the consolidated statements of income over the period of the leases so as to produce an approximately constant periodic rate of charge on the remaining balance of the obligations for each accounting period. Contingent rentals are charged to the consolidated statements of income of the accounting period in which they are incurred. There were no contingent rentals recognized by the Group during the years presented.

***(iii) Operating lease charges***

Where the Group has the use of assets held under operating leases, payments made under the leases are charged to the consolidated statements of income in equal installments over the accounting periods covered by the lease term, except where an alternative basis is more representative of the pattern of benefits to be derived from the leased asset. Lease incentives received are recognized in the consolidated statements of income as an integral part of the aggregate net lease payments made. Contingent rentals are charged to the consolidated statements of income in the accounting period in which they are incurred. There were no contingent rentals recognized by the Group during the years presented.

The cost of acquiring land held under an operating lease is amortized on a straight-line basis over the period of the lease term.

## **Table of Contents**

Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **2 Principal accounting policies (continued)**

#### **(i) Impairment of assets**

##### **(i) Impairment of investments in equity securities and other receivables**

Investments in equity securities and other current receivables that are stated at cost are reviewed at each balance sheet date to determine whether there is objective evidence of impairment.

If any such evidence exists, any impairment loss/allowance is determined and recognized as follows:

- For unquoted equity securities carried at cost, the impairment loss is measured as the difference between the carrying amount of the financial asset and the estimated future cash flows, discounted at the current market rate of return for a similar financial asset where the effect of discounting is material. Impairment losses for equity securities are not reversed.
- For trade and other current receivables and other financial assets carried at amortized cost, the impairment loss is measured as the difference between the asset's carrying amount and present value of estimated future cash flows, discounted at the financial asset's original effective interest rate (i.e. the effective interest rate computed at initial recognition of these assets), where the effect of discounting is material.

If in a subsequent period the amount of an impairment decreases and the decrease can be linked objectively to an event occurring after the impairment loss was recognized, the impairment loss is reversed through the consolidated statements of income. A reversal of an impairment loss shall not result in the asset's carrying amount exceeding that which would have been determined had no impairment loss been recognized in prior years.

##### **(ii) Impairment of other assets**

Internal and external sources of information are reviewed at each balance sheet date to identify indications that the following assets may be impaired or, except in the case of goodwill, an impairment loss previously recognized no longer exists or may have decreased:

- property, plant and equipment;
- construction in progress;

## **Table of Contents**

Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **2 Principal accounting policies (continued)**

#### **(i) Impairment of assets (continued)**

##### **(ii) Impairment of other assets (continued)**

- pre-paid interests in leasehold land classified as being held under an operating lease;
- investments in associates;
- goodwill; and
- other intangible assets

If any such indication exists, the asset's recoverable amount is estimated. For goodwill and other intangible assets that have indefinite useful lives, the recoverable amount is estimated annually whether or not there is any indication of impairment.

##### **(i) Calculation of recoverable amount**

The recoverable amount of an asset is the greater of its net selling price and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of time value of money and the risks specific to the asset. Where an asset does not generate cash inflows largely independent of those from other assets, the recoverable amount is determined for the smallest group of assets that generates cash inflows independently (i.e. a cash-generating unit).

##### **(ii) Recognition of impairment losses**

An impairment loss is recognized in the consolidated statements of income whenever the carrying amount of an asset, or the cash-generating unit to which it belongs, exceeds its recoverable amount. Impairment losses recognized in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to the cash-generating unit (or group of units) and then, to reduce the carrying amount of the other assets in the unit (or group of units) on a pro rata basis, except that the carrying value of an asset will not be reduced below its individual fair value less costs to sell, or value in use, if determinable.

## **Table of Contents**

Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **2 Principal accounting policies (continued)**

#### ***(i) Impairment of assets (continued)***

##### ***(ii) Impairment of other assets (continued)***

##### ***(iii) Reversals of impairment losses***

In respect of assets other than goodwill, an impairment loss is reversed if there has been a favorable change in the estimates used to determine the recoverable amount. An impairment loss in respect of goodwill is not reversed.

A reversal of an impairment loss is limited to the asset's carrying amount that would have been determined had no impairment loss been recognized in prior years. Reversals of impairment losses are credited to the consolidated statements of income in the year in which the reversals are recognized.

##### ***(iii) Interim financial reporting and impairment***

Under the Hong Kong Listing Rules, the Group is required to prepare an interim financial report in compliance with HKAS 34 Interim financial reporting, in respect of the first six months of the financial year. At the end of the interim period, the Group applies the same impairment testing, recognition, and reversal criteria as it would at the end of the financial year (see notes 2(i)(i) and (ii)).

Impairment losses recognized in an interim period in respect of goodwill and unquoted equity securities carried at cost are not reversed in a subsequent period. This is the case even if no loss, or a smaller loss, would have been recognized had the impairment been assessed only at the end of the financial year to which the interim period relates. No impairment losses are recognized in respect of goodwill and unquoted equity securities carried at cost during the interim period.

#### ***(j) Construction in progress***

Construction in progress is stated at cost less any impairment losses (see note 2(i)). Cost comprises direct costs of construction as well as interest expense and exchange differences capitalized during the periods of construction and installation. Capitalization of these costs ceases and the construction in progress is transferred to property, plant and equipment when substantially all the activities necessary to prepare the assets for their intended use are completed. No depreciation is provided in respect of construction in progress until it is completed and ready for its intended use. No exchange differences were capitalized to the construction in progress during the years presented.

## **Table of Contents**

Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **2 Principal accounting policies (continued)**

#### ***(k) Inventories***

Inventories are stated at the lower of cost and net realizable value. Cost represents purchase cost of goods calculated using the weighted average cost method. Net realizable value is determined by reference to the sales proceeds of items sold in the ordinary course of business or to management's estimates based on prevailing market conditions.

When inventories are sold, the carrying amount of those inventories is recognized as a deduction of other net income due to its insignificance. The amount of any write-down of inventories to net realizable value and all losses of inventories are recognized as an expense in the period the write-down or loss occurs. The amount of any reversal of any write-down of inventories, arising from an increase in net realizable value, is recognized as a reduction in the amount of inventories recognized as an expense in the period in which the reversal occurs. No reversal of any write-down of inventories occurred during the years presented.

#### ***(l) Accounts receivable and other receivables***

Accounts receivable and other receivables are initially recognized at fair value and thereafter stated at amortized cost less allowances for doubtful accounts (see note 2(i)), except where the effect of discounting would be immaterial. In such case, the receivables are stated at cost less allowances for doubtful accounts (see note 2(i)).

#### ***(m) Deferred revenue***

Deferred revenue consists primarily of deferred revenue from prepaid service fees received from subscribers and deferred tax credit of purchase of domestic telecommunications equipment.

Revenue from prepaid service fees is recognized when the mobile telecommunications services are rendered.

Deferred tax credit of purchase of domestic telecommunications equipment is amortized over the remaining lives of the related property, plant and equipment and credited as non-operating income in the consolidated statements of income.

## **Table of Contents**

Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **2 Principal accounting policies (continued)**

#### ***(n) Interest-bearing borrowings***

Interest-bearing borrowings are recognized initially at fair value less attributable transaction costs. Subsequent to initial recognition, interest-bearing borrowings are stated at amortized cost with any difference between the amount initially recognized and redemption value being recognized in the consolidated statements of income over the period of the borrowings, together with any interest and fees payable, using the effective interest method.

#### ***(o) Accounts payable and other payables***

Accounts payable and other payables are initially recognized at fair value and subsequently stated at amortized cost unless the effect of discounting would be immaterial, in which case they are stated at cost.

#### ***(p) Revenue recognition***

Revenue is recognized when it is probable that the economic benefits will accrue to the Group and when the revenue can be measured reliably on the following basis:

- (i) usage fees, value-added services fees and other operating revenue are recognized as revenue when the service is rendered;
- (ii) monthly fees are recognized as revenue in the month during which the service is rendered;
- (iii) deferred revenue from prepaid services is recognized as revenue when the mobile telecommunications services are rendered upon actual usage by subscribers;
- (iv) interest income is recognized as it accrues using the effective interest method; and
- (v) sales of SIM cards and handsets are recognized on delivery of goods to the buyer. Such revenue, net of cost of goods sold, is included in other net income due to its insignificance.

## **Table of Contents**

Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **2 Principal accounting policies (continued)**

#### ***(q) Translation of foreign currencies***

The reporting currency of the Group's operations is Renminbi. See note 34. Foreign currency transactions are recorded at the applicable rates of exchange prevailing on the transaction dates. Monetary assets and liabilities denominated in currencies other than the functional currency are translated at the foreign exchange rates ruling at the balance sheet date. Exchange gains and losses, other than those capitalized as construction in progress, are recognized in the consolidated statements of income. Exchange differences attributable to the translation of borrowings denominated in currencies other than the functional currency and used for financing the construction of property, plant and equipment, are included in the cost of the related construction in progress. No exchange differences were capitalized to construction in progress during the years presented.

Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the foreign exchange rates ruling at the transaction dates. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are translated using the foreign exchange rates ruling at the dates the fair value was determined.

The results of foreign operations are translated into Renminbi at the exchange rates approximating the foreign exchange rates ruling at the dates of the transactions. Balance sheet items of foreign operations, including goodwill arising on consolidation of foreign operations acquired on or after January 1, 2005, are translated into Renminbi at the foreign exchange rates ruling at the balance sheet date. The resulting exchange differences are recognized directly in a separate component of equity.

On disposal of a foreign operation, the cumulative amount of the exchange differences recognized under equity, which relate to that foreign operation is included in the calculation of the profit or loss on disposal.



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**Table of Contents**

Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

**2 Principal accounting policies (continued)**

**(r) Income Tax**

Income tax for the year comprises current tax and movements in deferred tax assets and liabilities. Current tax and movements in deferred tax assets and liabilities are recognized in the consolidated statements of income except to the extent that they relate to items recognized directly in equity, in which case they are recognized in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

Deferred tax assets and liabilities arise from deductible and taxable temporary differences respectively, being the differences between the carrying amounts of assets and liabilities for financial reporting purposes and their tax bases. Deferred tax assets also arise from unused tax losses and unused tax credits.

Apart from certain limited exceptions, all deferred tax liabilities, and all deferred tax assets to the extent that it is probable that future taxable profits will be available against which the asset can be utilized, are recognized. Future taxable profits that may support the recognition of deferred tax assets arising from deductible temporary differences include those that will arise from the reversal of existing taxable temporary differences, provided those differences relate to the same taxation authority and the same taxable entity, and are expected to reverse either in the same period as the expected reversal of the deductible temporary difference or in periods into which a tax loss arising from the deferred tax asset can be carried back or forward. The same criteria are adopted when determining whether existing taxable temporary differences support the recognition of deferred tax assets arising from unused tax losses and credits, that is, those differences are taken into account if they relate to the same taxation authority and the same taxable entity, and are expected to reverse in a period, or periods, in which the tax loss or credit can be utilized.

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## **Table of Contents**

Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **2 Principal accounting policies (continued)**

#### **(r) Income tax (continued)**

The limited exceptions to recognition of deferred tax assets and liabilities are those temporary differences arising from goodwill not deductible for tax purposes, the initial recognition of assets or liabilities that affect neither accounting nor taxable profit (provided they are not part of a business combination), and temporary differences relating to investments in subsidiaries to the extent that, in the case of taxable differences, the Group controls the timing of the reversal and it is probable that the differences will not reverse in the foreseeable future, or in the case of deductible differences, unless it is probable that they will reverse in the future.

The amount of deferred tax recognized is measured based on the expected manner of realization or settlement of the carrying amount of the assets and liabilities, using tax rates enacted or substantively enacted at the balance sheet date. Deferred tax assets and liabilities are not discounted.

The carrying amount of a deferred tax asset is reviewed at each balance sheet date and is reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow the related tax benefit to be utilized. Any such reduction is reversed to the extent that it becomes probable that sufficient taxable profits will be available.

Current tax balances and deferred tax balances, and movements therein, are presented separately from each other and are not offset. Current tax assets are offset against current tax liabilities, and deferred tax assets against deferred tax liabilities, if the Group has the legally enforceable right to set off current tax assets against current tax liabilities and the following additional conditions are met:

- in the case of current tax assets and liabilities, the Group intends either to settle on a net basis, or to realize the asset and settle the liability simultaneously; or
- in the case of deferred tax assets and liabilities, if they relate to income taxes levied by the same taxation authority on either:
  - the same taxable entity; or

## **Table of Contents**

Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **2 Principal accounting policies (continued)**

#### **(r) Income tax (continued)**

- different taxable entities, which, in each future period in which significant amounts of deferred tax liabilities or assets are expected to be settled or recovered, intend to realize the current tax assets and settle the current tax liabilities on a net basis or realize and settle simultaneously.

#### **(s) Provisions and contingent liabilities**

- (i) Provisions are recognized for liabilities of uncertain timing or amount when the Group has a legal or constructive obligation arising as a result of a past event, it is probable that an outflow of economic benefits will be required to settle the obligation and a reliable estimate can be made. Where the time value of money is material, provisions are stated at the present value of the expenditures expected to settle the obligation.

Where it is not probable that an outflow of economic benefits will be required, or the amount cannot be estimated reliably, the obligation is disclosed as a contingent liability, unless the probability of outflow of economic benefits is remote. Possible obligations, whose existence will only be confirmed by the occurrence or non-occurrence of one or more future events are also disclosed as contingent liabilities unless the probability of outflow of economic benefits is remote.

- (ii) Provision for customer point reward program (the Program )

The Group invites its subscribers to participate in a customer point reward program (the Program ), which provides subscribers the option of electing to receive free telecommunications services or other non-cash gifts. The level of bonus points earned under the Program varies depending on the subscribers' service consumption, loyalty and payment history. The estimated incremental costs of providing these free rewards are expensed in the consolidated statements of income and are accrued as a current liability on the consolidated balance sheet based on (i) the number of subscribers who are qualified to exercise their redemption right at period/year end and the estimated rate of redemptions based on past experience; (ii) the estimated number of subscribers who have no right to redeem the incentives at period/year end, but who will ultimately earn and claim awards under the Program; and (iii) type of incentives that subscribers will select for redemption based on past experience. As subscribers redeem rewards or their entitlements expire, the provision is reduced accordingly.

## **Table of Contents**

Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **2 Principal accounting policies (continued)**

#### ***(t) Employee benefits***

##### **(i) Short term employee benefits and contributions to defined contribution retirement plans**

Salaries, annual bonuses, paid annual leave, leave passage, contributions to defined contribution plans and the cost of non-monetary benefits are accrued in the year in which the associated services are rendered by employees. Where payment or settlement is deferred and the effect would be material, these amounts are stated at their present values.

The Company and a subsidiary in Hong Kong are required to make contributions to Mandatory Provident Funds under the Hong Kong Mandatory Provident Fund Schemes Ordinance. Such contributions are recognized as an expense in the consolidated statements of income as incurred.

The employees of the subsidiaries in Mainland China participate in defined contribution retirement plans managed by the local government authorities whereby the subsidiaries are required to contribute to the schemes at fixed rates of the employees' salary costs. In addition to the local governmental defined contribution retirement plans, certain subsidiaries also participate in supplementary defined contribution retirement plans managed by independent insurance companies whereby the subsidiaries are required to make contributions to the retirement plans at fixed rates of the employees' salary costs or in accordance with the terms of the plans. The Group's contributions to these plans are charged to the consolidated statements of income when incurred. The subsidiaries have no obligations for the payment of retirement and other post-retirement benefits of staff other than the contributions described above.

##### **(ii) Share-based payments**

The fair value of share options granted to employees is recognized as an employee cost with a corresponding increase in a capital reserve within equity. The fair value is measured at grant date using the binomial lattice model, taking into account the terms and conditions upon which the options were granted. Where the employees have to meet vesting conditions before becoming unconditionally entitled to the share options, the total estimated fair value of the share options is spread over the vesting period, taking into account the probability that the options will vest. Otherwise, the fair value of options is recognized in the period in which the options are granted.

## **Table of Contents**

Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **2 Principal accounting policies (continued)**

#### ***(t) Employee benefits (continued)***

##### ***(ii) Share-based payments (continued)***

During the vesting period, the number of share options that is expected to vest is reviewed. Any adjustments to the cumulative fair value recognized in prior years are charged/credited to the consolidated statements of income for the year of the review, unless the original employee expenses qualify for recognition as an asset, with a corresponding adjustment to the capital reserve. On vesting date, the amount recognized as an expense is adjusted to reflect the actual number of share options that vest (with a corresponding adjustment to the capital reserve) except where forfeiture is only due to not achieving vesting conditions that relate to the market price of the Company's shares. The equity amount is recognized in the capital reserve until either the option is exercised (when it is transferred to the share premium account) or the option expires (when it is released directly to retained earnings).

##### ***(iii) Termination benefits***

Termination benefits are recognized when, and only when the Group demonstrably commits itself to terminate employment or to provide benefits as a result of voluntary redundancy by having a detailed formal plan which is without realistic possibility of withdrawal.

#### ***(u) Borrowing costs***

Borrowing costs are expensed in the consolidated statements of income in the period in which they are incurred, except to the extent that they are capitalized as being directly attributable to the acquisition, construction or production of an asset which necessarily takes a substantial period of time to get ready for its intended use or sale.

The capitalization of borrowing costs as part of the cost of a qualifying asset commences when expenditure for the asset is being incurred, borrowing costs are being incurred and activities that are necessary to prepare the asset for its intended use or sale are in progress. Capitalization of borrowing costs is suspended or ceased when substantially all the activities necessary to prepare the qualifying asset for its intended use or sale are interrupted or completed.

## **Table of Contents**

Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **2 Principal accounting policies (continued)**

#### **(v) Net income per share**

The calculation of basic net income per share for the years ended December 31, 2004, 2005 and 2006 are based on the profit attributable to equity shareholders of the Company and the weighted average number of shares in issue during the years.

The calculation of diluted net income per share for the year ended December 31, 2006 has been computed after adjusting for the effects of all dilutive potential ordinary shares. All dilutive potential ordinary shares arise from the share options granted under the share option scheme which, if converted to ordinary shares, would decrease net income per share.

The calculation of diluted net income per share for the years ended December 31, 2004 and 2005 have been computed after adding back the interest expense on the convertible notes and adjusting for the effects of all dilutive potential ordinary shares. All dilutive potential ordinary shares arise from the share options granted under the share option scheme and convertible notes issued by the Group which, if converted to ordinary shares, would decrease net income per share.

#### **(w) Related parties**

For the purposes of these consolidated financial statements, a party is considered to be related to be the Group if:

- (i) the party has the ability, directly or indirectly through one or more intermediaries, to control the Group or exercise significant influence over the Group in making financial and operating policy decisions, or has joint control over the Group;
- (ii) the Group and the party are subject to common control;
- (iii) the party is an associate of the Group;
- (iv) the party is a member of key management personnel of the Group or the Group's parent, or a close family member of such an individual, or is an entity under the control, joint control or significant influence of such individuals;
- (v) the party is a close family member of a party referred to in (i) or is an entity under the control, joint control or significant influence of such individuals; or
- (vi) the party is a post-employment benefit plan which is for the benefit of employees of the Group or of any entity that is a related party of the Group.

Close family members of an individual are those family members who may be expected to influence, or be influenced by, that individual in their dealings with the entity.



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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

**2 Principal accounting policies (continued)**

**(x) Segment reporting**

A segment is a distinguishable component of the Group that is engaged either in providing products or services (business segment), or in providing products or services within a particular economic environment (geographical segment), which is subject to risks and rewards that are different from those of other segments.

No analysis of the Group's operating revenue and contribution to profit from operations by geographical segment or business segment has been presented as the majority of the Group's operating activities are carried out in Mainland China and less than 10% of the Group's operating revenue and contribution to profit from operations were derived from activities outside Mainland China or outside the Group's mobile telecommunications and related services activities. There is no other geographical or business segment with segment assets equal to or greater than 10% of the Group's total assets.

**(y) Use of estimates**

The preparation of financial statements in conformity with HKFRSs requires management to make judgments, estimates and assumptions that affect the application of policies and reported amounts of assets, liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgments about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

Judgments made by management in the application of HKFRSs that have significant effect on the consolidated financial statements are discussed in note 38.



## **Table of Contents**

Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **2 Principal accounting policies (continued)**

#### **(z) *Minority interests***

Minority interests represent the portion of the net assets of subsidiaries attributable to interests that are not owned by the Company, whether directly or indirectly through subsidiaries, and in respect of which the Group has not agreed any additional terms with the holders of those interests which would result in the Group as a whole having a contractual obligation in respect of those interests that meets the definition of a financial liability. Minority interests are presented in the consolidated balance sheets within equity, separately from equity attributable to the equity shareholders of the Company. Minority interests in the results of the Group are presented on the face of the consolidated statements of income as an allocation of the total profit or loss for the year between minority interests and the equity shareholders of the Company.

