FINANCIAL REVIEW

Benefiting from China's stable and rapid economic growth, vigorous market demand and healthy competitive environment, together with the Group's highly efficient quality network, strong brand advantages and economies of scale, this year, building on years of its sustained successive development, subscribers, revenue and profits marked another terrific record year for 2006, delivering an overall impressive performance. Operating revenue for 2006 rose to RMB295,358 million, up 21.5 per cent.. Earnings capability was further enhanced. Profit attributable to shareholders increased 23.3 per cent. to RMB66,026 million. Margin of profit attributable to shareholders rose to a relatively high level of 22.4 per cent.. EBITDA reached RMB159,574 million, up 19.7 per cent.. Basic earnings per share grew 22.5 per cent. to RMB3.32. The Group continued to reinforce its financial strengths, which further consolidated its industry leadership position in the mobile telecommunications market in China.

* *Financial information for the year 2006 set out in this Financial Review includes the operating results of the Company, its thirty-one operating subsidiaries in Mainland China and the newly acquired China Mobile Peoples Telephone Company Limited whereas that of the year 2005 includes the operating results of the Company and its thirty-one operating subsidiaries.*

Extracts from income statement

	2006 RMB million	2005 RMB million	Change %
Operating revenue (Turnover)	**295,358**	243,041	21.5
Usage fees and monthly fees	**211,339**	181,765	16.3
Value-added services fees	**69,309**	50,187	38.1
Other operating revenue	**14,710**	11,089	32.7
Operating expenses	**203,230**	169,355	20.0
Leased lines	**2,451**	3,224	(24.0)
Interconnection	**18,783**	15,309	22.7
Depreciation	**64,574**	56,368	14.6
Personnel	**16,853**	14,200	18.7
Other operating expenses	**100,569**	80,254	25.3
Profit from operations	**92,128**	73,686	25.0
Other net income	**2,872**	3,284	(12.5)
Profit attributable to shareholders	**66,026**	53,549	23.3
EBITDA	**159,574**	133,338	19.7

Extracts from balance sheet

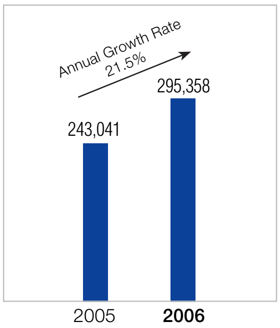
	2006 RMB million	2005 RMB million	Change %
Current assets	**171,507**	121,076	41.7
Non-current assets	**323,169**	299,951	7.7
Total assets	**494,676**	421,027	17.5
Current liabilities	**140,607**	109,954	27.9
Non-current liabilities	**34,696**	37,966	(8.6)
Total liabilities	**175,303**	147,920	18.5
Minority interests	**371**	283	31.1
Shareholders' equity	**319,002**	272,824	16.9

Extracts from cash flow statement

	2006 RMB million	2005 RMB million	Change %
Net cash generated from operating activities	**149,346**	131,709	13.4
Net cash used in investing activities	**(118,841)**	(87,116)	36.4
Net cash used in financing activities	**(23,587)**	(25,173)	(6.3)

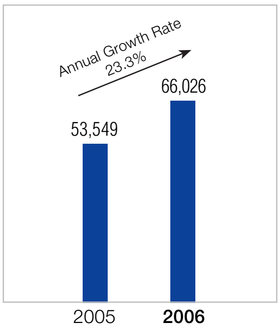
Operating Revenue

(RMB Million)



Profit Attributable to Shareholders

(RMB Million)



MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Summary of Financial Results

In 2006, benefiting from China's stable and rapid economic growth, vigorous market demand and healthy competitive environment, the Group continued to propel its economies of scale and maintain its innovative growth. Building upon its years of growth in the eastern region and leveraging its highly efficient superior network and strong brand advantages, the Group further explored into the central and western regions and the rural markets that have enormous market potential. Through rational capital expenditures, stringent cost control measures and comprehensive implementation of refined management methodology, the Group continued to deliver impressive operating performance.

With the continuing push of three driving forces – new customers, new businesses and new voice usage, the financial results of the Group marked a new height. Operating revenue of the Group for 2006 reached RMB295,358 million, representing an increase of 21.5 per cent. over the previous year. The operating revenue from value-added business, which has continued its rapid growth momentum, reached RMB69,309 million, representing an increase of 38.1 per cent. over the previous year, and accounted for 23.5 per cent. of the Group's total operating revenue. In order to maintain its competitive advantages and sustainable and healthy development, the Group allocated more resources towards the establishment of sales and marketing channels and the provisions of differentiated services in 2006 while appropriately expanding its network capacity and performing network maintenance at the same time. As such, operating expenses reached RMB203,230 million, representing an increase of 20.0 per cent. over the previous year. Such percentage increase in operating expenses from 2005 to 2006 was lower than that in operating revenue during the same period which, in combination with the continued decrease in average operating expenses per user per month and per minute, further demonstrated the Group's competitive advantages in its refined and effective cost control measures and economies of scale.

