

Operational Review

Introduction

In 1997, the Group achieved significant development of its cellular telecommunications operations in Guangdong and Zhejiang provinces. The subscriber base recorded impressive growth of 67 per cent from 2.043 million in 1996 to 3.405 million in 1997. This laid a solid foundation for the future development of the Group.

The Company was incorporated and completed its corporate restructuring in September 1997. After the corporate restructuring, the Company has 100 per cent ownership of Guangdong Mobile Communication Company Limited and 99.63 per cent ownership of Zhejiang Mobile Communication Company Limited. The Company's cellular telephone operations in Guangdong and Zhejiang provinces are vested in these two subsidiaries. The remaining 0.37 per cent interest in Zhejiang Mobile Communication Company Limited is held by three local companies in Zhejiang province.

The shares of the Company were listed on the New York Stock Exchange and the Hong Kong Stock Exchange on 22 October 1997 and 23 October 1997, respectively. After being listed for only three months, the Company became a constituent stock of the Hang Seng Index in Hong Kong.

Maintaining subscriber growth and high cellular usage

As at 31 December 1997, the Group had an aggregate subscriber base of 3.405 million. This represented substantial growth of approximately 67 per cent over 1996. Among these, 2.502 million cellular subscribers are in Guangdong, of which new subscribers comprised 934,000, an increase of 59.6 per cent over 1996. Zhejiang recorded dramatic growth of 90 per cent, with 428,000 new subscribers, taking the total subscriber base to 903,000.

During the year, the Group not only achieved strong growth in new subscribers, but also successfully maintained a high level of network usage. In 1997, total minutes of usage amounted to 14.4 billion minutes, an increase of 43.4 per cent over the previous year. Guangdong and Zhejiang contributed 10.7 billion minutes and 3.7 billion minutes respectively, showing growth rates of 39 per cent for Guangdong and 57.8 per cent for Zhejiang. During the year, the monthly average usage per subscriber of the Group was 440.5 minutes while the monthly average usage per subscriber for Guangdong province was 438.2 minutes and that for Zhejiang province was 447.5 minutes. The monthly average usage for 1997 was lower than that for the previous year.

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The impressive increase in total minutes of usage and the decrease in average usage per subscriber resulted directly from the substantial growth in total subscribers, changes in subscriber demographics and improvement in telecommunications infrastructure. It also indicates the promising potential for future growth in subscriber usage. The development of more value-added services is an effective way to improve customer service and encourage increased use of cellular telecommunications.

In 1997, in order to meet international standards in this respect, the Group developed and introduced value-added services such as international roaming, caller display, call forwarding, call waiting, conference calling, call filtering, mobile fax/data, stored value cards and public mobile phone cards. The Group's "Global Access Network" now extends to 22 countries and regions covering Singapore, Malaysia, Germany, Finland, Australia, the United Kingdom, Indonesia, Sweden, Italy, Switzerland, Turkey, Spain, Belgium, Lebanon, Denmark, France, the Netherlands, Austria, Poland, Hong Kong, Macau and Taiwan, realising our goal of "Accessing the whole country and roaming all over the world with a cellular phone".

The introduction of stored value cards was well received by the market. This proved to be a convenient and efficient service for users with an intermittent need for cellular telecommunications. The Group's innovative Mobile Office service not only offers subscribers a quality voice service, but also the convenience of mobile fax/data communication. In 1997, through attractive packaging, pricing and active marketing efforts, Mobile Office proved to be popular with business subscribers. The Group is optimistic about the potential of Mobile Office for further development.

Expanding the network to meet growing demand

To facilitate fast growth in its subscriber base, the Group dramatically expanded its GSM digital network in addition to improving and optimising its TACS analogue network. As of 31 December 1997, total network capacity had reached 5.58 million, of which 3.74 million came from GSM and 1.84 million from TACS. Base stations were increased to 4,980, 3,185 of which were base stations for the GSM digital network and 1,795 were base stations for the TACS analogue network. The number of channels expanded to 198,600 with digital comprising 124,200 and analogue 74,400.

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Through network expansion and improvements, the Group improved the operations of its networks and extended its network coverage to rural villages and manufacturing plants as well as high usage areas such as commercial buildings, shopping malls and specialty markets. This helped to improve the network's connection rate and to maintain the drop-out rate at a relatively low level.

Customer service the focus of marketing strategies

The Group believes that its business is wholly controlled by market conditions which in turn are driven by subscribers. As a result, the Group is a highly customer-oriented organisation. The Group endeavours to offer high-quality and efficient services to subscribers. While improving and optimising the infrastructure of its mobile telecommunications network, the Group also enhanced its computerised management information system.

In Guangdong province, the computerised management information system has been extended to cover all cities, counties and major villages with consequent improvements in service efficiency that have enabled the Group to keep pace with the rapid growth in its business. In Zhejiang province, the Group has also introduced a computerised management information system. A pilot scheme has been completed in Jiaxing and preparatory work is actively under way in cities such as Hangzhou, Wenzhou, Jinhua and Zhaoxing.

The Group has set up a subscriber service monitoring centre in Guangdong province and has established a hotline service. The service monitoring centre also provides major customers with prioritised services such as account opening, payments, enquiries and service directory. The Group has also established dedicated subscriber service desks for major customers in cities such as Guangzhou and Shenzhen. These services have proved to be very popular with major customers.