Where losses applicable to the minority exceed the minority's interest in the equity of a subsidiary, the excess, and any further losses applicable to the minority, are charged against the Group's interest except to the extent that the minority has a binding obligation to, and is able to, make additional investment to cover the losses. If the subsidiary subsequently reports profits, the Group's interest is allocated all such profits until the minority's share of losses previously absorbed by the Group has been recovered.

### **3 Changes in accounting policies**

The HKICPA has issued certain new and revised HKFRSs that are first effective or available for early adoption for current accounting period of the Group.

Note 2 summarizes the accounting policies of the Group after the adoption of these developments to the extent that they are relevant to the Group. The adoption of these new and revised HKFRSs did not result in any significant impact for current and prior accounting periods.

The Group has not applied any new standard or interpretation that is not yet effective for the current accounting period (see note 39) except for HK(IFRIC) 10 *Interim financial reporting and impairment*, which is effective for accounting periods beginning on or after November 1, 2006.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **4 Operating revenue**

The principal activities of the Group are the provision of mobile telecommunications and related services in thirty-one provinces, autonomous regions and municipalities of Mainland China and Hong Kong Special Administrative Region ( Hong Kong ). The principal activity of the Company is investment holding.

Operating revenue represents usage fees, monthly fees, value-added services fees and other operating revenue derived from the Group's mobile telecommunications networks, net of PRC business tax. Business tax is charged at approximately 3% of the corresponding revenue. No business tax is charged on the revenue generated from the Group's mobile telecommunications and related services in Hong Kong.

*Operating revenue consists of:*

- (i) Usage fees which represent standard local usage fee for airtime and, where applicable, Domestic Direct Dial ( DDD ) charges and International Direct Dial ( IDD ) charges receivable from subscribers for the use of the Group's mobile telecommunications networks and facilities and fees in respect of roaming out calls. Roaming out calls are those made by the Group's subscribers outside the local service areas. See note 5 (ii).
- (ii) Monthly fees which represent fixed amounts charged to subscribers each month for their entitlement to use the Group's mobile telecommunications and related services.
- (iii) Value-added services fees mainly derived from voice value-added services, short message service ( SMS ) revenue and non-SMS data business revenue.
- (iv) Other operating revenue mainly represents interconnection revenue.

### **5 Operating expenses**

Operating expenses consist of:

- (i) Leased line charges which represent expenses paid or payable for the use of leased lines between the main switches, base transceiver stations, base station controllers, base stations, fixed line network connectors and long distance network connectors.
- (ii) Interconnection charges which represent amounts paid or payable in respect of call made between the Group's mobile telecommunications networks, the fixed line networks and other GSM network operators in the PRC. Included in the amounts are also charges in respect of the Group's subscribers roaming outside the service areas of the Group's mobile telecommunications networks (see note 4 (i)).

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***5 Operating expenses (continued)**

(iii) Personnel expenses which represent staff salaries, bonuses and medical benefits, provision for staff welfare expenses, contributions to staff retirement scheme and equity settled share-based payment expenses.

(iv) Other operating expenses which consist of:

|   | <i>Year ended December 31,</i> |             |             |
|---|--------------------------------|-------------|-------------|
|   | <b>2004</b>                    | <b>2005</b> | <b>2006</b> |
|   | <b>RMB</b>                     | <b>RMB</b>  | <b>RMB</b>  |
| Selling and promotion                                 | 26,460                         | 34,117      | 47,145      |
| Maintenance   | 8,588                          | 11,851      | 15,257      |
| Allowance for doubtful accounts and other receivables | 2,273                          | 2,968       | 3,852       |
| Operating lease charges                               | 3,379                          | 4,157       | 5,272       |
| Other expenses (Note)                                 | 22,111                         | 27,161      | 29,246      |
|   | 62,811                         | 80,254      | 100,772     |

Note: Other expenses consist of offices expenses, utilities charges, traveling expenses, entertainment expenses, spectrum charges and number resources fees, insurance expenses, consumables and supplies, debt collection fees, write-off of property, plant and equipment, amortization of other intangible assets and other miscellaneous expenses.

**6 Other net income**

Other net income primarily consists of the gross margin from sales of SIM cards and handsets.

|                                 | <i>Year ended December 31,</i> |             |             |
|---------------------------------|--------------------------------|-------------|-------------|
|                                 | <b>2004</b>                    | <b>2005</b> | <b>2006</b> |
|                                 | <b>RMB</b>                     | <b>RMB</b>  | <b>RMB</b>  |
| Sales of SIM cards and handsets | 6,035                          | 6,524       | 8,278       |
| Cost of SIM cards and handsets  | (2,868)                        | (3,240)     | (5,406)     |
|                                 | 3,167                          | 3,284       | 2,872       |

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***7 Non-operating net income**

Non-operating net income consists of:

|  | <i>Year ended December 31,</i> |              |              |
|--|--------------------------------|--------------|--------------|
|  | <i>2004</i>                    | <i>2005</i>  | <i>2006</i>  |
|  | <b>RMB</b>                     | <b>RMB</b>   | <b>RMB</b>   |
| Exchange gain/(loss)   | 21                             | (130)        | (212)        |
| Penalty income   | 232                            | 177          | 182          |
| Amortization of deferred tax credit of purchase of domestic telecommunications equipment | 352                            | 526          | 732          |
| Others   | 295                            | 452          | 315          |
| <b>Total non-operating net income</b>  | <b>900</b>                     | <b>1,025</b> | <b>1,017</b> |

**8 Finance costs**

Interest expense, net of the amounts capitalized, is as follows:

|  | <i>Year ended December 31,</i> |              |              |
|--|--------------------------------|--------------|--------------|
|  | <i>2004</i>                    | <i>2005</i>  | <i>2006</i>  |
|  | <b>RMB</b>                     | <b>RMB</b>   | <b>RMB</b>   |
| Interest incurred                      | 719                            | 685          | 948          |
| Interest capitalized                   | (16)                           | (2)          |              |
|  | 703                            | 683          | 948          |
| Interest expenses of fixed rate notes  | 330                            |              |              |
| Interest expenses of convertible notes | 129                            | 135          |              |
| Interest expenses of bonds             | 517                            | 528          | 562          |
| <b>Interest expense</b>                | <b>1,679</b>                   | <b>1,346</b> | <b>1,510</b> |

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***9 Directors remuneration**

Directors remuneration is as follows:

*(Expressed in Hong Kong dollars)*

|   | <i>Directors<br/>fees<br/>HK\$ 000</i> | <i>Salaries,<br/>allowances<br/>and benefits<br/>in kind<br/>HK\$ 000</i> | <i>Performance<br/>related<br/>bonuses<br/>HK\$ 000</i> | <i>Retirement<br/>scheme<br/>contributions<br/>HK\$ 000</i> | <i>Subtotal<br/>HK\$ 000</i> | <i>Fair value<br/>of share<br/>options<br/>HK\$ 000</i> | <i>2005<br/>Total<br/>HK\$ 000</i> |
|---|--|---|---|---|------------------------------|---|------------------------------------|
| <b>Executive directors</b>                              |  |   |   |   |                              |   |                                    |
| WANG Jianzhou   | 180                                    | 1,172   | 660   | 258   | 2,270                        | 4,264   | 6,534                              |
| LI Yue  | 180                                    | 960   | 540   | 210   | 1,890                        | 2,080   | 3,970                              |
| LU Xiangdong  | 180                                    | 960   | 540   | 210   | 1,890                        | 2,080   | 3,970                              |
| XUE Taohai  | 180                                    | 960   | 540   | 212   | 1,892                        | 2,080   | 3,972                              |
| ZHANG Chenshuang  | 180                                    | 960   | 540   | 220   | 1,900                        | 2,080   | 3,980                              |
| LI Mofang   | 180                                    | 960   | 540   | 226   | 1,906                        | 2,080   | 3,986                              |
| HE Ning   | 180                                    | 960   | 540   | 161   | 1,841                        | 2,080   | 3,921                              |
| LI Gang   | 180                                    | 854   | 520   | 190   | 1,744                        | 1,371   | 3,115                              |
| XU Long   | 180                                    | 920   | 640   | 299   | 2,039                        | 1,331   | 3,370                              |
| <b>Independent non-executive directors</b>              |  |   |   |   |                              |   |                                    |
| LO Ka Shui  | 505                                    |   |   |   | 505                          | 395   | 900                                |
| WONG Kwong Shing, Frank                                 | 440                                    |   |   |   | 440                          | 395   | 835                                |
| CHENG Mo Chi, Moses                                     | 440                                    |   |   |   | 440                          | 395   | 835                                |
| <b>Non-executive directors</b>                          |  |   |   |   |                              |   |                                    |
| J. Brian CLARK (resigned on March 11, 2005)             | 34                                     |   |   |   | 34                           |   | 34                                 |
| Julian Michael HORN-SMITH (appointed on March 11, 2005) | 146                                    |   |   |   | 146                          | 395   | 541                                |
|   | 3,185                                  | 8,706   | 5,060   | 1,986   | 18,937                       | 21,026  | 39,963                             |

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Notes to Consolidated Financial Statements (continued)

(Amounts in millions, except share data)

**9 Directors remuneration (continued)**

|  | <i>Directors<br/>fees</i> | <i>Salaries,<br/>allowances<br/>and benefits<br/>in kind</i> | <i>Performance<br/>related<br/>bonuses</i> | <i>Retirement<br/>scheme<br/>contributions</i> | <i>Subtotal</i> | <i>Fair value<br/>of share<br/>options</i> | <i>2006<br/>Total</i> |
|--|---------------------------|--|--|--|-----------------|--|-----------------------|
|  | HK\$ '000                 | HK\$ '000  | HK\$ '000                                  | HK\$ '000                                      | HK\$ '000       | HK\$ '000                                  | HK\$ '000             |
| <b>Executive directors</b>                           |                           |  |  |  |                 |  |                       |
| WANG Jianzhou  | 180                       | 1,172  | 660  | 255  | 2,267           | 7,161                                      | 9,428                 |
| LI Yue   | 180                       | 960  | 540  | 217  | 1,897           | 5,241                                      | 7,138                 |
| LU Xiangdong   | 180                       | 960  | 540  | 217  | 1,897           | 5,241                                      | 7,138                 |
| XUE Taohai   | 180                       | 960  | 540  | 219  | 1,899           | 5,241                                      | 7,140                 |
| ZHANG Chenshuang                                     | 180                       | 960  | 540  | 227  | 1,907           | 5,241                                      | 7,148                 |
| SHA Yuejia (appointed on March 16, 2006)             | 143                       | 765  | 540  | 209  | 1,657           | 3,903                                      | 5,560                 |
| LIU Aili (appointed on March 16, 2006)               | 143                       | 765  | 540  | 208  | 1,656           | 934  | 2,590                 |
| XIN Fanfei (appointed on January 3, 2006)            | 179                       | 955  | 540  | 179  | 1,853           |  | 1,853                 |
| XU Long  | 180                       | 920  | 400  | 132  | 1,632           | 2,050                                      | 3,682                 |
| LI Mofang (resigned on March 16, 2006)               | 37                        | 195  |  | 91   | 323             | 1,171                                      | 1,494                 |
| HE Ning (resigned on January 3, 2006)                | 1                         | 6  |  |  | 7               | 32   | 39                    |
| LI Gang (resigned on January 3, 2006)                | 1                         |  |  |  | 1               | 12   | 13                    |
| <b>Independent non-executive directors</b>           |                           |  |  |  |                 |  |                       |
| LO Ka Shui   | 505                       |  |  |  | 505             | 2,428                                      | 2,933                 |
| WONG Kwong Shing, Frank                              | 440                       |  |  |  | 440             | 2,428                                      | 2,868                 |
| CHENG Mo Chi, Moses                                  | 440                       |  |  |  | 440             | 2,428                                      | 2,868                 |
| <b>Non-executive directors</b>                       |                           |  |  |  |                 |  |                       |
| Paul Michael DONOVAN (appointed on June 7, 2006)     | 102                       |  |  |  | 102             |  | 102                   |
| Julian Michael HORN-SMITH (resigned on June 7, 2006) | 78                        |  |  |  | 78              | 1,149                                      | 1,227                 |
|  | 3,149                     | 8,618  | 4,840                                      | 1,954  | 18,561          | 44,660                                     | 63,221                |

The above emoluments include the fair value of share options granted to certain directors under the Company's share option scheme as estimated at the grant date. The details of the share option scheme are disclosed in note 33. As set out in note 2(t)(ii), the fair value of share options granted to the employees including directors is measured based on a binomial lattice model and recognized as an expense in the consolidated statements of income. However, such expense does not represent the actual benefit paid/payable to the employees including directors.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***10 Individuals with highest emoluments**

For the year ended December 31, 2005 and 2006, all of the five individuals with the highest emoluments are directors whose emoluments are disclosed in note 9.

**11 Income tax**

- (i) The provision for Hong Kong profits tax for 2006 is calculated at 17.5% (2004: 17.5%; 2005: 17.5%) of the estimated assessable profits for the year. For the years ended December 31, 2004 and 2005, no provision has been made for Hong Kong profits tax as there were no estimated Hong Kong assessable profits during the year.
- (ii) The provision for the PRC enterprise income tax is based on a statutory income tax rate of 33% of the assessable profit of the Group as determined in accordance with the relevant income tax rules and regulations of the PRC during the year, except for certain subsidiaries of the Company and certain operations of the subsidiaries located within special economic zones in the PRC, which enjoy a preferential rate of 30% or 15% respectively.

Income tax in the consolidated statements of income represents:

|   | <i>Year ended December 31,</i> |             |             |
|---|--------------------------------|-------------|-------------|
|   | <i>2004</i>                    | <i>2005</i> | <i>2006</i> |
|   | <b>RMB</b>                     | <b>RMB</b>  | <b>RMB</b>  |
| Provision for Hong Kong profits tax on the estimated assessable profits for the year  |                                |             | 3           |
| Under-provision in respect of Hong Kong profits tax for prior year                    |                                |             | 9           |
| Provision for PRC enterprise income tax on the estimated taxable profits for the year | 20,145                         | 27,487      | 31,802      |
| Over-provision in respect of PRC enterprise income tax for prior years                | (357)                          | (247)       | (550)       |
|   | 19,788                         | 27,240      | 31,264      |
| Origination and reversal of temporary differences (note 22)                           | (608)                          | (2,565)     | (470)       |
|   | 19,180                         | 24,675      | 30,794      |

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***11 Income tax (continued)**

The provision for income tax differs from the amount computed by applying the PRC statutory income tax rate of 33% to profit before tax for the following reasons:

|   | <i>Year ended December 31,</i> |             |             |
|---|--------------------------------|-------------|-------------|
|   | <i>2004</i>                    | <i>2005</i> | <i>2006</i> |
|   | <b>RMB</b>                     | <b>RMB</b>  | <b>RMB</b>  |
| Expected PRC taxation at statutory tax rates  | 20,114                         | 25,827      | 31,980      |
| Non-taxable item  |                                |             |             |
| - Interest income   | (26)                           | (24)        | (34)        |
| Non-deductible expenses on PRC operations   | 635                            | 711         | 1,068       |
| Non-deductible expenses on Hong Kong operations   | 217                            | 180         | 236         |
| Rate differential on PRC operations   | (1,390)                        | (1,801)     | (1,986)     |
| Rate differential on Hong Kong operations   | 166                            | 123         | 175         |
| Reversal of deferred taxation due to change of tax rate on certain PRC operating subsidiaries | (13)                           | (1)         | (56)        |
| Over-provision for PRC operations in prior years  | (357)                          | (247)       | (550)       |
| Under-provision for Hong Kong operations in prior year  |                                |             | 9           |
| Others  | (166)                          | (93)        | (48)        |
| Income tax  | 19,180                         | 24,675      | 30,794      |

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***12 Dividends****(a) Dividends attributable to the year:**

|  | <i>Year ended December 31,</i> |               |               |
|--|--------------------------------|---------------|---------------|
|  | <i>2004</i>                    | <i>2005</i>   | <i>2006</i>   |
|  | <b>RMB</b>                     | <b>RMB</b>    | <b>RMB</b>    |
| Ordinary interim dividend declared and paid of HK\$0.62 (equivalent to approximately RMB0.64) (2004: HK\$0.20 (equivalent to approximately RMB0.21); 2005: HK\$0.45 (equivalent to approximately RMB0.47)) per share                     | 4,175                          | 9,259         | 12,612        |
| Special interim dividend declared and paid of HK\$0.09 (equivalent to approximately RMB0.09) (2004: nil; 2005: nil) per share  |                                |               | 1,831         |
| Ordinary final dividend proposed after the balance sheet date of HK\$0.763 (equivalent to approximately RMB0.767) (2004: HK\$0.46 (equivalent to approximately RMB0.49); 2005: HK\$0.57 (equivalent to approximately RMB0.59)) per share | 9,614                          | 11,767        | 15,327        |
| Special final dividend proposed after the balance sheet date of HK\$0.069 (equivalent to approximately RMB0.069) (2004: nil; 2005: nil) per share  |                                |               | 1,386         |
|  | <b>13,789</b>                  | <b>21,026</b> | <b>31,156</b> |

The proposed ordinary and special final dividends which are declared in Hong Kong dollars are translated into RMB at the rate HK\$1 = RMB1.00467, being the rate announced by the State Administration of Foreign Exchange in the PRC on December 31, 2006. As the ordinary and special final dividend are declared after the balance sheet date, such dividends are not recognized as liabilities at December 31, 2006.

**(b) Dividends attributable to the previous financial year, approved and paid during the year:**

|   | <i>2004</i> | <i>2005</i> | <i>2006</i> |
|---|-------------|-------------|-------------|
|   | <b>RMB</b>  | <b>RMB</b>  | <b>RMB</b>  |
| Final dividend in respect of the previous financial year, approved and paid during the year, of HK\$0.57 (equivalent to approximately RMB0.59) (2004: HK\$0.20 (equivalent to approximately RMB0.21); 2005: HK\$0.46 (equivalent to approximately RMB0.49)) per share | 4,174       | 9,635       | 11,719      |

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***13 Amounts due from/to ultimate holding company and amount due to immediate holding company**

Amounts due from/to ultimate holding company are unsecured, non-interest bearing, repayable on demand and arose in the ordinary course of business.

Amount due to immediate holding company under current liabilities represented interest payable on the deferred consideration payable (see note 26), which is expected to be settled within one year.

**14 Other receivables**

|                                       | <i>December 31,</i> |             |
|---------------------------------------|---------------------|-------------|
|                                       | <i>2005</i>         | <i>2006</i> |
|                                       | <b>RMB</b>          | <b>RMB</b>  |
| Other receivables                     | 2,021               | 2,610       |
| Less: Allowance for doubtful accounts | (110)               | (110)       |
|                                       | 1,911               | 2,500       |

Other receivables primarily comprise receivables from sales agents of revenue collected on behalf of the Group, utilities deposits and rental deposits.

All of the other receivables, except utilities deposits and rental deposits, are expected to be recovered within one year.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***14 Other receivables (continued)**

Allowance for doubtful accounts for the years is analyzed as follows:

|   | <b>RMB</b> |
|---|------------|
| At January 1, 2004                      | 113        |
| Acquired on acquisition of subsidiaries | 6          |
| Provision for the year                  | 40         |
| Written-off                             | (20)       |
| At December 31, 2004                    | 139        |
| Written-back for the year               | (19)       |
| Written-off                             | (10)       |
| At December 31, 2005                    | 110        |
| Provision for the year                  | 1          |
| Written-off                             | (1)        |
| At December 31, 2006                    | 110        |

**15 Accounts receivable**

|                                       | <i>December 31,</i> | <i>2005</i> | <i>2006</i> |
|---------------------------------------|---------------------|-------------|-------------|
|                                       | <b>RMB</b>          | <b>RMB</b>  | <b>RMB</b>  |
| Accounts receivable                   | 10,068              | 11,083      |             |
| Less: Allowance for doubtful accounts | (3,465)             | (3,930)     |             |
|                                       | 6,603               | 7,153       |             |

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***15 Accounts receivable (continued)**

Ageing analysis of accounts receivable, net of allowance for doubtful accounts, is analyzed as follows:

|                | <i>December 31,</i> |             |
|----------------|---------------------|-------------|
|                | <i>2005</i>         | <i>2006</i> |
|                | <b>RMB</b>          | <b>RMB</b>  |
| Within 30 days | 5,269               | 5,447       |
| 31-60 days     | 697                 | 911         |
| 61-90 days     | 637                 | 581         |
| Over 90 days   |                     | 214         |
|                | 6,603               | 7,153       |

Accounts receivable from customers are due for payment within one month from the date of billing. Customers with balances that are overdue or exceed credit limits are required to settle all outstanding balances before any further phone calls can be made.

All of the accounts receivable are expected to be recovered within one year.

Allowance for doubtful accounts for the years is analyzed as follows:

|   | <b>RMB</b> |
|---|------------|
| At January 1, 2004                      | 4,418      |
| Acquired on acquisition of subsidiaries | 1,074      |
| Provision for the year                  | 2,233      |
| Written-off                             | (4,072)    |
| At December 31, 2004                    | 3,653      |
| Provision for the year                  | 2,987      |
| Written-off                             | (3,175)    |
| At December 31, 2005                    | 3,465      |
| Acquired on acquisition of a subsidiary | 26         |
| Provision for the year                  | 3,851      |
| Written-off                             | (3,412)    |
| At December 31, 2006                    | 3,930      |

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***16 Inventories**

Inventories primarily comprise handsets, SIM cards and handset accessories.

**17 Property, plant and equipment**

Property, plant and equipment for the years is analyzed as follows:

|  | <i>December 31,</i> |             |
|--|---------------------|-------------|
|  | <i>2005</i>         | <i>2006</i> |
|  | <b>RMB</b>          | <b>RMB</b>  |
| Buildings  | 37,486              | 43,496      |
| Telecommunications transceivers, switching centers, transmission and other network equipment | 311,859             | 352,523     |
| Office equipment, furniture and fixtures and others  | 14,780              | 15,175      |
|  | 364,125             | 411,194     |
| Less: Accumulated depreciation   | (147,620)           | (192,920)   |
|  | 216,505             | 218,274     |

The estimated useful lives of certain existing network equipment are affected by the continuing evolution of telecommunications technology and the appearance of a large number of new technologies and services. During the first half of 2006, management reviewed the current conditions of existing network equipment and assessed the impact of the continuous evolution in telecommunications technology on that network equipment. As a result, management revised the estimated useful lives of certain network equipment from 7 years to 5 years.

The change in accounting estimate is accounted for prospectively from January 1, 2006. Effect of change in useful lives is estimated to have increased depreciation by approximately RMB11,451 and RMB8,197 for year ended December 31, 2006 and for the assets revised remaining useful lives, respectively. In addition, due to the expected changes of mobile switching technologies, including the development of soft switching technologies, to conform with the new generation mobile technologies in 2007 and for years beyond, management revised the estimated useful life of existing switching center equipment (excluding soft switching equipment, which conforms with the new generation of mobile technologies) from seven years to five years in 2007. The additional depreciation charges resulting from this revision in 2007 are estimated to be less than the additional depreciation charges resulting from our revision in the estimated useful life of our 2G wireless network equipment in 2006. As the effect of such change of depreciable lives represents a timing difference, the change of estimated useful lives does not change the total depreciation expenses of those assets during those assets' lives.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **17 Property, plant and equipment (continued)**

The Group leases certain telecommunications equipment under capital leases. None of the leases includes contingent rentals.

In connection with the Restructuring, pursuant to an approval document dated September 5, 1997 issued by China State-owned Assets Administration Bureau, the property, plant and equipment and land lease prepayments of Guangdong Mobile and Zhejiang Mobile as of May 31, 1997 were valued by Zhongqihua Assets Appraisal Company ( ZAAC ), a firm of independent valuers registered in the PRC, on a replacement cost basis. The value of property, plant and equipment and land lease prepayments of Guangdong Mobile and Zhejiang Mobile has been determined at RMB15,630 reflecting a surplus on revaluation of approximately RMB3,529.

In connection with the acquisition of Jiangsu Mobile, and pursuant to an approval document dated April 7, 1998 issued by China State-owned Assets Administration Bureau, the property, plant and equipment and land lease prepayments of Jiangsu Mobile as of December 31, 1997 were valued by ZAAC on a replacement cost basis. The value of property, plant and equipment and land lease prepayments of Jiangsu Mobile has been determined at RMB7,879 reflecting a surplus on revaluation of approximately RMB2,443.

In connection with the acquisition of Fujian Mobile, Henan Mobile and Hainan Mobile, and pursuant to an approval document dated September 27, 1999 issued by the Ministry of Finance, the property, plant and equipment and land lease prepayments of Fujian Mobile, Henan Mobile and Hainan Mobile as of June 30, 1999 were valued by China International Engineering Consulting Corporation on a replacement cost basis. The aggregate value of property, plant and equipment and land lease prepayments of Fujian Mobile, Henan Mobile and Hainan Mobile has been determined at RMB10,684 reflecting a surplus on revaluation of approximately RMB391.

In connection with the acquisition of Beijing Mobile, Shanghai Mobile, Tianjin Mobile, Hebei Mobile, Liaoning Mobile, Shandong Mobile and Guangxi Mobile, and pursuant to an approval document dated August 28, 2000 issued by the Ministry of Finance, the property, plant and equipment and land lease prepayments of Beijing Mobile, Shanghai Mobile, Tianjin Mobile, Hebei Mobile, Liaoning Mobile, Shandong Mobile and Guangxi Mobile as of June 30, 2000 were valued by China Assets Appraisal Corporation Ltd. on a replacement cost basis. The aggregate value of property, plant and equipment and land lease prepayments of Beijing Mobile, Shanghai Mobile, Tianjin Mobile, Hebei Mobile, Liaoning Mobile, Shandong Mobile and Guangxi Mobile has been determined at RMB37,252 reflecting a surplus on revaluation of approximately RMB4,823.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **17 Property, plant and equipment (continued)**

In connection with the acquisition of Anhui Mobile, Jiangxi Mobile, Chongqing Mobile, Sichuan Mobile, Hubei Mobile, Hunan Mobile, Shaanxi Mobile and Shanxi Mobile, and pursuant to an approval document dated May 15, 2002 issued by the Ministry of Finance, the property, plant and equipment and land lease prepayments of Anhui Mobile, Jiangxi Mobile, Chongqing Mobile, Sichuan Mobile, Hubei Mobile, Hunan Mobile, Shaanxi Mobile and Shanxi Mobile as of December 31, 2001 were valued by China Enterprise Appraisals (CEA) on a replacement cost basis. The aggregate value of property, plant and equipment and land lease prepayments of Anhui Mobile, Jiangxi Mobile, Chongqing Mobile, Sichuan Mobile, Hubei Mobile, Hunan Mobile, Shaanxi Mobile and Shanxi Mobile has been determined at RMB39,499 reflecting a net deficit on revaluation of approximately RMB833.

In connection with the acquisition of Neimenggu Mobile, Jilin Mobile, Heilongjiang Mobile, Guizhou Mobile, Yunnan Mobile, Xizang Mobile, Gansu Mobile, Qinghai Mobile, Ningxia Mobile, Xinjiang Mobile, Jingyi Design Institute and CMC, and pursuant to an approval document dated March 31, 2004 issued by the SASACSC, the property, plant and equipment and land lease prepayments of Neimenggu Mobile, Jilin Mobile, Heilongjiang Mobile, Guizhou Mobile, Yunnan Mobile, Xizang Mobile, Gansu Mobile, Qinghai Mobile, Ningxia Mobile, Xinjiang Mobile, Jingyi Design Institute and CMC as of December 31, 2003 were valued by CEA, China United Assets Appraisals and Zhongdi Real Estate Valuation on a replacement cost basis. The aggregate value of property, plant and equipment and land lease prepayments of Neimenggu Mobile, Jilin Mobile, Heilongjiang Mobile, Guizhou Mobile, Yunnan Mobile, Xizang Mobile, Gansu Mobile, Qinghai Mobile, Ningxia Mobile and Xinjiang Mobile has been determined at RMB33,996 reflecting a net deficit on revaluation of approximately RMB2,781.

The Group's buildings and land lease prepayments in each of the above mentioned subsidiaries were also valued separately by Chesterton Petty Limited, independent qualified valuers in Hong Kong as of May 31, 1997, December 31, 1997, June 30, 1999, June 30, 2000, December 31, 2001 and December 31, 2003 respectively. The values of such reports have been determined at approximately the same value by the independent qualified valuers in the PRC.

Other than revaluations carried out in compliance with relevant PRC rules and regulations, the Group has no plan to revalue its property, plant and equipment and land lease prepayments on a regular basis.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***17 Property, plant and equipment (continued)**

The effect of the above six revaluations is to decrease annual depreciation charges by approximately RMB1,088 (2005: approximately RMB646) and increase amortization of land lease prepayments by RMB55 (2005: approximately RMB98).

The historical cost net book value of the property, plant and equipment and land lease prepayments of these subsidiaries in the Group's financial statements as of the respective revaluation dates and the revalued basis of these property, plant and equipment and land lease prepayments are as follows:

|  | <i>Net book<br/>value<br/>RMB</i> | <i>Revalued<br/>amount<br/>RMB</i> |
|--|-----------------------------------|------------------------------------|
| Buildings  | 9,824                             | 10,348                             |
| Telecommunications transceivers, switching centers, transmission and other network equipment | 121,567                           | 126,450                            |
| Office equipment, furniture and fixtures and others  | 4,658                             | 4,397                              |
| Total property, plant and equipment  | 136,049                           | 141,195                            |
| Land lease prepayments   | 1,319                             | 3,745                              |

**18 Goodwill**

|   | <i>Goodwill<br/>RMB</i> | <i>Positive<br/>goodwill<br/>carried in<br/>reserves<br/>RMB</i> |
|---|-------------------------|--|
| <i>Cost and carrying amount:</i>                                  |                         |  |
| Balance at January 1, 2005, December 31, 2005 and January 1, 2006 | 35,300                  | 296,800  |
| Additions arising on acquisition of a subsidiary                  | 1,594                   |  |
| Balance at December 31, 2006                                      | 36,894                  | 296,800  |



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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

**18 Goodwill (continued)**

***Impairment tests for goodwill***

As set out in HKAS 36, cash generating units are the smallest identifiable group of assets that generate cash inflows from continuing use that are largely independent of the cash flows from other assets. For the purpose of impairment testing of goodwill, goodwill is allocated to a group of cash-generating units (being subsidiaries acquired in each acquisition). Such group of cash-generating units represents the lowest level within the Group at which the goodwill is monitored for internal management purposes and also is within the segment determined in accordance with HKAS 14 Segment Reporting .

The recoverable amount of the cash-generating units equals the value-in-use which is determined by the discounted cash flow method. The data from the Group's detailed planning is used to project cash flows for the subsidiaries (cash generating units) to which the goodwill relates for the five years ending December 31, 2011 with subsequent transition to perpetuity. For the years following the detailed planning period, the assumed continual growth of 0.5% for the operation in Hong Kong and 1% for operations in Mainland China to perpetuity are used which comply with general expectations for the business. The present value of cash flows is calculated by discounting with a pre-tax interest rate of approximately 11%.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***19 Other intangible assets**

|                                | <i>December 31,</i> |             |
|--------------------------------|---------------------|-------------|
|                                | <i>2005</i>         | <i>2006</i> |
|                                | <b>RMB</b>          | <b>RMB</b>  |
| Brand name                     |                     | 184         |
| Customer base                  |                     | 516         |
| Others                         |                     | 378         |
|                                |                     | 1,078       |
| Less: Accumulated amortization |                     | (378)       |
|                                |                     | 700         |

The aggregate amortization expenses for other intangible assets were RMB203 for the year ended December 31, 2006. The amortization charge for the year is included in other operating expenses in the consolidated statements of income. No amortization expenses for other intangible assets were recorded for the two years ended December 31, 2004 and 2005 since the Group did not have any other intangible assets in 2004 and 2005. Based on other intangible assets as of December 31, 2006, amortization expense will be approximately RMB207, RMB192, RMB13, RMB11 and RMB10, respectively, for five years ending December 31, 2007, 2008, 2009, 2010 and 2011.

***Impairment test for other intangible assets***

The brand name resulted from the acquisition in current year and assessed to be indefinite. The factors considered in the assessment of the useful life of the brand name include analysis of market and competitive trends, product life cycles, brand extension opportunities and management's long term strategic development. Overall, these factors provided evidence that the brand name is expected to generate long-term net cash inflows to the Group indefinitely.

The recoverable amount of the brand name is estimated based on value-in-use calculations by discounted future cash flows annually. The data from the Group's detailed planning is used to project cash flows for the subsidiary (cash generating unit) to which the intangible assets relate for the five years ending December 31, 2011 with subsequent transition to perpetuity. For the years following the detailed planning period, the assumed continual growth of 0.5% perpetuity is used which complies with general expectations for the business. The present value of cash flows is calculated by discounting with a pre-tax interest rate of approximately 11%.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***20 Interest in associates**

*December 31,*  
**2005      2006**  
**RMB      RMB**

|                     |
|---------------------|
| Share of net assets |
|---------------------|

Details of the associates, all of which are unlisted corporate entities, are as follows:

| <i>Name of associate</i>                     | <i>Place of<br/>incorporation<br/>and operation</i> | <i>Proportion of<br/>ownership<br/>interest held<br/>by the subsidiary</i> | <i>Principal activity</i>                      |
|--|---|--|--|
| China Motion United Telecom Limited          | Hong Kong   | 30%  | Provision of<br>telecommunications<br>services |
| Shenzhen China Motion Telecom United Limited | PRC   | 30%  | Provision of<br>telecommunications<br>services |

Owing to the lack of recent audited financial statements of the associates, the Group's share of the associates' net assets are based on latest management accounts which showed net liabilities as at December 31, 2005 and 2006. The Group has made full impairment loss on the cost of investment in the associates in 2005 and 2006.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***21 Other financial assets**

|  | <i>December 31,</i> |             |
|--|---------------------|-------------|
|  | <i>2005</i>         | <i>2006</i> |
|  | <b>RMB</b>          | <b>RMB</b>  |
| <b>Available-for-sale equity securities:</b> |                     |             |
| - Unlisted equity securities in the PRC      | 77                  | 77          |

**22 Deferred tax assets and liabilities**

- (a) The components of deferred tax assets/(liabilities) recognized in the consolidated balance sheet and the movements during the year for the Group are as follows:

*Deferred tax assets and liabilities recognized and the movements during 2005*

|   | <i>At<br/>January 1,<br/>2005<br/>RMB</i> | <i>Credited/<br/>(charged) to<br/>consolidated<br/>statements<br/>of income<br/>RMB</i> | <i>At<br/>December 31,<br/>2005<br/>RMB</i> |
|---|---|---|---|
| Deferred tax assets arising from:                         |   |   |   |
| Provision for obsolete inventories                        | 30  | (21)  | 9   |
| Write-off of certain network equipment and related assets | 2,226                                     | 1,739   | 3,965                                       |
| Income recognition on prepaid service fees                | 42  | (42)  |   |
| Provision for certain operating expenses                  | 876                                       | 804   | 1,680                                       |
| Allowance for doubtful accounts                           | 894                                       | 77  | 971   |
|   | 4,068                                     | 2,557   | 6,625                                       |
| Deferred tax liabilities arising from:                    |   |   |   |
| Capitalized interest                                      | (105)                                     | 8   | (97)  |
| Total   | 3,963                                     | 2,565   | 6,528                                       |

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***22 Deferred tax assets and liabilities (continued)***Deferred tax assets and liabilities recognized and the movements during 2006*

|   | <i>At<br/>January 1,<br/>2006<br/>RMB</i> | <i>Acquired<br/>on<br/>acquisition<br/>of a<br/>subsidiary<br/>RMB</i> | <i>Credited/<br/>(charged) to<br/>consolidated<br/>statements<br/>of income<br/>RMB</i> | <i>Exchange<br/>difference<br/>RMB</i> | <i>At<br/>December 31,<br/>2006<br/>RMB</i> |
|---|---|--|---|--|---|
| Deferred tax assets arising from:                         |   |  |   |  |   |
| Provision for obsolete inventories                        | 9   |  | (1)   |  | 8   |
| Write-off of certain network equipment and related assets | 3,965                                     |  | (1,195)   |  | 2,770                                       |
| Provision for certain operating expenses                  | 1,680                                     |  | 1,485   |  | 3,165                                       |
| Allowance for doubtful accounts                           | 971                                       |  | 199   |  | 1,170                                       |
|   | 6,625                                     |  | 488   |  | 7,113                                       |
| Deferred tax liabilities arising from:                    |   |  |   |  |   |
| Capitalized interest                                      | (97)                                      |  | 17  |  | (80)  |
| Depreciation allowance in excess of related depreciation  |   | (80)   | (35)  | 3                                      | (112)                                       |
|   | (97)                                      | (80)   | (18)  | 3                                      | (192)                                       |
| Total   | 6,528                                     | (80)   | 470   | 3                                      | 6,921                                       |

|   | <b>December 31,<br/>2005<br/>RMB</b> | <b>2006<br/>RMB</b> |
|---|--------------------------------------|---------------------|
| Net deferred tax assets recognized in the consolidated balance sheet      | 6,625                                | 7,113               |
| Net deferred tax liabilities recognized in the consolidated balance sheet | (97)                                 | (192)               |
|   | 6,528                                | 6,921               |

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***22 Deferred tax assets and liabilities (continued)**

(b) As described in note 17, in connection with the Restructuring and the subsequent acquisitions, the property, plant and equipment of Guangdong Mobile and Zhejiang Mobile and the acquired subsidiaries were revalued on different basis dates. Such revalued amounts would serve as the tax base for these assets for future years. As a result, the timing differences that gave rise to the potential net deferred tax liabilities of these subsidiaries relating to the revaluation of property, plant and equipment of totaling RMB6,732 were eliminated. In addition, in connection with the Fifth Acquisition, the tax base of the acquired subsidiaries' assets and liabilities have been adjusted to conform to the related financial carrying amounts. As a result, the timing differences that gave rise to the potential net deferred tax assets of these subsidiaries relating to the temporary differences allowance for doubtful accounts and capitalized interest of totaling RMB105 were eliminated.

Additionally, the tax losses carried forward relating to Liaoning Mobile and Guangxi Mobile, Chongqing Mobile and Sichuan Mobile, and Jilin Mobile, Xinjiang Mobile, Jingyi Design Institute and CMC of RMB72, RMB378 and RMB228 were eliminated as of June 30, 2000, December 31, 2001 and December 31, 2003 respectively.

**23 Accounts payable**

Accounts payable primarily include payables for network expansion projects expenditure, leased lines and interconnection expenses.

The ageing analysis of accounts payable as of December 31 is analyzed as follows:

|                               | <i>December 31,</i> |             |
|-------------------------------|---------------------|-------------|
|                               | <i>2005</i>         | <i>2006</i> |
|                               | <b>RMB</b>          | <b>RMB</b>  |
| Amounts payables in the next: |                     |             |
| 1 month or on demand          | 27,493              | 41,026      |
| 2 3 months                    | 4,599               | 5,629       |
| 4 6 months                    | 3,675               | 4,067       |
| 7 9 months                    | 1,448               | 2,086       |
| 10 12 months                  | 4,716               | 4,432       |
|                               | 41,931              | 57,240      |

The accounts payable are expected to be settled within one year.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***24 Deferred revenue**

Deferred revenue includes primarily prepaid service fees received from subscribers and deferred tax credit of purchase of domestic telecommunications equipment. Prepaid service fees are recognized as revenue when the mobile telecommunications services are rendered upon actual usage by subscribers. Deferred tax credit of purchase of domestic telecommunications equipment is amortized as non-operating income over the remaining lives of the related property, plant and equipment.

|   | <i>December 31,</i> |             |
|---|---------------------|-------------|
|   | <i>2005</i>         | <i>2006</i> |
|   | <b>RMB</b>          | <b>RMB</b>  |
| Balance at beginning of year                        | 13,880              | 18,299      |
| Additions during the year                           | 105,407             | 130,477     |
| Recognized in the consolidated statements of income | (100,988)           | (126,023)   |
| Balance at end of year                              | 18,299              | 22,753      |
| Less: Current portion                               | (16,975)            | (21,823)    |
| Non-current portion                                 | 1,324               | 930         |

**25 Accrued expenses and other payables**

|                                      | <i>December 31,</i> |             |
|--------------------------------------|---------------------|-------------|
|                                      | <i>2005</i>         | <i>2006</i> |
|                                      | <b>RMB</b>          | <b>RMB</b>  |
| Other payables                       | 9,030               | 8,071       |
| Receipts in advance                  | 23,856              | 27,147      |
| Accrued salaries, wages and benefits | 2,200               | 2,643       |
| Accrued expenses                     | 4,921               | 8,269       |
|                                      | 40,007              | 46,130      |

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***26 Interest-bearing borrowings**

|                                | Note | December 31, |             |        |             |              |         |
|--------------------------------|------|--------------|-------------|--------|-------------|--------------|---------|
|                                |      | 2005<br>Non- | current     | Total  | Current     | 2006<br>Non- | current |
|                                |      | liabilities  | liabilities | RMB    | liabilities | liabilities  | Total   |
|                                |      | RMB          | RMB         |        | RMB         | RMB          | RMB     |
| Bonds                          | (a)  |              | 12,912      | 12,912 | 2,996       | 9,941        | 12,937  |
| Deferred consideration payable | (b)  |              | 23,633      | 23,633 |             | 23,633       | 23,633  |
|                                |      |              | 36,545      | 36,545 | 2,996       | 33,574       | 36,570  |

All of the above interest-bearing borrowings are unsecured and are not expected to be settled within one year except the bonds under current liabilities, which will mature in 2007 (see note 26(a)(ii)).