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The Group has conducted extensive research into market demand. Subscribers from a wide spectrum were analysed on the basis of various subjects including subscriber demographics, income patterns and geographical distribution. This research and analysis has enabled the Group to develop appropriate marketing strategies which have successfully attracted new subscribers. As a result of the complete deregulation of terminal equipment, subscribers can now register to use the Group's services with their own cellular phones. This has stimulated significant market demand. A record was set when the subscriber base in Guangdong province increased by 100,000 in a single month.

The Group also leveraged special opportunities such as World Telecom Day on 17 May 1997 as well as its corporate restructuring and listing to introduce promotional packages targeted at attracting subscribers to use the well-developed and flexible network services provided by "Global

Access Network". In Zhejiang province alone, the World Telecom Day promotion secured 51,000 new subscribers, while the latter promotion also achieved impressive results with a further 70,000 new subscribers registered during the one-and-a-half month promotion period.

To cater for subscriber demand, the Group has been actively expanding its distribution channels by aggressively developing its own cellular telecommunication sales outlets and representative sales arrangements, in addition to making full use of the extensive network of Posts and Telecommunications Administrations' sales outlets. In 1997, the Group successfully introduced the 138 prefix to relieve pressure on available numbering resources and to provide scope for future growth in subscriber base.

As a result of these efforts, the Group maintained a combined market share of more than 97.5 per cent of the mobile telecommunications market in Guangdong province and in Zhejiang province.

* Average revenue per subscriber per month is calculated by dividing the usage fees, monthly fees, connection fees and other receipts during the year by the average number of subscribers during the year and dividing the result by the number of months in the year

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Community service

The Group recognises that corporate growth is closely linked to community development. In 1997, the Group participated in a number of social welfare activities to actively contribute towards the progress of the community.

In 1997, the Group donated RMB1.5 million to construct the "Global Access Hope Primary School" in the poor mountainous regions in Guangdong province, promoting education in regions of limited means in China.

In addition, the Company accepted an invitation from the government of the Hong Kong Special Administrative Region to jointly sponsor the 1997 Chinese New Year fireworks display with Hongkong Telecom to celebrate the Chinese New Year and to bring happiness to Hong Kong people during the festive season.

Looking into the future

In recent years, China has undergone rapid economic growth, expanded its open-door policy and embarked on intensive economic reform. This has contributed to a significant increase in investment and upgrading of technology standards, as well as to a significant improvement in service quality in the telecommunications business. The telecommunications industry is now one of the fastest growing business sectors in China. Based on subscriber numbers, China boasts one of the largest telecommunications networks in the world.

Although the subscriber base for both fixed-line and cellular telecommunications has witnessed dramatic growth in the last five years, the average telephone penetration rate in China remains low in comparison with other Asian countries and developed countries. As a result, the telecommunications industry in China has the potential to continue to grow rapidly. Even in Guangdong and Zhejiang provinces, the cellular penetration rates are still low, being only 3.57 per

cent and 2.04 per cent respectively. The Group believes that the market still has potential for major growth.

In 1998, the Group will continue to expand its cellular telecommunications infrastructure. The focus is to extend GSM coverage and to increase network capacity while optimising the TACS network, and further improving the efficiency of the usage of GSM network spectrum. The Group is also planning to adopt the DCS 1800 system. More importantly, the Group will actively open up the potential market by offering new telephone number ranges with the prefixes "135", "136" and "137". New value-added services are planned, including short message service, voicemail and a Chinese language secretarial service to meet the needs of a wide spectrum of subscribers.

The Group will actively adopt advanced management information systems to enhance its management to meet international standards and to improve its operating efficiency, as well as to expedite the development of the huge potential market in China. This is so that the Group can provide top-quality services to subscribers, to maximise return on investment to shareholders and to offer the best value for their money. The Group will also explore strategic investment opportunities in China's telecommunications market, including opportunities to acquire quality telecommunications businesses. The Group is currently in discussions with relevant parties about acquiring a cellular telecommunications business in Jiangsu Province.

At the first session of the Ninth National People's Congress in March 1998, a motion was passed to implement the restructuring of government bodies. The Ministry of Information Industry was established to assume all the government functions of the previous Ministry of Posts and Telecommunications. The Group believes that this institutional reform, which created a demarcation between government and enterprise functions,

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will help to establish a fairer and a more orderly competitive environment. This is not only beneficial to the overall development of the telecommunications industry in China, but will also contribute towards improving the management, operations and service quality of the Group. The Group has received reassurance that the Ministry of Information Industry will

assume all undertakings given by the previous Ministry of Posts and Telecommunications at the time of listing of the Company's shares.

The year 2000 date-change problem has always been a major concern to senior management of the Group. To avoid any adverse impact created by the year 2000 problem the Group has already set up a dedicated team to address this issue.

Summary of operating statistics

Operating Data	Year ended 31 December			
	1994	1995	1996	1997
Cellular Penetration (%)	0.53	1.13	1.81	2.97
Cellular Subscriber Base ('000)	576	1,256	2,043	3,405
Market Share (%)	100	99	98	97.6
Annual Churn Rate (%)	0.5	0.7	1.3	1.64
Total Minutes of Use (millions)	2,760	5,798	10,042	14,400
Average MOU per Sub per Month	539	527	507	441
ARPU per Month — RMB	897	691	524	474
— US\$	108	83	63	57
Cellular Subscriber Capacity ('000)	719	1,845	3,272	5,580
Base Stations	673	1,992	3,217	4,980