**(a) Bonds**

- (i) On June 18, 2001, Guangdong Mobile issued guaranteed bonds with a principal amount of RMB5,000 (the Ten-year Bonds) at an issue price equal to the face value of the bonds.

The Ten-year Bonds bear interest at a floating rate, adjusted annually from the first day of each interest payable year and payable annually. The bonds, redeemable at 100% of the principal amount, will mature on June 18, 2011 and the interest will be accrued up to June 17, 2011.

- (ii) On October 28, 2002, Guangdong Mobile issued five-year guaranteed bonds (the Five-year Bonds) and fifteen-year guaranteed bonds (the Fifteen-year Bonds), with a principal amount of RMB3,000 and RMB5,000 respectively, at an issue price equal to the face value of the bonds.

The Five-year Bonds and the Fifteen-year Bonds bear interest at the rate of 3.5% per annum and 4.5% per annum respectively and payable annually. They are redeemable at 100% of the principal amount and will mature on October 28, 2007 and October 28, 2017 and the interest will be accrued up to October 27, 2007 and October 27, 2017, respectively.



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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

**26 Interest-bearing borrowings (continued)**

**(a) Bonds (continued)**

- (iii) The Company has issued a joint and irrevocable guarantee (the Guarantee ) for the performance of the above bonds. CMCC, the ultimate holding company, has also issued a further guarantee in relation to the performance by the Company of its obligations under the Guarantee. The maximum exposure of the Guarantee is the face value of the bonds.

**(b) Deferred consideration payable**

This represents the balances of the deferred consideration of RMB9,976 and RMB13,657 payable to immediate holding company in respect of the acquisitions of subsidiaries in 2002 and 2004, respectively.

The deferred consideration payable is unsecured, bears interest at the rate of two-year US dollar LIBOR swap rate per annum (for the year ended December 31, 2005: 2.595 to 2.998% per annum and for the year ended December 31, 2006: 2.595 to 5.418% per annum). The balances are subordinated to other senior debts owed by the Company from time to time. The Company may make early payment of all or part of the balances at any time before the repayment date without penalty. The balances in respect of the acquisitions of subsidiaries in 2002 and 2004 are due on July 1, 2017 and 2019, respectively.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***27 Obligations under capital lease**

- (i) Hainan Mobile entered into certain capital lease agreements to finance the purchase of telecommunications equipment. The leases are denominated in Renminbi and the lease term expired in 2003. The legal title of the equipment will be transferred to Hainan Mobile when all outstanding lease payments are paid.
- (ii) The following is a schedule by years of future minimum lease payments under capital lease together with the present value of the net minimum lease payments as of December 31, 2006:

|   | <b>RMB</b> |
|---|------------|
| 2007  | 71         |
| Total minimum lease payments                            | 71         |
| Less: Amount representing interest                      | (3)        |
| Present value of net minimum lease payments             | 68         |
| Less: Obligations under capital lease - current portion | (68)       |

**28 Commitments and contingencies****(a) Operating leases**

Future minimum lease payments as of December 31, 2006 under non-cancelable operating leases having initial or remaining lease terms of more than one year are as follows:

|            | <b>RMB</b> |
|------------|------------|
| 2007       | 4,644      |
| 2008       | 2,689      |
| 2009       | 1,835      |
| 2010       | 1,407      |
| 2011       | 1,040      |
| Thereafter | 2,057      |
|            | 13,672     |

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***28 Commitments and contingencies (continued)****(b) Capital commitments**

As of December 31, 2006, the Group had capital commitments as follows:

|                                   | <b>RMB</b> |
|-----------------------------------|------------|
| Authorized and contracted for     | 10,480     |
| Authorized but not contracted for | 58,292     |
|                                   | 68,772     |

**29 Employee retirement benefits**

**(a)** As stipulated by the regulations of Mainland China, the subsidiaries in Mainland China participate in basic defined contribution pension plans organized by their respective Municipal Governments under which they are governed.

Employees in Mainland China are entitled to retirement benefits equal to a fixed proportion of their salary at their normal retirement age. The Group has no other material obligation for payment of basic retirement benefits beyond the annual contributions which are calculated at a rate based on the salaries, bonuses and certain allowances of its employees.

Other than the above, certain subsidiaries also participate in supplementary defined contribution retirement plans managed by independent insurance companies whereby the subsidiaries are required to make contributions to the retirement plans at fixed rates of the employees' salary costs or in accordance with the terms of the plans.

Expenses incurred by the subsidiaries in connection with the retirement scheme were RMB771, RMB886 and RMB1,149, respectively, for three years ended December 31, 2004, 2005 and 2006, respectively.

**(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\$0.02. Contributions to the scheme vest immediately.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***30 Related party transactions****(a) Transactions with CMCC Group**

Following the completion of acquisition of the ten mobile telecommunications companies and other mobile telecommunications assets on July 1, 2004, the Group operates the mobile telecommunications services in all thirty-one provinces, autonomous regions and directly administered municipalities in the PRC. Prior to the acquisition, transactions entered into by the Group with the subsidiaries previously directly owned by the Company's ultimate holding company, CMCC, are considered as related party transactions. Following the acquisition, as these subsidiaries now become the members of the Group, these transactions are eliminated on a consolidated basis and therefore are not considered as related party transactions.

The following is a summary of principal related party transactions entered into by the Group with CMCC and its subsidiaries, excluding the Group (the CMCC Group), for the year ended December 31, 2005 and 2006.

|  | <i>Note</i> | <i>Year ended December 31,</i> |             |
|--|-------------|--------------------------------|-------------|
|  |             | <i>2005</i>                    | <i>2006</i> |
|  |             | <b>RMB</b>                     | <b>RMB</b>  |
| Property leasing and management services charges | (i)         | 589                            | 804         |
| Telecommunications services charges              | (ii)        | 1,866                          | 2,359       |
| Interest paid/payable                            | (iii)       | 647                            | 946         |

-

Notes:

- (i) Property leasing and management services charges represent the rental and property management fees paid or payable to CMCC Group in respect of business premises and offices, retail outlets, warehouses and synchronized clock ports.
- (ii) Telecommunications services charges represent the amounts paid or payable to CMCC Group for the telecommunications project planning, design and construction services; telecommunications line and pipeline construction services; and telecommunications line maintenance services.
- (iii) Interest paid/payable represents the interest paid or payable to CMHK (BVI), the Company's immediate holding company, in respect of the balances of purchase consideration for acquisition of subsidiaries.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***30 Related party transactions (continued)****(a) Transactions with CMCC Group (continued)**

The following is a summary of principal related party transactions carried out by the Group with CMCC Group for the year ended December 31, 2004.

|  | <i>Note</i> | <b>RMB</b> |
|--|-------------|------------|
| Interconnection revenue  | (i)         | 2,438      |
| Interconnection charges  | (ii)        | 2,117      |
| Leased line charges  | (iii)       | 132        |
| Spectrum fees  | (iv)        | 303        |
| Operating lease charges  | (v)         | 281        |
| Roaming billing processing fees  | (vi)        | 22         |
| Equipment maintenance service fees   | (vii)       | 81         |
| Construction and related service fees  | (viii)      | 287        |
| Purchase of transmission tower and transmission tower-related service and antenna maintenance service fees | (ix)        | 148        |
| Prepaid card sales commission income   | (x)         | 142        |
| Prepaid card sales commission expenses   | (x)         | 155        |
| Technology platform development and maintenance service income   | (xi)        | 25         |
| Telecommunications lines maintenance service fees  | (xii)       | 54         |
| Interest paid / payable  | (xiii)      | 645        |

Notes:

- (i) A mobile telephone user using roaming services is charged at the respective roaming usage rate and applicable long distance charges for roaming in calls. Interconnection revenue represents domestic and international roaming in usage charges and applicable long distance charges from non-subscribers received or receivable from the relevant domestic and international mobile telecommunication operators through the CMCC Group.
- (ii) A mobile telephone user using roaming services is charged at the respective roaming usage rate and applicable long distance charges for roaming out calls. Interconnection charges represent the amount of domestic and international roaming out charges and applicable long distance charges received or receivable from subscribers which are to be remitted to the relevant domestic and international mobile telecommunication operators for their share of revenue through the CMCC Group.
- (iii) Leased line charges represent expenses paid or payable to the CMCC Group for the use of inter-provincial leased lines which link the Group's mobile switching centers together and with other mobile switching centers of the CMCC Group.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **30 Related party transactions (continued)**

#### ***(a) Transactions with CMCC Group (continued)***

Notes: (continued)

- (iv) Spectrum fees represent the spectrum usage fees paid or payable to the CMCC Group for the usage of the frequency bands allocated to the Company's subsidiaries in the PRC.
- (v) Operating lease charges represent the rental and property management fees paid or payable to the subsidiaries of CMCC for operating leases in respect of land and buildings and others.
- (vi) Roaming billing processing fees represent the amounts paid or payable to the CMCC Group for the provision of the roaming billing processing services to the Company's subsidiaries.
- (vii) Equipment maintenance service fees represent the amount paid or payable to subsidiaries of CMCC for the provision of the maintenance services to the Company's subsidiaries.
- (viii) Construction and related service fees represent the amount paid or payable to subsidiaries of CMCC for the provision of telecommunications projects planning, design and construction services and telecommunications lines and pipelines construction services to the Company's subsidiaries.
- (ix) This represents payment made by Hebei Mobile to acquire transmission towers from a subsidiary of CMCC and expenses paid or payable to relevant subsidiary of CMCC for the provision of transmission towers related services and antenna maintenance services provided to Hebei Mobile; and payment made by the Group to Hubei Communication Services Company, a subsidiary of CMCC, in respect of the purchase of transmission towers and for the provision of transmission tower related services.
- (x) Prepaid card sales commission income and commission expenses represent handling charges received/receivable from subsidiaries of CMCC to the Company's subsidiaries or paid/payable by the Company's subsidiaries to subsidiaries of CMCC in respect of prepaid card services.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **30 Related party transactions (continued)**

#### ***(a) Transactions with CMCC (continued)***

Notes: (continued)

- (xi) Technology platform development and maintenance service income represents the amounts received or receivable from the CMCC Group in respect of equipment charges, systems integration fees, software licensing fees, technical support fees and/or major overhaul charges for the mobile information service center platform.
  - (xii) Telecommunications lines maintenance service fees represent the amount paid or payable by Anhui Mobile, Jiangxi Mobile, Chongqing Mobile, Sichuan Mobile, Hubei Mobile, Hunan Mobile, Shaanxi Mobile and Shanxi Mobile to the relevant subsidiaries of CMCC for the provision of telecommunications lines maintenance services.
  - (xiii) Interest paid/payable represents the interest paid or payable to CMCC and CMHK (BVI) in respect of the designated loans borrowed and the balance of purchase consideration for acquisition of subsidiaries.
- (b)** Pursuant to a resolution passed at the extraordinary general meeting held on June 16, 2004, the Company acquired the entire issued share capital of Neimenggu Mobile BVI, Jilin Mobile BVI, Heilongjiang Mobile BVI, Guizhou Mobile BVI, Yunnan Mobile BVI, Xizang Mobile BVI, Gansu Mobile BVI, Qinghai Mobile BVI, Ningxia Mobile BVI, Xinjiang Mobile BVI, Zhongjing Design Institute BVI and CMC BVI from CMHK (BVI), the immediate holding company of the Company, for a total consideration of US\$3,650 (RMB equivalent 30,210). The total consideration was satisfied by cash. The only assets of each of Neimenggu Mobile BVI, Jilin Mobile BVI, Heilongjiang Mobile BVI, Guizhou Mobile BVI, Yunnan Mobile BVI, Xizang Mobile BVI, Gansu Mobile BVI, Qinghai Mobile BVI, Ningxia Mobile BVI, Xinjiang Mobile BVI, Zhongjing Design Institute BVI and CMC BVI are their interests in the entire equity of Neimenggu Mobile, Jilin Mobile, Heilongjiang Mobile, Guizhou Mobile, Yunnan Mobile, Xizang Mobile, Gansu Mobile, Qinghai Mobile, Ningxia Mobile, Xinjiang Mobile, Jingyi Design Institute and CMC respectively.

#### ***(c) Key management personnel remuneration***

Remuneration for key management personnel is disclosed in note 9.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***31 Transactions with other state-controlled entities in the PRC**

Apart from transactions with the CMCC Group (see note 30), the Group, a state-controlled enterprise, conducts certain business activities with enterprises directly or indirectly owned or controlled by the PRC government and government authorities and agencies (collectively referred to as state-controlled entities) in the ordinary course of business. These transactions primarily include rendering and receiving services, sales and purchase of goods and deposits with financial institutions, are carried out at terms similar to those that would be entered into with non-state-controlled entities and have been reflected in the consolidated financial statements.

As part of the transactions with state-controlled entities as mentioned above, the Group has material transactions with other state-controlled telecommunications operators in the PRC in the normal course of providing telecommunications services. These transactions are conducted and settled in accordance with rules and regulations stipulated by the MII of the PRC Government. Additionally, the Group has material transactions and balances with state-controlled financial institutions.

Set out below are the principal transactions with state-controlled telecommunications operators and state-controlled financial institutions in the PRC:

**(a) Principal transactions with state-controlled telecommunications operators in the PRC:**

|                         | <i>Year ended December 31,</i> |             |             |
|-------------------------|--------------------------------|-------------|-------------|
|                         | <i>2004</i>                    | <i>2005</i> | <i>2006</i> |
|                         | <b>RMB</b>                     | <b>RMB</b>  | <b>RMB</b>  |
| Interconnection revenue | 4,208                          | 6,196       | 8,510       |
| Interconnection charges | 10,016                         | 13,588      | 16,416      |
| Leased line charges     | 3,385                          | 3,054       | 1,757       |

**(b) Principal balances with state-controlled telecommunications operators in the PRC:**

|                                | <i>December 31,</i> |             |
|--------------------------------|---------------------|-------------|
|                                | <i>2005</i>         | <i>2006</i> |
|                                | <b>RMB</b>          | <b>RMB</b>  |
| Accounts and other receivables | 180                 | 452         |
| Accounts and other payable     | 2,172               | 1,846       |



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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***31 Transactions with other state-controlled entities in the PRC (continued)****(c) Principal transactions with state-controlled financial institutions in the PRC:**

|                 | <i>Year ended<br/>December 31,</i> |             |             |
|-----------------|------------------------------------|-------------|-------------|
|                 | <i>2004</i>                        | <i>2005</i> | <i>2006</i> |
|                 | <b>RMB</b>                         | <b>RMB</b>  | <b>RMB</b>  |
| Interest income | 997                                | 1,528       | 2,584       |

**(d) Principal balances with state-controlled financial institutions in the PRC:**

|                           | <i>December 31,</i> |             |
|---------------------------|---------------------|-------------|
|                           | <i>2005</i>         | <i>2006</i> |
|                           | <b>RMB</b>          | <b>RMB</b>  |
| Deposits with banks       | 41,787              | 82,294      |
| Cash and cash equivalents | 59,368              | 68,197      |

**32 Shareholders' equity****Share capital**

|                                       | <i>Number of<br/>ordinary<br/><br/>shares</i> | <i>Nominal<br/>amount of<br/>each ordinary<br/>share</i> | <i>Amount<br/>HK\$</i> |
|---------------------------------------|---|--|------------------------|
| <b>Authorized:</b>                    |   |  |                        |
| Balance at December 31, 2005 and 2006 | 30,000,000,000                                | HK\$ 0.10  | 3,000                  |

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***32 Shareholders equity (continued)****Share capital (continued)**

|   | <i>Number of<br/>ordinary<br/><br/>shares</i> | <i>Nominal<br/><br/>amount of<br/>each ordinary<br/><br/>share</i> | <i>Amount<br/>HK\$</i> |
|---|---|--|------------------------|
| <b><i>Issued and fully paid:</i></b>    |   |  |                        |
| Balance at January 1, 2005              | 19,700,639,399                                | HK\$ 0.10  | 1,970                  |
| Shares issued under share option scheme | 134,521,000                                   | HK\$ 0.10  | 14                     |
| Balance at December 31, 2005            | 19,835,160,399                                |  | 1,984                  |
|   |   | RMB equivalent   | 2,116                  |
| Balance at January 1, 2006              | 19,835,160,399                                | HK\$ 0.10  | 1,984                  |
| Shares issued under share option scheme | 132,654,741                                   | HK\$ 0.10  | 13                     |
| Balance at December 31, 2006            | 19,967,815,140                                |  | 1,997                  |
|   |   | RMB equivalent   | 2,130                  |

(Amounts in the following paragraphs are expressed in dollars.)

The Company was established in Hong Kong on September 3, 1997 as a limited company, with a registered share capital of HK\$10,000 divided into 100,000 shares of HK\$0.10 each, two of which were issued and credited as fully paid.

At an extraordinary general meeting of the Company held on September 27, 1997,

- (i) the authorized share capital of the Company was increased from HK\$10,000 to HK\$1,600,000,000 by the creation of an additional 15,999,900,000 shares of HK\$0.10 each; and
- (ii) 9,009,999,998 shares were credited as fully paid and issued to CMHK (BVI) for the transfer of interests in Guangdong Mobile and Zhejiang Mobile to the Company.

Pursuant to the resolutions passed on October 21, 1997, the Company issued 2,600,000,000 shares of HK\$0.10 each at HK\$11.68 per share and the shares were listed on the New York Stock Exchange and the SEHK on October 22, 1997 and October 23, 1997, respectively. On November 7, 1997, the Company issued 170,788,000 shares of HK\$0.10 each at HK\$11.68 per share by way of a placing among professional and institutional investors.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **32 Shareholders' equity (continued)**

#### ***Share capital (continued)***

(Amounts in the following paragraphs are expressed in dollars.)

Pursuant to ordinary resolutions passed at directors' meetings held on November 1, 1999 and November 3, 1999 respectively, the Company issued 560,700,000 and 84,104,000 ordinary shares of HK\$0.10 each to professional and institutional investors, at a consideration of HK\$24.10 per share, for financing the acquisition of Fujian Mobile BVI, Henan Mobile BVI and Hainan Mobile BVI.

Pursuant to an ordinary resolution passed at an extraordinary general meeting held on November 11, 1999, 1,273,195,021 ordinary shares of HK\$0.10 each were issued and credited as fully paid to CMHK (BVI), at a consideration of HK\$24.10 per share as part of the consideration for the acquisition of Fujian Mobile BVI, Henan Mobile BVI and Hainan Mobile BVI.

Pursuant to resolutions passed at directors' meetings held on November 2, 2000 and November 8, 2000 respectively, the Company issued 1,068,396,405 and 47,247,440 ordinary shares of HK\$0.10 each to professional and institutional investors, at a consideration of HK\$48 per share, for financing the acquisition of Beijing Mobile BVI, Shanghai Mobile BVI, Tianjin Mobile BVI, Hebei Mobile BVI, Liaoning Mobile BVI, Shandong Mobile BVI and Guangxi Mobile BVI.

Pursuant to ordinary resolutions passed at an extraordinary general meeting held on November 10, 2000, the Company's authorized share capital was increased to HK\$3,000,000,000 by the creation of an additional 14,000,000,000 ordinary shares of HK\$0.10 each, ranking pari passu with the existing shares of the Company, and 3,779,407,375 ordinary shares of HK\$0.10 each were issued and credited as fully paid to CMHK (BVI), at a consideration of HK\$48 per share as part of the consideration for the acquisition of Beijing Mobile BVI, Shanghai Mobile BVI, Tianjin Mobile BVI, Hebei Mobile BVI, Liaoning Mobile BVI, Shandong Mobile BVI and Guangxi Mobile BVI.

Pursuant to a resolution passed at a directors' meeting held on May 16, 2002, the Company issued 236,634,212 ordinary shares of HK\$0.10 each to Vodafone Holdings (Jersey) Limited, at a consideration of HK\$24.7217 per share, for financing the acquisition of Anhui Mobile BVI, Jiangxi Mobile BVI, Chongqing Mobile BVI, Sichuan Mobile BVI, Hubei Mobile BVI, Hunan Mobile BVI, Shaanxi Mobile BVI and Shanxi Mobile BVI.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **32 Shareholders equity (continued)**

#### ***Share capital (continued)***

(Amounts in the following paragraphs are expressed in dollars.)

Pursuant to an ordinary resolution passed at an extraordinary general meeting held on June 24, 2002, 827,514,446 ordinary shares of HK\$0.10 each were issued and credited as fully paid to CMHK (BVI) at HK\$24.7217 per share as part of the consideration of the acquisition of Anhui Mobile BVI, Jiangxi Mobile BVI, Chongqing Mobile BVI, Sichuan Mobile BVI, Hubei Mobile BVI, Hunan Mobile BVI, Shaanxi Mobile BVI and Shanxi Mobile BVI.

The holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at meetings of the Company. All ordinary shares rank equally with regard to the Company's residual assets.

#### ***Reserves***

##### ***Capital reserve***

This amount represents the total of the following:

the additional earnings of Guangdong Mobile and Zhejiang Mobile from June 1, 1997 to September 26, 1997, the completion date of the Restructuring (December 31, 2005 and 2006: RMB1,135);

goodwill arising on the acquisition of Jiangsu Mobile BVI and Jiangsu Mobile on June 3, 1998 (December 31, 2005 and 2006: RMB15,569), which has been eliminated against capital reserve immediately upon acquisition;

goodwill arising on the acquisition of Fujian Mobile BVI, Henan Mobile BVI, Hainan Mobile BVI, Fujian Mobile, Henan Mobile and Hainan Mobile on November 11, 1999 (December 31, 2005 and 2006: RMB42,340), which has been eliminated against capital reserve immediately upon acquisition;

goodwill arising on the acquisition of Beijing Mobile BVI, Shanghai Mobile BVI, Tianjin Mobile BVI, Hebei Mobile BVI, Liaoning Mobile BVI, Shandong Mobile BVI, Guangxi Mobile BVI, Beijing Mobile, Shanghai Mobile, Tianjin Mobile, Hebei Mobile, Liaoning Mobile, Shandong Mobile and Guangxi Mobile on November 12, 2000 (December 31, 2005 and 2006: RMB238,891), which has been eliminated against capital reserve immediately upon acquisition; and

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **32 Shareholders' equity (continued)**

#### ***Reserves (continued)***

##### ***Capital reserve (continued)***

the fair value of the actual or estimated number of unexercised share options granted to employees of the Company recognized in accordance with the accounting policy adopted for share-based payments in note 2(t)(ii) (December 31, 2005: RMB 1,255 and December 31, 2006: RMB3,031);

##### ***PRC statutory reserves***

PRC statutory reserves include general reserve, enterprise expansion fund, statutory surplus reserve and statutory public welfare fund.

In accordance with Accounting Regulations for Business Enterprises, foreign investment enterprises in Mainland China are required to transfer at least 10% of their profit after taxation, as determined under accounting principles generally accepted in the PRC ( PRC GAAP ) to the general reserve until the balance of the general reserve is equal to 50% of their registered capital. Moreover, they are required to transfer a certain percentage of their profit after taxation, as determined under PRC GAAP, to the enterprise expansion fund. During the year, appropriations were made by each of the above subsidiaries to the general reserve and the enterprise expansion fund each at 10% of their profit after taxation determined under PRC GAAP.

The general reserve can be used to reduce previous years' losses and to increase the capital of the subsidiaries while the enterprise expansion fund can be used to increase the capital of the subsidiaries, to acquire property, plant and equipment and to increase current assets.

At December 31, 2000, Shanghai Mobile has not yet registered as a wholly-foreign owned enterprise. As a result, appropriations were made by Shanghai Mobile, according to its Articles of Association to the statutory surplus reserve and the statutory public welfare fund both at 10% of its profit after taxation determined under PRC GAAP during the year ended December 31, 2000.

Statutory surplus reserve can be used to reduce previous years' losses, if any, and may be converted into paid-up capital, provided that the balance after such conversion is not less than 25% of the registered capital of the subsidiaries. Statutory public welfare fund can only be utilized on capital items for the collective benefits of the employees such as the construction of staff quarters and other staff welfare facilities. This reserve is non-distributable other than in liquidation.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **32 Shareholders equity (continued)**

#### ***Reserves (continued)***

##### ***PRC statutory reserves (continued)***

At December 31, 2005 and 2006, the balances of the general reserve, enterprise expansion fund, statutory surplus reserve and statutory public welfare fund were RMB24,035 and RMB30,836, RMB29,325 and RMB36,098, RMB31 and RMB26 and RMB4 and RMB1, respectively.

##### ***Exchange reserve***

The exchange reserve comprises all foreign exchange differences arising from the translation of the financial statements of foreign operations. The reserve is dealt with in accordance with the accounting policies set out in note 2(q).

##### ***Distributable reserves***

At December 31, 2005 and 2006, the amount of distributable reserves of the Company amounted to RMB64,441 and RMB65,806.

### **33 Equity compensation benefits**

Pursuant to a resolution passed an annual general meeting held on June 24, 2002, the share option scheme established on October 8, 1997 (the Old Scheme ) was terminated and the current share option scheme (the Current Scheme ) was adopted.

Under the Old Scheme, the directors of the Company may, at their discretion, invite employees, including executive directors of the Company or any of its subsidiaries, to take up options to subscribe for shares of the Company. Under the Current Scheme, the directors of the Company may, at their discretion, invite employees, including executive directors and non-executive directors of the Company, any of its holding companies and any of their respective subsidiaries and any entity in which the Company or any of its subsidiaries holds any equity interest, to take up options to subscribe for shares of the Company.

The maximum aggregate number of shares which can be subscribed pursuant to options that are or may be granted under the above schemes equals to 10% of the total issued share capital of the Company as at the date of adoption of the Current Scheme. Options lapsed or canceled in accordance with the terms of the Old Scheme or the Current Scheme will not be counted for the purpose of calculating this 10% limit. The consideration payable for the grant of option under each of the Old Scheme and the Current Scheme is HK\$1.00.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **33 Equity compensation benefits (continued)**

For options granted before September 1, 2001 under the Old Scheme, the exercise price of options was determined by the directors of the Company at their discretion provided that such price may not be set below a minimum price which is the higher of:

- (i) the nominal value of a share; and
- (ii) 80% of the average of the closing price of the share on the SEHK on the five trading days immediately preceding the date on which the option was granted.

With effect from September 1, 2001, the SEHK requires that the exercise price of options to be at least the higher of the nominal value of a share, the closing price of the shares on the SEHK on the date on which the option was granted and the average closing price of the shares on the SEHK for the five trading days immediately preceding the date on which the option was granted.

For options granted under the Current Scheme, the exercise price of options shall be determined by the directors of the Company at their discretion provided that such price may not be set below a minimum price which is the highest of:

- (i) the nominal value of a share;
- (ii) the closing price of the shares on the SEHK on the date on which the option was granted; and
- (iii) the average closing price of the shares on the SEHK for the five trading days immediately preceding the date on which the option was granted.

Under both the Old Scheme and the Current Scheme, the term of the option is determined by the directors at their discretion, provided that all options shall be exercised within 10 years after the adoption of the scheme (in the case of the Old Scheme) and within 10 years after the date on which the option is granted (in the case of the Current Scheme).



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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***33 Equity compensation benefits (continued)**

- (a) *The terms and conditions of the grants that existed during the years are as follows, whereby all options are settled by physical delivery of shares:*

|                             | Number of instruments |           |   | Contractual<br>life of<br>options |
|-----------------------------|-----------------------|-----------|---|-----------------------------------|
|                             | 2005                  | 2006      | Vesting conditions  |                                   |
| Option granted to directors |                       |           |   |                                   |
| - on November 26, 1999 *    | 2,000,000             |           | 50% on date of grant,<br><br>50% three years from the date of grant   | 8 years                           |
| - on April 25, 2000         | 1,516,000             | 1,000,000 | 50% two years from the date of grant,<br>50% five years from the date of grant  | 7 years                           |
| - on June 22, 2001          | 142,500               | 250       | 50% two years from the date of grant,<br>50% five years from the date of grant  | 6 years                           |
| - on July 3, 2002           | 375,000               | 370,000   | 50% two years from the date of grant,<br>50% five years from the date of grant  | 10 years                          |
| - on October 28, 2004       | 1,518,000             | 908,200   | 40% one year from the date of grant, 30%<br>two years from the date of grant, 30%<br>three years from the date of grant | 10 years                          |
| - on December 21, 2004      | 600,000               | 515,000   | 40% one year from the date of grant, 30%<br>two years from the date of grant, 30%<br>three years from the date of grant | 10 years                          |
| - on November 8, 2005       | 7,790,000             | 6,465,500 | 40% one year from the date of grant, 30%<br>two years from the date of grant, 30%<br>three years from the date of grant | 10 years                          |

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***33 Equity compensation benefits (continued)***(a) The terms and conditions of the grants that existed during the years are as follows, whereby all options are settled by physical delivery of shares: (continued)*

|                                   | Number of instruments |             |   | Contractual life of options |
|-----------------------------------|-----------------------|-------------|---|-----------------------------|
|                                   | 2005                  | 2006        | Vesting conditions  |                             |
| Option granted to other employees |                       |             |   |                             |
| - on November 26, 1999*           |                       | 1,000,000   | 50% on date of grant,<br><br>50% three years from the date of grant   | 8 years                     |
| - on April 25, 2000               | 26,092,000            | 4,858,500   | 50% two years from the date of grant,<br><br>50% five years from the date of grant  | 7 years                     |
| - on June 22, 2001                | 52,390,750            | 7,542,550   | 50% two years from the date of grant,<br><br>50% five years from the date of grant  | 6 years                     |
| - on July 3, 2002                 | 75,570,000            | 71,864,350  | 50% two years from the date of grant,<br><br>50% five years from the date of grant  | 10 years                    |
| - on October 28, 2004             | 213,121,500           | 156,838,619 | 40% one year from the date of grant,<br><br>30% two years from the date of grant,<br><br>30% three years from the date of grant | 10 years                    |
| - on November 8, 2005             | 281,578,500           | 275,800,490 | 40% one year from the date of grant,<br><br>30% two years from the date of grant,<br><br>30% three years from the date of grant | 10 years                    |
| Total share options               | 662,694,250           | 527,163,459 |   |                             |

\* The number of shares involved in the options outstanding at the beginning of the year included 1,000,000 share options granted to Mr. He Ning, who was resigned as executive director and vice president of the Company during the year.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***33 Equity compensation benefits (continued)***(b) The number and weighted average exercise prices of share options are as follows:*

|                               | <b>December 31,</b>   |   | <b>December 31,</b>   |   |
|-------------------------------|---|---|---|---|
|                               | <b>2005</b>   | <b>2005</b>   | <b>2006</b>   | <b>2006</b>   |
|                               | <b>Weighted<br/>average<br/>exercise<br/>price<br/>HK\$</b> | <b>Number of<br/>shares<br/>involved<br/>in the options</b> | <b>Weighted<br/>average<br/>exercise<br/>price<br/>HK\$</b> | <b>Number of<br/>shares<br/>involved<br/>in the options</b> |
| Balance at beginning of year  | 25.39   | 511,060,000   | 29.76   | 662,694,250   |
| Granted                       | 34.87   | 289,777,500   |   |   |
| Exercised                     | 24.13   | (134,521,000)   | 30.11   | (132,654,741)   |
| Canceled                      | 30.38   | (3,622,250)   | 32.36   | (2,876,050)   |
| Balance at end of year        | 29.76   | 662,694,250   | 29.66   | 527,163,459   |
| Option vested at December 31, | 31.19   | 94,537,550  | 30.54   | 200,201,609   |

The weighted average share price at the date of exercise for shares options exercised during the year was HK\$51.16 (2005: HK\$34.20).

The options outstanding at December 31, 2005 and 2006 had exercise prices ranging from HK\$22.75 to HK\$45.04 and a weighted average remaining contractual life of 7.9 years (2005: 8.1 years).

The fair value of services received in return for share options granted are measured by reference to the fair value of share options granted. The estimate of the fair value of the services received is measured based on a binomial lattice model. The contractual life of the option is used as an input into this model. Expectations of early exercise are incorporated into the binomial lattice model. No share options were granted during 2006. The fair value of options granted during the year ended December 31, 2005 was HK\$10.28. The significant assumptions of the model included share price of HK\$34.50 at the grant date, exercise price of HK\$34.87, expected volatility (expressed as weighted average volatility used in the modeling under binomial lattice model) of 24.6%, option life (expressed as weighted average life used in the modeling under binomial lattice model) of 10 years, expected dividends of 2.6% and risk-free interest rate (based on Exchange Fund Notes) of 4.5%. The expected volatility is based on the historic volatility (calculated based on the weighted average remaining life of the share options), adjusted for any expected changes to future volatility due to publicly available information. Expected dividends are based on historical dividends and planned dividend payout ratio, if any. Changes in the subjective input assumptions could materially affect the fair value estimate.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **34 Foreign currency exchange**

The Renminbi is not freely convertible into foreign currencies. All foreign exchange transactions involving Renminbi must take place through the People's Bank of China or other institutions authorized to buy and sell foreign exchange or at a swap center.

Currently the Company's subsidiaries established in the PRC are able to purchase foreign exchange for settlement of current account transactions (as defined in the applicable regulations), including payment of dividends without the approval of the State Administration of Foreign Exchange (SAFE). However, there can be no assurance that the current authorization for foreign investment enterprises to retain their foreign exchange to satisfy foreign exchange liabilities or to pay dividends in the future will not be limited or eliminated or that the subsidiaries of the Company will be able to obtain sufficient foreign exchange to pay dividends or satisfy their foreign exchange requirements. Foreign exchange transactions under the capital account continue to be subject to limitations and require approvals of the SAFE, which could affect the ability of the Company's subsidiaries established in the PRC to obtain foreign exchange through debt or equity financing, including by means of loans or capital contribution from the Company.

### **35 Financial instruments**

Exposure to credit, liquidity, interest rate and foreign currency risks arises in the normal course of the Group's business. These risks are limited by the Group's financial management policies and practices described below.

#### ***(a) Credit risk***

Substantially all the Group's cash and cash equivalents are deposited with financial institutions in Hong Kong and Mainland China. The accounts receivable of the Group are mainly spread among an extensive number of subscribers.

The Group's credit risk is primarily attributable to accounts receivable and other receivables. Management has a credit policy in place and the exposures to these credit risks are monitored on an ongoing basis.

The maximum exposure to credit risk is represented by the carrying amount of each financial asset in the balance sheet. The Group does not have any significant exposure to any individual customer or counterparty. The credit risk on liquid funds is limited because the majority of the counter parties are financial institutions with high credit rating assigned by international credit-rating agencies and state-controlled financial institutions with good reputation.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***35 Financial instruments (continued)****(b) Liquidity risk**

The Group's policy is to regularly monitor current and expected liquidity requirements to ensure that it maintains sufficient reserves of cash to meet its liquidity requirements in the short and longer term.

**(c) Interest rate risk**

The Group has interest rate risk as certain interest-bearing borrowings are on a variable rate basis. The interest rates and terms of repayment of the interest-bearing borrowings of the Group are disclosed in note 26. The Group's cash and cash equivalents and deposits with banks are all short-term in nature, any future variations in interest rates will not have a significant impact on the results of the Group.

During the year, the Group had not entered into any interest rate swap contracts.

**(d) Foreign currency risk**

The Group has foreign currency risk as certain cash and cash equivalents are denominated in foreign currencies, principally US dollars and Hong Kong dollars. The Group does not expect any appreciation or depreciation of the Renminbi against foreign currency which might materially affect the Group's result of operations.

During the year, the Group had not entered into any forward exchange contracts.

**(e) Fair values**

The following financial assets and financial liabilities have their carrying amounts approximately equal to their fair values: accounts receivable, other receivables, prepayments and other current assets, deposits with banks, cash and cash equivalents, accounts payable, bills payable, accrued expenses and other payables and deferred consideration payable except as follows:

|                              | 2005                   |                   | 2006                   |                   |
|------------------------------|------------------------|-------------------|------------------------|-------------------|
|                              | Carrying Amount<br>RMB | Fair value<br>RMB | Carrying amount<br>RMB | Fair value<br>RMB |
| Interest-bearing borrowings: |                        |                   |                        |                   |
| - bonds                      | 12,912                 | 13,685            | 12,937                 | 13,218            |

The fair value of bonds is based on quoted market prices at the balance sheet date without any deduction for transaction costs.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***36 Principal subsidiaries**

Details of the Company's principal subsidiaries are as follows:

| <i>Name of company</i> | <i>Place and<br/>date of<br/>incorporation/<br/>establishment</i> | <i>Authorized, issued and<br/>paid up capital</i> |                           | <i>Attributable<br/>equity<br/>interest %</i> | <i>Principal<br/>activity/ies</i>        |
|------------------------|---|---|---------------------------|---|--|
|                        |   | <i>Authorized</i>                                 | <i>Issued and paid up</i> |   |  |
| Guangdong Mobile       | PRC<br>September 28,<br>1988                                      |   | RMB 5,595                 | 100%  | Mobile<br>telecommunications<br>operator |
| Zhejiang Mobile        | PRC<br>February 2,<br>1996  |   | RMB 2,118                 | 100%  | Mobile<br>telecommunications<br>operator |
| Jiangsu Mobile BVI     | BVI<br>March 6,<br>1998   | 10,000 shares<br>at HK\$1                         | 1 share at HK\$1          | 100%  | Investment holding<br>company            |
| Jiangsu Mobile         | PRC<br>December 10,<br>1992                                       |   | RMB 2,800                 | 100%  | Mobile<br>telecommunications<br>operator |
| Fujian Mobile BVI      | BVI<br>September 1,<br>1999                                       | 10,000 shares<br>at HK\$1                         | 1 share at HK\$1          | 100%  | Investment holding<br>company            |
| Fujian Mobile          | PRC<br>September 7,<br>1999                                       |   | RMB 5,247                 | 100%  | Mobile<br>telecommunications<br>operator |
| Henan Mobile BVI       | BVI<br>September 1,<br>1999                                       | 10,000 shares<br>at HK\$1                         | 1 share at HK\$1          | 100%  | Investment holding<br>company            |
| Henan Mobile           | PRC<br>August 6,<br>1999  |   | RMB 4,368                 | 100%  | Mobile<br>telecommunications<br>operator |

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|                    |                             |                           |                  |      |  |
|--------------------|-----------------------------|---------------------------|------------------|------|--|
| Hainan Mobile BVI  | BVI<br>September 1,<br>1999 | 10,000 shares<br>at HK\$1 | 1 share at HK\$1 | 100% | Investment holding<br>company            |
| Hainan Mobile      | PRC<br>August 19,<br>1999   |                           | RMB 643          | 100% | Mobile<br>telecommunications<br>operator |
| Beijing Mobile BVI | BVI<br>September 1,<br>2000 | 10,000 shares<br>at HK\$1 | 1 share at HK\$1 | 100% | Investment holding<br>company            |
| Beijing Mobile     | PRC<br>July 26, 2000        |                           | RMB6,125         | 100% | Mobile<br>telecommunications<br>operator |

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***36 Principal subsidiaries (continued)**

Details of the Company's principal subsidiaries are as follows (continued):

| <i>Name of company</i> | <i>Place and<br/>date of<br/>incorporation/<br/>establishment</i> | <i>Authorized, issued and<br/>paid up capital</i> |                           | <i>Attributable<br/>equity<br/>interest %</i> | <i>Principal<br/>activity/ies</i>        |
|------------------------|---|---|---------------------------|---|--|
|                        |   | <i>Authorized</i>                                 | <i>Issued and paid up</i> |   |  |
| Shanghai Mobile BVI    | BVI<br>September 1,<br>2000                                       | 10,000 shares<br>at HK\$1                         | 1 share at HK\$1          | 100%  | Investment holding company               |
| Shanghai Mobile        | PRC<br>August 4,<br>2000  |   | RMB6,039                  | 100%  | Mobile<br>telecommunications<br>operator |
| Tianjin Mobile BVI     | BVI<br>September 1,<br>2000                                       | 10,000 shares<br>at HK\$1                         | 1 share at HK\$1          | 100%  | Investment holding<br>company            |
| Tianjin Mobile         | PRC<br>July 24,<br>2000   |   | RMB2,151                  | 100%  | Mobile<br>telecommunications<br>operator |
| Hebei Mobile BVI       | BVI<br>September 1,<br>2000                                       | 10,000 shares<br>at HK\$1                         | 1 share at HK\$1          | 100%  | Investment holding<br>company            |
| Hebei Mobile           | PRC<br>July 31,<br>2000   |   | RMB4,315                  | 100%  | Mobile<br>telecommunications<br>operator |
| Liaoning Mobile BVI    | BVI<br>September 1,<br>2000                                       | 10,000 shares<br>at HK\$1                         | 1 share at HK\$1          | 100%  | Investment holding<br>company            |
| Liaoning Mobile        | PRC<br>August 7,<br>2000  |   | RMB5,140                  | 100%  | Mobile<br>telecommunications<br>operator |



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|                     |                             |                           |                  |      |  |
|---------------------|-----------------------------|---------------------------|------------------|------|--|
| Shandong Mobile BVI | BVI<br>September 1,<br>2000 | 10,000 shares<br>at HK\$1 | 1 share at HK\$1 | 100% | Investment holding<br>company            |
| Shandong Mobile     | PRC<br>August 7,<br>2000    |                           | RMB6,342         | 100% | Mobile<br>telecommunications<br>operator |
| Guangxi Mobile BVI  | BVI<br>September 1,<br>2000 | 10,000 shares<br>at HK\$1 | 1 share at HK\$1 | 100% | Investment holding<br>company            |
| Guangxi Mobile      | PRC<br>August 3,<br>2000    |                           | RMB2,341         | 100% | Mobile<br>telecommunications<br>operator |

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***36 Principal subsidiaries (continued)**

Details of the Company's principal subsidiaries are as follows (continued):

| <i>Name of company</i> | <i>Place and</i>                            | <i>Authorized, issued and</i> |                           | <i>Attributable equity interest %</i> | <i>Principal activity/ies</i>      |
|------------------------|---|-------------------------------|---------------------------|---------------------------------------|------------------------------------|
|                        | <i>date of incorporation/ establishment</i> | <i>paid up capital</i>        | <i>Issued and paid up</i> |                                       |                                    |
|                        |   | <i>Authorized</i>             |                           |                                       |                                    |
| Anhui Mobile BVI       | PRC<br>May 10, 2002                         | 10,000 shares<br>at HK\$1     | 1 share at HK\$1          | 100%                                  | Investment holding company         |
| Anhui Mobile           | PRC<br>January 29,<br>2002                  |                               | RMB4,099                  | 100%                                  | Mobile telecommunications operator |
| Jiangxi Mobile BVI     | BVI<br>May 10, 2002                         | 10,000 shares<br>at HK\$1     | 1 share at HK\$1          | 100%                                  | Investment holding company         |
| Jiangxi Mobile         | PRC<br>January 18,<br>2002                  |                               | RMB2,933                  | 100%                                  | Mobile telecommunications operator |
| Chongqing Mobile BVI   | BVI<br>May 10, 2002                         | 10,000 shares<br>at HK\$1     | 1 share at HK\$1          | 100%                                  | Investment holding company         |
| Chongqing Mobile       | PRC<br>January 28,<br>2002                  |                               | RMB3,030                  | 100%                                  | Mobile telecommunications operator |
| Sichuan Mobile BVI     | BVI<br>May 10, 2002                         | 10,000 shares<br>at HK\$1     | 1 share at HK\$1          | 100%                                  | Investment holding company         |
| Sichuan Mobile         | PRC<br>February 4,<br>2002                  |                               | RMB7,484                  | 100%                                  | Mobile telecommunications operator |
| Hubei Mobile BVI       | BVI<br>May 10, 2002                         | 10,000 shares<br>at HK\$1     | 1 share at HK\$1          | 100%                                  | Investment holding company         |
| Hubei Mobile           | PRC<br>February 1,<br>2002                  |                               | RMB3,961                  | 100%                                  | Mobile telecommunications operator |
| Hunan Mobile BVI       | BVI<br>May 10, 2002                         | 10,000 shares<br>at HK\$1     | 1 share at HK\$1          | 100%                                  | Investment holding company         |

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***36 Principal subsidiaries (continued)**

Details of the Company's principal subsidiaries are as follows (continued):

| <i>Name of company</i>  | <i>Place and date of incorporation/ establishment</i> | <i>Authorized, issued and paid up capital</i> |                           | <i>Attributable equity interest %</i> | <i>Principal activity/ies</i>      |
|-------------------------|---|---|---------------------------|---------------------------------------|------------------------------------|
|                         |   | <i>Authorized</i>                             | <i>Issued and paid up</i> |                                       |                                    |
| Hunan Mobile            | PRC<br>February 6, 2002                               |   | RMB4,016                  | 100%                                  | Mobile telecommunications operator |
| Shaanxi Mobile BVI      | BVI<br>May 10, 2002                                   | 10,000 shares at HK\$1                        | 1 share at HK\$1          | 100%                                  | Investment holding company         |
| Shaanxi Mobile          | PRC<br>February 3, 2002                               |   | RMB3,171                  | 100%                                  | Mobile telecommunications operator |
| Shanxi Mobile BVI       | BVI<br>May 10, 2002                                   | 10,000 shares at HK\$1                        | 1 share at HK\$1          | 100%                                  | Investment holding company         |
| Shanxi Mobile           | PRC<br>February 4, 2002                               |   | RMB2,773                  | 100%                                  | Mobile telecommunications operator |
| Neimenggu Mobile BVI    | BVI<br>March 4, 2004                                  | 10,000 shares at HK\$1                        | 1 share at HK\$1          | 100%                                  | Investment holding company         |
| Neimenggu Mobile        | PRC<br>January 16, 2004                               |   | RMB2,863                  | 100%                                  | Mobile telecommunications operator |
| Jilin Mobile BVI        | BVI<br>March 4, 2004                                  | 10,000 shares at HK\$1                        | 1 share at HK\$1          | 100%                                  | Investment holding company         |
| Jilin Mobile            | PRC<br>January 18, 2004                               |   | RMB3,278                  | 100%                                  | Mobile telecommunications operator |
| Heilongjiang Mobile BVI | BVI<br>March 4, 2004                                  | 10,000 shares at HK\$1                        | 1 share at HK\$1          | 100%                                  | Investment holding company         |
| Heilongjiang Mobile     | PRC<br>February 2, 2004                               |   | RMB4,501                  | 100%                                  | Mobile telecommunications operator |



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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***36 Principal subsidiaries (continued)**

Details of the Company's principal subsidiaries are as follows (continued):

| <i>Name of company</i> | <i>Place and date of incorporation/ establishment</i> | <i>Authorized, issued and paid up capital</i><br><i>Authorized</i> | <i>Issued and paid up</i> | <i>Attributable equity interest %</i> | <i>Principal activity/ies</i>      |
|------------------------|---|--|---------------------------|---------------------------------------|------------------------------------|
| Guizhou Mobile BVI     | BVI<br>March 4, 2004                                  | 10,000 shares at HK\$1   | 1 share at HK\$1          | 100%                                  | Investment holding company         |
| Guizhou Mobile         | PRC<br>January 19, 2004                               |  | RMB2,542                  | 100%                                  | Mobile telecommunications operator |
| Yunnan Mobile BVI      | BVI<br>March 4, 2004                                  | 10,000 shares at HK\$1   | 1 share at HK\$1          | 100%                                  | Investment holding company         |
| Yunnan Mobile          | PRC<br>January 19, 2004                               |  | RMB4,137                  | 100%                                  | Mobile telecommunications operator |
| Xizang Mobile BVI      | BVI<br>March 4, 2004                                  | 10,000 shares at HK\$1   | 1 share at HK\$1          | 100%                                  | Investment holding company         |
| Xizang Mobile          | PRC<br>February 9, 2004                               |  | RMB849                    | 100%                                  | Mobile telecommunications operator |
| Gansu Mobile BVI       | BVI<br>March 4, 2004                                  | 10,000 shares at HK\$1   | 1 share at HK\$1          | 100%                                  | Investment holding company         |
| Gansu Mobile           | PRC<br>January 29, 2004                               |  | RMB1,703                  | 100%                                  | Mobile telecommunications operator |
| Qinghai Mobile BVI     | BVI<br>March 4, 2004                                  | 10,000 shares at HK\$1   | 1 share at HK\$1          | 100%                                  | Investment holding company         |
| Qinghai Mobile         | PRC<br>February 2, 2004                               |  | RMB903                    | 100%                                  | Mobile telecommunications operator |
| Ningxia Mobile BVI     | BVI<br>March 4, 2004                                  | 10,000 shares at HK\$1   | 1 share at HK\$1          | 100%                                  | Investment holding company         |
| Ningxia Mobile         | PRC<br>January 30,                                    |  | RMB740                    | 100%                                  | Mobile telecommunications operator |

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|                     |                            |                           |                  |      |  |
|---------------------|----------------------------|---------------------------|------------------|------|--|
| Xinjiang Mobile BVI | BVI<br>March 4, 2004       | 10,000 shares<br>at HK\$1 | 1 share at HK\$1 | 100% | Investment holding<br>company            |
| Xinjiang Mobile     | PRC<br>February 3,<br>2004 |                           | RMB2,582         | 100% | Mobile<br>telecommunications<br>operator |

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***36 Principal subsidiaries (continued)**

Details of the Company's principal subsidiaries are as follows (continued):

| <i>Name of company</i>                 | <i>Place and date of incorporation/ establishment</i> | <i>Authorized, issued and paid up capital</i> |                           | <i>Attributable equity interest %</i> | <i>Principal activity/ies</i>   |
|--|---|---|---------------------------|---------------------------------------|---|
|  |   | <i>Authorized</i>                             | <i>Issued and paid up</i> |                                       |   |
| Zhongjing Design Institute BVI         | BVI<br>March 4, 2004                                  | 10,000 shares at HK\$1                        | 1 share at HK\$1          | 100%                                  | Investment holding company  |
| Jingyi Design Institute                | PRC<br>March 15, 2004                                 |   | RMB160                    | 100%                                  | Provision of telecommunications network planning design and consulting services |
| CMC BVI                                | BVI<br>March 4, 2004                                  | 10,000 shares at HK\$1                        | 1 share at HK\$1          | 100%                                  | Investment holding company  |
| CMC                                    | PRC<br>February 27, 2004                              |   | RMB1,642                  | 100%                                  | Network and business coordination center  |
| China Mobile Holding Company Limited   | PRC<br>June 9, 2000                                   |   | US\$ 30                   | 100%                                  | Investment holding company  |
| China Mobile (Shenzhen) Limited        | PRC<br>March 20, 2003                                 |   | US\$ 8                    | 100%                                  | Provision of roaming clearance services   |
| Aspire Holdings Limited                | Cayman Islands<br>June 5, 2000                        | 1,500,000,000 shares at HK\$0.1               | HK\$94                    | 66.41%                                | Investment holding company  |
| Aspire (BVI) Limited                   | BVI<br>June 7, 2000                                   | 50,000 shares at US\$1                        | US\$0.001                 | 66.41%                                | Investment holding company  |
| Aspire Technologies (Shenzhen) Limited | PRC<br>December 1,                                    |   | US\$ 10                   | 66.41%                                | Technology platform   |

| 2000  |                          |      |   |        | development and maintenance  |
|---|--------------------------|------|---|--------|--|
| Aspire Information Network (Shenzhen) Limited | PRC<br>August 1,<br>2001 | US\$ | 5 | 66.41% | Provision of mobile data solutions, system integration and development |

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***36 Principal subsidiaries (continued)**

Details of the Company's principal subsidiaries are as follows (continued):

| <i>Name of company</i>                            | <i>Place and<br/>date of<br/>incorporation/<br/>establishment</i> | <i>Authorized, issued and<br/>paid up capital</i>                                      |                           | <i>Attributable<br/>equity<br/>interest %</i> | <i>Principal<br/>activity/ies</i>  |
|---|---|--|---------------------------|---|--|
|   |   | <i>Authorized</i>  | <i>Issued and paid up</i> |   |  |
| Aspire Information Technologies (Beijing) Limited | PRC<br>October 9,<br>2004   |  | US\$5                     | 66.41%  | Technology platform development and maintenance  |
| Fujian FUNO                                       | PRC<br>April 8, 1998  |  | US\$4                     | 51%   | Network planning and optimizing construction-testing and supervising, technology support, development and training of Nokia GSM 900/1800 Mobile Communication System |
| Advanced Roaming & Clearing House Limited         | BVI<br>April 4,<br>2005   | 50,000 shares at US\$1   | 2 share at US\$1          | 100%  | Provision of roaming clearance service   |
| Fit Best Limited                                  | BVI<br>September 15,<br>2005                                      | 50,000 shares at US\$1   | 1 share at US\$1          | 100%  | Investment holding company   |
| Peoples Telephone                                 | Hong Kong<br>June 28,<br>1994                                     | 2,500,000,000 ordinary shares at HK\$0.48<br>154,125,000 preference shares at HK\$0.48 | HK\$357 ordinary shares   | 100%  | Provision of mobile telecommunications and related services  |

Dividends declared in respect of previous financial year, approved and paid by the Company's subsidiaries for the financial years ended December 31, 2004, 2005 and 2006 amounting to RMB25,978, RMB28,625, RMB28,680 respectively. All dividend income from these subsidiaries was entirely eliminated in preparing the consolidated financial statements.



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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **37 Non-adjusting post balance sheet events**

After the balance sheet date the directors proposed ordinary and special final dividends. Further details are disclosed in note 12(a).

Pursuant to the PRC enterprise income tax law passed by the Tenth National People's Congress on March 16, 2007, the new enterprise income tax rates for domestic and foreign enterprises are unified at 25% and will be effective from January 1, 2008. The impact of such change of enterprise income tax rate on the Group's consolidated financial statements will depend on detailed pronouncements that are subsequently issued. Since implementation measures for transitional policies on preferential tax rates granted according to current tax law and administrative regulations have not yet been announced, management cannot reasonably estimate the financial impact of the new tax law to the Group at this stage.

### **38 Accounting estimates and judgments**

#### ***Key sources of estimation uncertainty***

Notes 18, 19 and 35 contain information about the assumptions and their risk factors relating to goodwill impairment, impairment of other intangible assets with indefinite useful lives and financial instruments. Other key sources of estimation uncertainty are as follows:

#### ***Allowance for doubtful accounts***

Management assesses allowance for doubtful accounts based upon evaluation of the recoverability of the accounts receivable and other receivables at each balance sheet date. The estimates are based on the ageing of the accounts receivable and other receivables balances and the historical write-off experience, net of recoveries. If the financial condition of the customers were to deteriorate, additional allowance may be required.

#### ***Depreciation***

Depreciation is calculated to write off the cost of items of property, plant and equipment, less their estimated residual value, if any, using the straight-line method over their estimated useful lives. Management reviews the estimated useful lives and residual values of the assets annually in order to determine the amount of depreciation expense to be recorded during any reporting period. The useful lives and residual values are based on the Group's historical experience with similar assets and taking into account anticipated technological changes. The depreciation expense for future periods is adjusted if there are significant changes from previous estimates.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

**38 Accounting estimates and judgments (continued)**

***Amortization of other intangible assets***

Amortization of other intangible assets is calculated to write off the cost of items of other intangible assets using the straight-line method over their estimated useful lives unless such lives are indefinite. Management reviews the estimated useful lives of other intangible assets annually in order to determine the amount of amortization expense to be recorded during any reporting period. The useful lives are based on the estimate period over which future economic benefits will be received by the Group and taking into account any unexpected adverse changes in circumstances or events. The amortization expense for future periods is adjusted if there are significant changes from previous estimates.

***Impairment of property, plant and equipment***

The Group's property, plant and equipment comprise a significant portion of the Group's total assets. Changes in technology or industry conditions may cause the estimated period of use or the value of these assets to change. Long-lived assets including property, plant and equipment are reviewed for impairment at least annually or whenever events or changes in circumstances have indicated that their carrying amounts may not be recoverable. If any such indication exists, the asset's recoverable amount is estimated.

The recoverable amount of an asset is the greater of its net selling price and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset, which requires significant judgment relating to level of revenue and amount of operating costs. Management uses all readily available information in determining an amount that is a reasonable approximation of the recoverable amount, including estimates based on reasonable and supportable assumptions and projections of revenue and operating costs. Changes in these estimates could have a significant impact on the carrying value of the assets and could result in additional impairment charge or reversal of impairment in future periods.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

**39 Possible impact of amendments, new standards and interpretations issued but not yet effective for the annual accounting year ended December 31, 2006**

Up to the date of issue of these consolidated financial statements, the HKICPA has issued a number of amendments, new standards and interpretations which are not yet effective for the year ended December 31, 2006 and which have not been adopted in these consolidated financial statements.

Management is in the process of making an assessment of what the impact of these amendments, new standards and new interpretations is expected to be in the period of initial application. So far it has concluded that the adoption is unlikely to have a significant impact on the Group's results of operations and financial position.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **40 Significant differences between HK GAAP and US GAAP**

The Group's accounting policies conform with generally accepted accounting principles in Hong Kong ( HK GAAP ) which differ in certain material respects from those applicable generally accepted accounting principles in the United States of America ( US GAAP ).

The significant differences relate principally to the following items and the adjustments considered necessary to present the net income and shareholders' equity in accordance with US GAAP are shown in the tables set out below:

#### ***(a) Effect of combination of entities under common control***

Under HK GAAP, the Group adopted the purchase accounting method to account for the purchase of subsidiaries from the holding company. Under the purchase accounting method, the acquired results are included in the results of operations from the date of their acquisition. For acquisitions before January 1, 2001, goodwill arising on the acquisition, being the excess of the cost over the fair value of the Group's share of the separable net assets acquired, is eliminated against reserves immediately on acquisition. For acquisitions on or after January 1, 2001, goodwill arising on the acquisition is amortized to the consolidated statements of income on a straight-line basis over 20 years. With effect from January 1, 2005, in order to comply with HKFRS 3 and HKAS 36, the Group adopted a new accounting policy for goodwill. The Group no longer amortizes positive goodwill. Such goodwill is tested annually for impairment, including in the year of its initial recognition, as well as when there are indications of impairment.

As a result of the Group and the acquired subsidiaries, being under common control prior to the acquisition, such acquisitions under US GAAP are considered combinations of entities under common control. Under US GAAP, combinations of entities under common control are accounted for under the as if pooling-of-interests method, whereby assets and liabilities are accounted for at historical cost and the financial statements of previously separate companies for periods prior to the combination are restated on a combined basis. The consideration paid and payable by the Group has been treated as distribution to owner in the year of acquisition. Goodwill arising on consolidation and the amortization of goodwill which are recognized under HK GAAP have been reversed for US GAAP purposes.

#### ***(b) Capitalization of interest***

Under HK GAAP, interest costs are only capitalized to the extent that funds are borrowed and used for the purpose of obtaining qualifying asset which necessarily takes a substantial period of time to get ready for its intended use.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

**40 Significant differences between HK GAAP and US GAAP (continued)**

***(b) Capitalization of interest (continued)***

Under US GAAP, interest costs capitalized are determined based on specific borrowings related to the acquisition or construction of an asset, if an entity's financing plans associate a specific new borrowing with a qualifying asset. If average accumulated expenditures for the asset exceed the amounts of specific new borrowings associated with an asset, additional interest costs capitalized are based on the weighted average interest rate applicable to other borrowings of the entity.

***(c) Revaluation and impairment of property, plant and equipment and land lease prepayments***

For certain periods prior to May 31, 1997, the property, plant and equipment and land lease prepayments of the subsidiaries were revalued in compliance with PRC rules and regulations, resulting in an increase in shareholders' equity.

Additionally, the property, plant and equipment and land lease prepayments of the subsidiaries were revalued as a result of the restructuring that occurred in 1997 and the subsequent acquisitions. These property, plant and equipment and land lease prepayments revaluations result in an increase in shareholders' equity with respect to the increase in carrying amount of certain property, plant and equipment and land lease prepayments above their historical cost bases, except the Fourth Acquisition and Fifth Acquisition.

In connection with the Fourth Acquisition and the Fifth Acquisition, the property, plant and equipment and land lease prepayments of the subsidiaries acquired were revalued at December 31, 2001 and December 31, 2003 respectively. Such revaluations resulted in an increase directly to those shareholders' equity with respect to the increase in carrying amount of certain property, plant and equipment and land lease prepayments above their historical cost bases, and a charge to the consolidated statements of income with respect to the decrease in carrying amount of certain property, plant and equipment and land lease prepayments below their historical cost bases.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **40 Significant differences between HK GAAP and US GAAP (continued)**

#### ***(c) Revaluation and impairment of property, plant and equipment and land lease prepayments (continued)***

The carrying amount of property, plant and equipment and land lease prepayments under HK GAAP is reviewed periodically in order to assess whether the recoverable amount has declined below the carrying amount. When such a decline occurs, the carrying amount is reduced to the recoverable amount based on the expected future cash flows generated by the property, plant and equipment and land lease prepayments, discounted to their present values using a pre-tax discount rate that reflects current market assessments of time value of money and the risks specific to the asset. A subsequent increase in the recoverable amount is written back to results of operations when circumstances and events that led to the write-down or write-off cease to exist.

Under US GAAP, property, plant and equipment are stated at their historical cost, less accumulated depreciation and land lease prepayments are stated at their historical cost, charged to income statement on a straight line basis over the period of the lease term. Accordingly, the revaluation reserve recorded directly to shareholders' equity and the charge to statements of income under HK GAAP as a result of the revaluation of property, plant and equipment and land lease prepayments are reversed for US GAAP purposes. Additionally, as a result of the tax deductibility of the revaluation reserve, a deferred tax asset related to the reversal of the net revaluation reserve is created under US GAAP with a corresponding increase in shareholders' equity.

Under US GAAP, property, plant and equipment and land lease prepayments are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future undiscounted net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amounts of the assets exceed the fair value of the assets. Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to sell. Any subsequent increase in the recoverable amount written back to results of operations when circumstances and events that led to the write-down or write-off cease to exist under HK GAAP is reversed for US GAAP purposes.

For the years presented, there were no differences related to impairment charges under HK GAAP and US GAAP. The US GAAP difference as shown in the reconciliation represents the reversal of revaluation reserves and the related depreciation and charges which are recognized under HK GAAP.



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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **40 Significant differences between HK GAAP and US GAAP (continued)**

#### ***(d) Employee housing scheme***

The Group provides staff quarters under its employee housing schemes at below market prices. Under HK GAAP, employee housing scheme costs borne by the corresponding PTAs and not charged to the subsidiaries are not recognized by the subsidiaries.

Under US GAAP, employee housing scheme costs borne by the corresponding PTAs and not charged to the subsidiaries are reflected as an expense in the statements of income and a corresponding capital contribution. Additionally, under US GAAP, the costs to be borne by the subsidiaries are accrued over the term of the program.

#### ***(e) Deferred taxation***

Under HK GAAP, deferred tax assets and liabilities arise from deductible and taxable temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the tax bases respectively. The carrying amount of a deferred tax asset is reviewed at each balance sheet date and is reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow the related tax benefit to be utilized. Any such reduction is reversed to the extent that it becomes probable that sufficient taxable profit will be available.

Under US GAAP, provisions are made for all deferred taxes as they arise, except a valuation allowance is provided against deferred tax assets when realization of such amounts does not meet the criteria of more likely than not. For the years presented, there were no differences related to the recognition of deferred tax under HK GAAP and US GAAP. The US GAAP difference as shown in the reconciliation represents the deferred tax effects of US GAAP adjustments.

#### ***(f) Share option scheme***

The Group grants share options to directors and employees. Under HK GAAP and prior to January 1, 2005, the proceeds received are recognized as an increase to capital upon the exercise of the share options. The Group does not account for the issuance of stock options until they are exercised. With effect from January 1, 2005, in order to comply with HKFRS 2 Share-based payment, the Group recognizes the fair value of such share options as an expense in the consolidated statements of income, or as an asset, if the cost qualifies for recognition as an asset under the Group's accounting policies. A corresponding increase is recognized in a capital reserve within equity.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **40 Significant differences between HK GAAP and US GAAP (continued)**

#### ***(f) Share option scheme (continued)***

Under US GAAP, and prior to January 1, 2006, the Group follows Accounting Principles Board Opinion 25 ( APB 25 ), Accounting for Stock Issued to Employees , and determines compensation expenses based on the excess, if any, of the quoted market price of the shares on the date of grant over the exercise price of the stock options. Such amount is charged to the consolidated statements of income over the vesting period of the options. As a result, any expenses recognized based on the fair value of share options under HK GAAP is reversed under US GAAP. With effect from January 1, 2006, in order to comply with Statement of Financial Accounting Standards No. 123 (revised 2004), Share-Based Payment , the Group recognizes compensation expense for all previously unvested share-based payment at fair value. The Group adopts the modified-prospective transition method in which effective from January 1, 2006, the compensation expense is recognized at fair value for (i) share options granted after January 1, 2006; and (ii) all share options granted prior to January 1, 2006 that remain unvested at that date. No restatement for prior periods is required. As a result, the US GAAP difference as shown in the net income reconciliation for the year ended December 31, 2006 represented additional compensation expense recognized under US GAAP using fair value approach for unvested share options granted to employees and directors before November 7, 2002 of which no measurement was made to such share options under HK GAAP as the Group has adopted the transitional provisions set out in paragraph 53 of HKFRS 2.

For the years ended December 31, 2004 and 2005, the US GAAP difference as shown in the net income reconciliation represented the amortization of compensation expenses in relation to share option scheme amounting to RMB86 and RMB68 under APB 25, respectively and the reversal of expenses recognized based on the fair value of share options under HK GAAP amounting to RMB255 and RMB1,553, respectively.

#### ***(g) Revenue recognition***

Until June 30, 1999, under both HK GAAP and US GAAP, connection fees revenue and telephone number selection fees were recognized as received. Under US GAAP, effective July 1, 1999, net connection fees and telephone number selection fees received in excess of direct costs were deferred and recognized over the estimated customer usage period of approximately 48 months.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

**40 Significant differences between HK GAAP and US GAAP (continued)**

***(g) Revenue recognition (continued)***

Under US GAAP, effective January 1, 2000, the Group adopted provisions of Staff Accounting Bulletin No. 101, Revenue Recognition in Financial Statements ( SAB 101 ). In December 2003, Staff Accounting Bulletin No.104, Revenue Recognition ( SAB 104 ) updates the guidance in SAB 101 and Emerging Issues Task Force Issue 00-21 Revenue Arrangements with Multiple Deliverables ( EITF 00-21 ). EITF 00-21 addresses certain aspects of the accounting by a vendor for arrangements under which the vendor will perform multiple revenue generating activities. Under SAB 104, connection fees and telephone number selection fees received and incremental direct costs up to, but not exceeding such fees, were deferred and amortized over the estimated customer usage period for the related service. The cumulative effect from the adoption of SAB 104 was not material.

***(h) Interconnection, roaming and leased line agreements***

In May 2000, the Group entered into new agreements with CMCC for inter-provincial interconnection and domestic and international roaming services, and inter-provincial long distance transmission leased line arrangement with retrospective effect from October 1, 1999 for Guangdong Mobile, Zhejiang Mobile and Jiangsu Mobile and from April 1, 1999 for Fujian Mobile, Henan Mobile and Hainan Mobile. Under HK GAAP, the net savings refunded to the Group as a result of the two agreements taking retrospective effect were recorded in operations for the year ended December 31, 2000. Under US GAAP, such net savings are deferred and amortized on a straight-line basis over 7 years.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

**40 Significant differences between HK GAAP and US GAAP (continued)**

***(i) Recently Issued Accounting Standards  
SFAS No. 157***

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements . This Statement defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. This Statement applies under other accounting pronouncements that require or permit fair value measurements, the FASB having previously concluded in those accounting pronouncements that fair value is the relevant measurement attribute. Accordingly, this Statement does not require any new fair value measurements. However, for some entities, the application of this Statement will change current practice. This Statement is effective for financial statements issued for fiscal years beginning after November 15, 2007. Management is in the process of evaluating the potential impact of this standard.

***SFAS No. 159***

In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities , which permits entities to choose to measure many financial instruments and certain other items at fair value. SFAS No. 159 will be effective as of the beginning of an entity's first fiscal year that begins after November 15, 2007. Management is in the process of determining whether it will elect the fair value option allowed by the Standard.

***FASB Interpretation No. 48 ( FIN 48 )***

In June 2006, the FASB issued FIN 48, Accounting for Uncertainty in Income Taxes an Interpretation of FASB Statement No. 109 , which clarifies the accounting for uncertainty in tax positions. This interpretation requires that the entities recognize in the financial statements the impact of a tax position, if that position is more likely than not of being sustained upon examination, based on the technical merits of the position. FIN 48 will be effective for the fiscal years beginning after December 15, 2006. Management is in the process of evaluating the potential impact of this interpretation.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

**40 Significant differences between HK GAAP and US GAAP (continued)**

**(i) Recently Issued Accounting Standards (continued)**

***Staff Accounting Bulletin No. 108 ( SAB 108 )***

In September 2006, the SEC issued SAB 108, *Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements ( SAB 108 )*. SAB 108 provides guidance on the consideration of the effects of prior year misstatements in quantifying current year misstatements for the purpose of a materiality assessment. SAB 108 establishes an approach that requires quantification of financial statement errors based on the effects of each on a company's balance sheet and statement of operations and the related financial statement disclosures. The Company adopted SAB 108 and the adoption of SAB 108 did not have a material impact on the Company's consolidated financial position, results of operations or cash flows.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***40 Significant differences between HK GAAP and US GAAP (continued)**

The effect on net income of significant differences between HK GAAP and US GAAP is as follows:

|  | Note | Year ended December 31, |             |             |
|--|------|-------------------------|-------------|-------------|
|  |      | 2004<br>RMB             | 2005<br>RMB | 2006<br>RMB |
| Profit attributable to equity shareholders under HK GAAP                             |      | 41,749                  | 53,549      | 66,026      |
| <i>Adjustments:</i>  |      |                         |             |             |
| Effect of combination of entities under common control, net of tax                   | (a)  | 1,587                   |             |             |
| Capitalized interest   | (b)  | (116)                   | (106)       | (83)        |
| Revaluation of property, plant and equipment   | (c)  | (448)                   | (818)       | (1,145)     |
| Revaluation of land lease prepayments  | (c)  | 68                      | 98          | 55          |
| Share option scheme  | (f)  | 169                     | 1,485       | (212)       |
| Amortization of net connection fees and telephone number selection fees              | (g)  | 109                     | 6           |             |
| Amortization of net savings from interconnection, roaming and leased line agreements | (h)  | 86                      | 86          | 86          |
| Reversal of goodwill amortization  | (a)  | 1,930                   |             |             |
| Deferred tax effects of US GAAP adjustments  | (e)  | (73)                    | 204         | 347         |
| Net income under US GAAP   |      | 45,061                  | 54,504      | 65,074      |
| Basic net income per share in accordance with US GAAP                                |      | 2.29                    | 2.76        | 3.27        |
| Diluted net income per share in accordance with US GAAP                              |      | 2.29                    | 2.75        | 3.24        |
| Basic net income per ADS* in accordance with US GAAP                                 |      | 11.45                   | 13.81       | 16.36       |
| Diluted net income per ADS* in accordance with US GAAP                               |      | 11.43                   | 13.73       | 16.20       |

\* Based on a ratio of 5 ordinary shares to one ADS

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***40 Significant differences between HK GAAP and US GAAP (continued)**

The effect on shareholders' equity of significant differences between HK GAAP and US GAAP is as follows:

|  | <b>Note</b> | <b>As of December 31,<br/>2005<br/>RMB</b> | <b>2006<br/>RMB</b> |
|--|-------------|--|---------------------|
| Shareholders' equity under HK GAAP   |             | 272,824                                    | 319,002             |
| <i>Adjustments:</i>  |             |  |                     |
| Capitalized interest   | (b)         | 158  | 75                  |
| Revaluation of property, plant and equipment                                     |             |  |                     |
| - cost   | (c)         | (5,370)                                    | (5,370)             |
| - accumulated depreciation and others  | (c)         | 7,069                                      | 5,924               |
| Revaluation of land lease prepayments  | (c)         | (2,144)                                    | (2,089)             |
| Deferred tax adjustments on revaluations   | (e)         | 142  | 490                 |
| Employee housing scheme  | (d)         | (1,674)                                    | (1,674)             |
| Deemed capital contribution for employee housing scheme                          | (d)         | 1,674                                      | 1,674               |
| Deferral of net savings from interconnection, roaming and leased line agreements | (h)         | (114)                                      | (28)                |
| Reversal of goodwill   | (a)         | (35,300)                                   | (35,300)            |
| Deferred tax effects of US GAAP adjustments                                      | (e)         | (13)                                       | (14)                |
| Shareholders' equity under US GAAP   |             | 237,252                                    | 282,690             |

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***40 Significant differences between HK GAAP and US GAAP (continued)**

The following are condensed consolidated balance sheets of the Group as of December 31, 2005 and 2006, and the related condensed consolidated statements of income, total shareholders' equity and comprehensive income and cash flows for each of the years in the three-year period ended December 31, 2006, restated to reflect the impact of the differences between HK GAAP and US GAAP. Certain comparative figures have been reclassified to conform to current year's presentation.

**Condensed consolidated statements of income**

|  | <i>Year ended December 31,</i> |                 |                 |
|--|--------------------------------|-----------------|-----------------|
|  | <b>2004</b>                    | <b>2005</b>     | <b>2006</b>     |
|  | <b>RMB</b>                     | <b>RMB</b>      | <b>RMB</b>      |
| <b>Operating revenue</b>   |                                |                 |                 |
| Usage fees   | 136,876                        | 156,710         | 189,710         |
| Monthly fees   | 26,458                         | 25,055          | 21,629          |
| Value-added services fees  | 31,651                         | 50,187          | 69,309          |
| Connection fees  | 252                            | 7               |                 |
| Other operating revenue  | 15,400                         | 17,617          | 22,988          |
| <b>Total operating revenue</b>   | <b>210,637</b>                 | <b>249,576</b>  | <b>303,636</b>  |
| <b>Operating expenses</b>  |                                |                 |                 |
| Cost of services and sales (excluding depreciation of RMB47,050, RMB55,422 and RMB62,779 included below) | 24,387                         | 28,555          | 32,131          |
| Depreciation   | 47,050                         | 55,422          | 62,779          |
| Selling, general and administration  | 74,596                         | 87,878          | 115,228         |
| <b>Total operating expenses</b>  | <b>146,033</b>                 | <b>171,855</b>  | <b>210,138</b>  |
| <b>Profit from operations</b>  | <b>64,604</b>                  | <b>77,721</b>   | <b>93,498</b>   |
| <b>Non-operating net income</b>  | <b>949</b>                     | <b>499</b>      | <b>285</b>      |
| <b>Interest income</b>   | <b>1,032</b>                   | <b>1,615</b>    | <b>2,604</b>    |
| <b>Interest expense</b>  | <b>(1,738)</b>                 | <b>(1,346)</b>  | <b>(1,510)</b>  |
| <b>Profit before tax</b>   | <b>64,847</b>                  | <b>78,489</b>   | <b>94,877</b>   |
| <b>Income tax</b>  | <b>(19,764)</b>                | <b>(23,945)</b> | <b>(29,715)</b> |
| <b>Profit after tax</b>  | <b>45,083</b>                  | <b>54,544</b>   | <b>65,162</b>   |
| <b>Minority interests</b>  | <b>(22)</b>                    | <b>(40)</b>     | <b>(88)</b>     |
| <b>Net income</b>  | <b>45,061</b>                  | <b>54,504</b>   | <b>65,074</b>   |





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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***40 Significant differences between HK GAAP and US GAAP (continued)***Condensed consolidated statements of income (continued)*

|                                     | <i>Year ended December 31,</i> |             |             |
|-------------------------------------|--------------------------------|-------------|-------------|
|                                     | <i>2004</i>                    | <i>2005</i> | <i>2006</i> |
|                                     | <b>RMB</b>                     | <b>RMB</b>  | <b>RMB</b>  |
| <b>Basic net income per share</b>   | RMB2.29                        | RMB2.76     | RMB3.27     |
| <b>Basic net income per ADS*</b>    | RMB 11.45                      | RMB13.81    | RMB16.36    |
| <b>Diluted net income per share</b> | RMB 2.29                       | RMB2.75     | RMB3.24     |
| <b>Diluted net income per ADS*</b>  | RMB 11.43                      | RMB13.73    | RMB16.20    |

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\* Based on a ratio of 5 ordinary shares to one ADS

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***40 Significant differences between HK GAAP and US GAAP (continued)****Condensed consolidated balance sheets**

|  | <i>December 31,</i> |                |
|--|---------------------|----------------|
|  | <i>2005</i>         | <i>2006</i>    |
|  | <b>RMB</b>          | <b>RMB</b>     |
| <b>Assets</b>                            |                     |                |
| Current assets                           |                     |                |
| Cash and cash equivalents                | 64,461              | 71,167         |
| Deposits with banks                      | 41,925              | 82,294         |
| Accounts receivable                      | 6,446               | 6,747          |
| Other receivables                        | 1,888               | 2,454          |
| Tax recoverable                          | 165                 | 468            |
| Deferred income taxes                    | 2,660               | 4,352          |
| Inventories                              | 2,365               | 3,007          |
| Prepayments and other current assets     | 3,583               | 4,613          |
| Amount due from ultimate holding company | 63                  | 305            |
| Amounts due from related parties         | 180                 | 452            |
| <b>Total current assets</b>              | <b>123,736</b>      | <b>175,859</b> |
| Property, plant and equipment            | 218,362             | 218,903        |
| Construction in progress                 | 34,201              | 52,436         |
| Land lease prepayments                   | 5,099               | 5,586          |
| Goodwill                                 |                     | 1,594          |
| Other intangible assets                  |                     | 700            |
| Other financial assets                   | 77                  | 77             |
| Interest in associates                   |                     |                |
| Deferred income taxes                    | 4,143               | 3,260          |
| <b>Total assets</b>                      | <b>385,618</b>      | <b>458,415</b> |

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***40 Significant differences between HK GAAP and US GAAP (continued)****Condensed consolidated balance sheets (continued)**

|  | <i>December 31,</i> |                |
|--|---------------------|----------------|
|  | <i>2005</i>         | <i>2006</i>    |
|  | <b>RMB</b>          | <b>RMB</b>     |
| <b>Liabilities, minority interests and shareholders equity</b>       |                     |                |
| Current liabilities  |                     |                |
| Accounts payable   | 39,908              | 55,626         |
| Bills payable  | 1,359               | 2,212          |
| Interest-bearing borrowings  |                     | 2,996          |
| Current instalments of obligation under capital lease                | 68                  | 68             |
| Current taxation   | 9,249               | 9,823          |
| Amounts due to related parties                                       | 2,172               | 1,846          |
| Accrued expenses and other payables                                  | 39,858              | 45,898         |
| Amount due to immediate holding company                              | 96                  | 186            |
| Amount due to ultimate holding company                               | 269                 | 129            |
| Deferred revenue   | 16,975              | 21,851         |
| Total current liabilities  | 109,954             | 140,635        |
| Interest-bearing borrowings  | 12,912              | 9,941          |
| Deferred revenue, excluding current portion                          | 1,438               | 930            |
| Deferred income taxes  | 146                 | 215            |
| Amount due to immediate holding company                              | 23,633              | 23,633         |
| <b>Total liabilities</b>   | <b>148,083</b>      | <b>175,354</b> |
| Minority interests   | 283                 | 371            |
| <b>Shareholders equity</b>   | <b>237,252</b>      | <b>282,690</b> |
| <b>Total liabilities, minority interests and shareholders equity</b> | <b>385,618</b>      | <b>458,415</b> |

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***40 Significant differences between HK GAAP and US GAAP (continued)***Condensed consolidated statements of shareholders' equity and comprehensive income for the following years:*

|   | Shareholders<br>equity<br>RMB | Total<br>comprehensive<br>income<br>RMB |
|---|-------------------------------|---|
| Shareholders' equity at January 1, 2004         | 190,828                       |   |
| Net income for the year ended December 31, 2004 | 45,061                        | 45,061                                  |
| Issue of ordinary shares                        | 703                           |   |
| Deemed capital distribution                     | (30,210)                      |   |
| Distribution to owner                           | (8,349)                       |   |
| Stock-based compensation                        | 86                            |   |
| Total comprehensive income                      |                               | 45,061                                  |
| Shareholders' equity at December 31, 2004       | 198,119                       |   |
| Net income for the year ended December 31, 2005 | 54,504                        | 54,504                                  |
| Issue of ordinary shares                        | 3,422                         |   |
| Distribution to owner                           | (18,894)                      |   |
| Stock-based compensation                        | 68                            |   |
| Others  | 33                            |   |
| Total comprehensive income                      |                               | 54,504                                  |
| Shareholders' equity at December 31, 2005       | 237,252                       |   |
| Net income for the year ended December 31, 2006 | 65,074                        | 65,074                                  |
| Issue of ordinary shares                        | 4,093                         |   |
| Distribution to owner                           | (26,162)                      |   |
| Stock-based compensation                        | 2,476                         |   |
| Foreign currency translation                    | (43)                          | (43)                                    |
| Total comprehensive income                      |                               | 65,031                                  |
| Shareholders' equity at December 31, 2006       | 282,690                       |   |

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***40 Significant differences between HK GAAP and US GAAP (continued)*****Condensed consolidated statements of cash flows***

The Group applies HKAS 7 Cash Flow Statements. Its objectives and principles are similar to those set out in SFAS No. 95, Statement of Cash Flows (SFAS 95). The principal differences between the standards relate to classification. Under HKAS 7, the Group presents its cash flows for (a) operating activities; (b) investing activities; and (c) financing activities. Dividend received and interest received under investing activities and interest paid under financing activities shown under HKAS 7 would be included as operating activities under SFAS 95, with the exception of distributions, which under SFAS 95 would be classified as financing activities. Summarized cash flow data by operating, investing and financing activities in accordance with SFAS 95 are as follows:

|  | <i>Year ended December 31,</i> |             |             |
|--|--------------------------------|-------------|-------------|
|  | <i>2004</i>                    | <i>2005</i> | <i>2006</i> |
|  | <b>RMB</b>                     | <b>RMB</b>  | <b>RMB</b>  |
| Net cash inflow/(outflow) from                 |                                |             |             |
| Operating activities                           | 111,112                        | 131,593     | 150,401     |
| Investing activities                           | (65,619)                       | (88,635)    | (121,310)   |
| Financing activities                           | (40,644)                       | (23,538)    | (22,173)    |
| Increase in cash and cash equivalents          | 4,849                          | 19,420      | 6,918       |
| Cash and cash equivalents at beginning of year | 40,300                         | 45,149      | 64,461      |
| Effect of changes in foreign exchange rate     |                                | (108)       | (212)       |
| Cash and cash equivalents at end of year       | 45,149                         | 64,461      | 71,167      |
| Interest paid (net of amounts capitalized)     | 2,040                          | 1,635       | 1,414       |
| Income taxes paid                              | 18,244                         | 24,585      | 30,993      |

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***40 Significant differences between HK GAAP and US GAAP (continued)*****Significant non-cash transactions***

The Group incurred payables of RMB36,851 and RMB2,143 to equipment suppliers and banks respectively for additions of construction in progress during the year ended December 31, 2006.

The Group incurred payables of RMB28,176 and RMB1,332 to equipment suppliers and banks respectively for additions of construction in progress during the year ended December 31, 2005.

The Group incurred payables of RMB23,980 and RMB1,675 to equipment suppliers and banks respectively for additions of construction in progress during the year ended December 31, 2004.

**41 Additional information required by US GAAP**

The following additional financial statement disclosures are required under US GAAP and are presented on a US GAAP basis.

***Income tax***

The provision for Hong Kong profits tax for 2006 is calculated at 17.5% of the estimated assessable profits for the year. For the years ended December 31, 2004 and 2005, no provision has been made for Hong Kong profits tax as there were no estimated Hong Kong assessable profits during the year.

The provision for the PRC enterprise income tax is based on a statutory income tax rate of 33% of the assessable profit of the Group as determined in accordance with the relevant income tax rules and regulations of the PRC during the year, except for certain subsidiaries of the Company and certain operations of the subsidiaries located within special economic zones in the PRC, which enjoy a preferential rate of 30% or 15% respectively.

The components of income before income taxes are as follows:

|                     | <i>Year ended December 31,</i> |             |             |
|---------------------|--------------------------------|-------------|-------------|
|                     | <i>2004</i>                    | <i>2005</i> | <i>2006</i> |
|                     | <b>RMB</b>                     | <b>RMB</b>  | <b>RMB</b>  |
| Hong Kong operation | (1)                            | (1)         | 206         |
| PRC operation       | 64,848                         | 78,490      | 94,671      |
|                     | 64,847                         | 78,489      | 94,877      |

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***41 Additional information required by US GAAP (continued)****Income tax (continued)**

The components of income tax expense are as follows:

|                 | <i>Year ended December 31,</i> |             |             |
|-----------------|--------------------------------|-------------|-------------|
|                 | <i>2004</i>                    | <i>2005</i> | <i>2006</i> |
|                 | <b>RMB</b>                     | <b>RMB</b>  | <b>RMB</b>  |
| <b>Current</b>  |                                |             |             |
| Hong Kong       |                                |             | 12          |
| Mainland China  | 19,788                         | 26,714      | 30,520      |
|                 | 19,788                         | 26,714      | 30,532      |
| <b>Deferred</b> |                                |             |             |
| Hong Kong       |                                |             | 35          |
| Mainland China  | (24)                           | (2,769)     | (852)       |
|                 | (24)                           | (2,769)     | (817)       |
|                 | 19,764                         | 23,945      | 29,715      |

The provision for income tax differs from the amount computed by applying the PRC statutory income tax rate of 33% to profit before tax and minority interests for the following reasons:

|  | <i>Year ended December 31,</i> |             |             |
|--|--------------------------------|-------------|-------------|
|  | <i>2004</i>                    | <i>2005</i> | <i>2006</i> |
|  | <b>RMB</b>                     | <b>RMB</b>  | <b>RMB</b>  |
| Expected PRC taxation at statutory tax rates   | 21,400                         | 25,901      | 31,309      |
| Non-taxable items  |                                |             |             |
| - Connection fee   | (27)                           | (1)         |             |
| - Interest income  | (26)                           | (24)        | (34)        |
| Amortization of deferred tax credit  | (125)                          | (526)       | (732)       |
| Non-deductible expenses on PRC operations  | 415                            | 395         | 1,368       |
| Non-deductible expenses on Hong Kong operations  | 217                            | 175         | 236         |
| Rate differential on PRC operations  | (1,902)                        | (1,758)     | (1,949)     |
| Rate differential on Hong Kong operations  | 166                            | 119         | 175         |
| Reversal of deferred taxation due to change of income tax rate on certain PRC operating subsidiaries | 169                            | 4           | (69)        |
| Over-provision for PRC operations in prior years   | (357)                          | (247)       | (550)       |
| Under-provision for Hong Kong operations in prior year   |                                |             | 9           |
| Others   | (166)                          | (93)        | (48)        |



|            |        |        |        |
|------------|--------|--------|--------|
| Income tax | 19,764 | 23,945 | 29,715 |
|------------|--------|--------|--------|

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***41 Additional information required by US GAAP (continued)*****Income tax (continued)***

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management considers the scheduled reversal of deferred tax liabilities and projected future taxable income in making this assessment. Based upon the level of historical taxable income and projections for future taxable income over the periods in which the deferred tax assets are deductible, management believes it is more likely than not that the Group will realize the benefits of these deductible differences. The amount of the deferred tax asset considered realizable, however, could be reduced in the near term if estimates of future taxable income during the carryforward period are reduced.

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities are presented below.

|  | <i>December 31,</i> |             |
|--|---------------------|-------------|
|  | <i>2005</i>         | <i>2006</i> |
|  | <b>RMB</b>          | <b>RMB</b>  |
| Deferred tax assets:                                     |                     |             |
| Inventories  | 9                   | 8           |
| Accounts receivable                                      | 971                 | 1,170       |
| Property, plant and equipment and land lease prepayments | 4,107               | 3,260       |
| Accrued expenses and other payable                       | 1,680               | 3,165       |
| Deferred revenue   | 36                  | 9           |
| Gross deferred tax assets                                | 6,803               | 7,612       |
| Deferred tax liabilities:                                |                     |             |
| Property, plant and equipment and land lease prepayments | (146)               | (215)       |
| Net deferred tax assets                                  | 6,657               | 7,397       |
| Less: Current portion of net deferred tax assets         | (2,660)             | (4,352)     |
|  | 3,997               | 3,045       |

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***41 Additional information required by US GAAP (continued)*****Accounts receivable***

|                                       | <i>December 31,</i> |             |
|---------------------------------------|---------------------|-------------|
|                                       | <i>2005</i>         | <i>2006</i> |
|                                       | <b>RMB</b>          | <b>RMB</b>  |
| Accounts receivable                   | 9,911               | 10,677      |
| Less: Allowance for doubtful accounts | (3,465)             | (3,930)     |
|                                       | 6,446               | 6,747       |

Allowance for doubtful accounts is analyzed as follows:

|   | <b>RMB</b> |
|---|------------|
| At January 1, 2004                      | 5,169      |
| Provision for the year                  | 2,569      |
| Written-off                             | (4,085)    |
| At December 31, 2004                    | 3,653      |
| Provision for the year                  | 2,987      |
| Written-off                             | (3,175)    |
| At December 31, 2005                    | 3,465      |
| Acquired on acquisition of a subsidiary | 26         |
| Provision for the year                  | 3,851      |
| Written-off                             | (3,412)    |
| At December 31, 2006                    | 3,930      |

***Other receivables***

|                                       | <i>December 31,</i> |             |
|---------------------------------------|---------------------|-------------|
|                                       | <i>2005</i>         | <i>2006</i> |
|                                       | <b>RMB</b>          | <b>RMB</b>  |
| Other receivables                     | 1,998               | 2,564       |
| Less: Allowance for doubtful accounts | (110)               | (110)       |
|                                       | 1,888               | 2,454       |

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***41 Additional information required by US GAAP (continued)*****Other receivables (continued)***

Allowance for doubtful accounts is analyzed as follows:

|                           | <b>RMB</b> |
|---------------------------|------------|
| At January 1, 2004        | 115        |
| Provision for the year    | 46         |
| Written-off               | (22)       |
| At December 31, 2004      | 139        |
| Written-back for the year | (19)       |
| Written-off               | (10)       |
| At December 31, 2005      | 110        |
| Provision for the year    | 1          |
| Written-off               | (1)        |
| At December 31, 2006      | 110        |

***Property, plant and equipment***

|  | <b>December 31,</b> |             |
|--|---------------------|-------------|
|  | <b>2005</b>         | <b>2006</b> |
|  | <b>RMB</b>          | <b>RMB</b>  |
| Buildings  | 37,827              | 43,146      |
| Telecommunications transceivers, switching centers, transmission and other network equipment | 369,554             | 366,427     |
| Office equipment, furniture and fixtures and others  | 16,732              | 15,965      |
|  | 424,113             | 425,538     |
| Less: Accumulated depreciation   | (205,751)           | (206,635)   |
|  | 218,362             | 218,903     |

During the year, management reviewed the estimated useful lives of all the property, plant and equipment and changed the estimated useful lives of certain network equipment from 7 years to 5 years.

The change in accounting estimate is accounted for prospectively from January 1, 2006. The depreciation expenses increased and net income decreased approximately RMB11,773 and RMB8,296 for year ended December 31, 2006 and for the asset's revised remaining useful lives, respectively.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***41 Additional information required by US GAAP (continued)*****Goodwill***

|  | <i>December 31,</i> |             |
|--|---------------------|-------------|
|  | <i>2005</i>         | <i>2006</i> |
|  | <b>RMB</b>          | <b>RMB</b>  |
| Balance at beginning of year                     |                     |             |
| Additions arising on acquisition of a subsidiary |                     | 1,594       |
| Balance at end of year                           |                     | 1,594       |

***Deferred revenue and other items***

|   | <i>Year ended December 31,</i> |             |
|---|--------------------------------|-------------|
|   | <i>2005</i>                    | <i>2006</i> |
|   | <b>RMB</b>                     | <b>RMB</b>  |
| Balance at beginning of year                                  | 14,091                         | 18,413      |
| Addition during the year                                      | 105,407                        | 130,477     |
| Recognized in the condensed consolidated statements of income | (101,085)                      | (126,109)   |
| Balance at end of year  | 18,413                         | 22,781      |
| Less: Current portion   | (16,975)                       | (21,851)    |
|   | 1,438                          | 930         |

Deferred revenue comprises:

- (i) the unamortized portion of connection fees and telephone number selection fees received which are recognized over the estimated subscriber usage period for the related services;
- (ii) the deferred tax credit of purchase of domestic telecommunications equipment which is amortized over the remaining lives of the related property, plant and equipment;
- (iii) the prepaid services fees received from subscribers which are recognized as income when the mobile telecommunications services are rendered upon actual usage by subscribers; and

- (iv) the unamortized portion of net savings attributable to the Group as a result of the provincial interconnection, roaming and leased line agreements.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **41 Additional information required by US GAAP (continued)**

#### ***Stock option plan***

Details of the Company's stock option plan and options granted under the plan are contained in note 33. The fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model and the binomial lattice model for 2004 and 2005 respectively, with the following assumptions used for grants: expected dividend yield of 2.65% and 2.58% during 2004 and 2005; expected volatility of 27.38% and 24.58% for the share option granted during 2004 and 2005 respectively; risk-free interest rate of 4.06% and 4.54% during 2004 and 2005 respectively; and expected life of 10 years and 10 years during 2004 and 2005 respectively. The per share fair value of stock options granted during 2004 and 2005 were HK\$6.64 and HK\$10.28 on the date of grant, respectively.

The total intrinsic value of options exercised during 2004, 2005 and 2006 were HK\$nil, HK\$185 and HK\$677 respectively. Cash received from option exercise under the share option plans for 2004, 2005 and 2006 were HK\$662, HK\$3,246 and HK\$3,994 respectively. No actual tax benefit was realized from option exercises for the year purchased.

Prior to January 1, 2006, the Company applied the intrinsic-value-based method of accounting prescribed by APB 25, and related interpretations including FASB Interpretation No. 44, Account for Certain Transactions Involving Stock Compensation, an interpretation of APB Opinion No. 25, issued in March 2000, to account for its plan. Under this method, compensation expense is recorded on the date of grant only if the current market price of the underlying stock exceeds the exercise price. FASB No. 123, Accounting for Stock-Based Compensation (SFAS No. 123) and FASB No. 148, Accounting for Stock-Based Compensation Transition and Disclosure, an amendment of FASB 123, established accounting and disclosure requirements using a fair-value-based method of accounting for stock-based employee compensation plans. As permitted by the relevant accounting standards, the Company had elected to continue to apply the intrinsic-valued-based method of accounting described above, and had adopted only the disclosure requirements of SFAS No. 123, as amended. The compensation cost that has been charged against income prescribed by APB 25 for the Company's stock option plan was RMB86 for 2004 and RMB68 for 2005. The following table illustrates the effect on net income if the fair-value-based method had been applied to all outstanding and unvested awards in each period.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***41 Additional information required by US GAAP (continued)*****Stock option plan (continued)***

|   | <i>Year ended December 31,</i> |             |
|---|--------------------------------|-------------|
|   | <i>2004</i>                    | <i>2005</i> |
|   | <b>RMB</b>                     | <b>RMB</b>  |
| Net income, as reported   | 45,061                         | 54,504      |
| Add stock-based employee compensation expense included in net income                            | 86                             | 68          |
| Deduct total stock-based employee compensation expense determined under fair-value-based method | (842)                          | (1,752)     |
| Pro forma net income  | 44,305                         | 52,820      |
| Basic net income per share  |                                |             |
| As reported   | 2.29                           | 2.76        |
| Pro forma   | 2.25                           | 2.68        |
| Diluted net income per share  |                                |             |
| As reported   | 2.29                           | 2.75        |
| Pro forma   | 2.25                           | 2.66        |

Effective from January 1, 2006, the Company adopted the requirements of SFAS No. 123R using the modified-prospective transition method in which the grant-date fair values of unvested awards that are outstanding on the date of adoption are charged to expense over their remaining vesting periods. The compensation expense recognized for the year ended December 31, 2006 for the Company's stock option plan was RMB2,476. The aggregate intrinsic value of the share options outstanding and exercisable as of December 31, 2006 was RMB144 and RMB144, respectively.

As a result of adopting SFAS No. 123R on January 1, 2006, the Group's profit before income taxes and net profit for the year ended December 31, 2006 were both RMB2,439 lower than if it had continued to account for share-based compensation under APB 25. Basic and diluted income per share for the year ended December 31, 2006 were both RMB0.12 lower than if the Group had continued to account for the share-based compensation under APB 25. The adoption of SFAS No. 123R had no effect on the consolidated cash flow statement.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)***41 Additional information required by US GAAP (continued)****Net income per share**

The following is a reconciliation of the numerators and denominators of the basic and diluted net income per share computations prepared under US GAAP.

|                                      | <i>For the year ended December 31, 2004</i> |                      |                  | <i>For the year ended December 31, 2005</i> |                      |                  | <i>For the year ended December 31, 2006</i> |                      |                  |
|--------------------------------------|---|----------------------|------------------|---|----------------------|------------------|---|----------------------|------------------|
|                                      | <i>Income</i>                               | <i>Shares</i>        | <i>Per share</i> |   | <i>Shares</i>        | <i>Per share</i> |   | <i>Shares</i>        | <i>Per share</i> |
|                                      | <i>(Numerator)</i>                          | <i>(Denominator)</i> | <i>Amount</i>    | <i>Income</i>                               | <i>(Denominator)</i> | <i>Amount</i>    | <i>Income</i>                               | <i>(Denominator)</i> | <i>Amount</i>    |
| <b>Basic net income per share</b>    | 45,061                                      | 19,673               | 2.29             | 54,504                                      | 19,738               | 2.76             | 65,074                                      | 19,893               | 3.27             |
| <b>Effect of dilutive securities</b> |   |                      |                  |   |                      |                  |   |                      |                  |
| Convertible notes                    | 129   | 91                   |                  | 135   | 76                   |                  |   |                      |                  |
| Stock options                        |   | 10                   |                  |   | 78                   |                  |   | 186                  |                  |
| <b>Diluted net income per share</b>  | 45,190                                      | 19,774               | 2.29             | 54,639                                      | 19,892               | 2.75             | 65,074                                      | 20,079               | 3.24             |

**Principal related party transactions**

|  | <i>Note</i> | <i>Year ended December 31,</i> |             |             |
|--|-------------|--------------------------------|-------------|-------------|
|  |             | <i>2004</i>                    | <i>2005</i> | <i>2006</i> |
|  |             | <i>RMB</i>                     | <i>RMB</i>  | <i>RMB</i>  |
| Interconnection revenue  | (ii)        | 5,940                          | 6,196       | 8,510       |
| Interconnection charges  | (ii)        | 11,911                         | 13,588      | 16,416      |
| Leased line charges  | (ii)        | 3,745                          | 3,054       | 1,757       |
| Spectrum fees  | (i)         | 406                            |             |             |
| Property leasing and management service charges                | (i)         | 643                            | 780         | 804         |
| Telecommunications services charges                            | (i)         | 809                            | 1,898       | 2,359       |
| Technology platform development and maintenance service income | (i)         | 25                             | 12          |             |
| Interest paid/payable  | (i)         | 721                            | 647         | 946         |

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Notes:

- (i) Descriptions of the nature of the related party transactions are set forth in note 30.
- (ii) Descriptions of the nature of the related party transactions are set forth in note 31. The amounts also include charges paid or payable to the state-controlled telecommunications operators in the PRC.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **41 Additional information required by US GAAP (continued)**

#### ***Segment reporting***

SFAS No. 131, Disclosures about Segments of an Enterprise and Related Information, established standards for reporting information about operating segments in financial statements. Operating segments are defined as components of an enterprise about which separate financial information is available that is evaluated regularly by the chief operating decision maker, or decision making group, in deciding how to allocate resources and in assessing performance.

The Company's operating segments are comprised of its mobile telecommunications businesses operated within the thirty-one provinces, autonomous regions and municipalities in Mainland China and Hong Kong. The operating segments are managed separately because each operating segment represents a strategic business unit that serves different markets. All operating segments provide mobile telecommunications services to individual customers within their geographic market. The Company's operating segments have been aggregated into a single reportable segment as permitted under US GAAP because management believes all of the criteria for aggregation have been met.

#### ***Business risks***

The Group conducts its principal operations in the PRC and accordingly is subject to special considerations and significant risks not typically associated with investments in equity securities of United States and Western European companies. These include risks associated with, among others, the political, economic and legal environment, extensive government regulations and competition in the mobile telecommunications industry.

#### ***New telecommunications law***

In order to provide a uniform regulatory framework for the telecommunications industry in the PRC, the MII, pursuant to the direction of the PRC State Council, is currently preparing a draft of the Telecommunications Law of the PRC (the Telecommunications Law). The draft law, when formulated, will be submitted to the National People's Congress for review and adoption. It is unclear if and when the Telecommunications Law will be adopted, and the nature and scope of regulation envisaged by the Telecommunications Law are not fully known. There can be no assurance that the Telecommunications Law, if adopted, would not have a material adverse effect on the Group's business, financial condition and results of operations.

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Notes to Consolidated Financial Statements (continued)

*(Amounts in millions, except share data)*

### **41 Additional information required by US GAAP (continued)**

#### ***Amount of spectrum availability***

The Group's mobile telecommunications system's subscriber capacity is limited by the amount of spectrum available for use by the system. The former State Radio Regulatory Commission, now a department within the MII, is responsible for the overall allocation of radio frequency spectrum in the PRC. There can be no assurance that the Group would be granted additional spectrum when and if required, and any resulting levels of system congestion could result in subscriber dissatisfaction, decreased system usage by subscribers and increased churn rate.

#### ***Interconnection arrangement with networks of other operators***

The Group's mobile telecommunications services depend in large part upon access to the network of other operators. Any disruption of interconnection with the networks of operators could have a material adverse effect on the Group's results of operations.

#### ***Changes in technology***

The telecommunications industry is subject to rapid and significant changes in technology. Accordingly, the mobile telecommunications technologies that the Group currently employs may become obsolete or subject to competition from new technologies in the future, including new wireless telecommunications technologies. In addition, the new technologies the Group implements, such as wireless data applications, may not generate an acceptable rate of return.

#### ***New competition***

Current Chinese government policy concerning the telecommunications sector is to encourage orderly competition. There can be no assurance that the State Council will not approve additional telecommunications service providers in the future, including providers of mobile telecommunications services, that may compete against the Group. In addition, China's accession into the WTO could lead to increased foreign investment in the telecommunications market in Mainland China, thereby increasing competition and foreign participation in the mobile telecommunications service sector in Mainland China. Increased competition and foreign participation may have a material adverse effect on the Group's financial conditions and results of operation.

#### ***Self insurance risk***

The Group does not maintain any insurance policies to cover its assets.