Profit attributable to shareholders was RMB66,026 million, representing an increase of 23.3 per cent. over the previous year, and margin of profit attributable to shareholders reached a relatively high level of 22.4 per cent.. EBITDA was RMB159,574 million, representing an increase of 19.7 per cent. over the previous year, giving a margin of 54.0 per cent.. Basic earnings per share was RMB3.32, representing an increase of 22.5 per cent. from the previous year and demonstrating a relatively high profitability.

The Group sustained its robust cash flow as a result of favorable business growth, effective cost management and control measures, efficient capital expenditure and increasing economies of scale. In 2006, the Group's net cash generated from operating activities and free cash flow reached RMB149,346 million and RMB62,358 million, respectively. The Group's total debt to capitalization ratio and interest coverage multiple remained at a sound level. Each of Moody's and Standard and Poor's further upgraded the Company's corporate credit rating in 2006, reflecting that the prudent approach consistently adopted by the Company has won popular recognition from the market.

Operating Revenue (Turnover)

Operating revenue for 2006 reached RMB295,358 million, representing an increase of 21.5 per cent. over the previous year. The Group advocated and continued to promote rational competition, strengthened its innovative capabilities, and implemented effective measures to further develop its market. Subscriber base continued its rapid growth momentum. The average net increase of the Group's number of subscribers exceeded 4.43 million per month in 2006. Total minutes of usage increased to 1,252,146 million minutes, representing an increase of 38.6 per cent. from the previous year. The revenue per minute declined by 12.3 per cent. from the previous year. Such rate of decline was under sound control and the growth rate of both the voice usage volume and revenue increased proportionately. The growth in subscriber base and voice volume usage ensured the rapid growth in operating revenue and ARPU stability.

The Group proactively carried out product innovations and business promotion for valued-added business. The Group's various value-added business maintained good growth momentum and the increase in the revenue attributable to such business was notable in 2006. Revenue from value-added business reached RMB69,309 million in 2006, representing an increase of 38.1 per cent. over the previous year, and accounted for 23.5 per cent. of the Group's total operating revenue, representing an increase of 2.9 percentage points compared to that of 20.6 per cent. in the previous year, thus reaching a relatively high level among its international counterparts. Revenue from Short Message Services (SMS) and non-SMS data businesses reached RMB52,888 million in 2006 and accounted for 76.3 per cent. of the Group's revenue from value-added business. While the SMS business continued to maintain its relatively high growth rate, businesses such as WAP, "Color Ring" and Multimedia Messaging Service (MMS) grew rapidly. New product offerings and new applications such as "IM" and mobile email were introduced to the market. Businesses such as mobile music were also proactively developed. As a result, the revenue structure of the value-added business was further optimized in 2006.

Operating Expenses

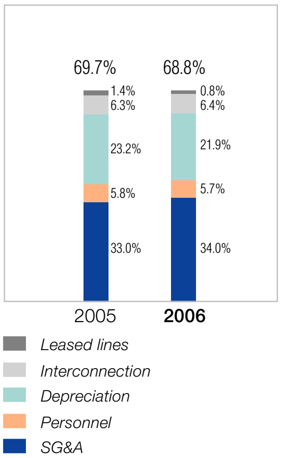
The Group benefited from its refined and effective cost control measures consistently adopted, efficient capital expenditures and notably its advantages of economies of scale. As a result, the percentage increase in operating expenses from 2005 to 2006 was lower than the increase in operating revenue during the same period, and the Group's costs structure became more rationalized. Operating expenses for 2006 were RMB203,230 million, representing an increase of 20.0 per cent. from the previous year. Operating expenses for 2006 amounted to 68.8 per cent. of the total operating revenue, representing a decline of 0.9 percentage points from the previous year. Average operating expenses per user per month for 2006 were RMB61.8, representing a decline of 1.7 per cent. from the previous year, and the average operating expenses per minute of usage were RMB0.162, representing a decline of 13.4 per cent. from the previous year.

The Group continued to optimize its network structure and augment the Group's network. Self-constructed and jointly-constructed lines have reached a sizeable scale. The Group's leased line expenses continued to decline significantly. The Group's leased line expenses for 2006 were RMB2,451 million, representing a decline of 24.0 per cent. from the previous year. Leased line expenses accounted for 0.8 per cent. of the total operating revenue in 2006.

As a result of the sustained growth of the Group's subscriber base and the continued increase in voice usage volume, interconnection expenses were RMB18,783 million in 2006, representing an increase of 22.7 per cent. over the previous year and amounted to 6.4 per cent. of the total operating revenue. The Group increased its efforts to optimize network structure, carefully reorganized and re-routed traffic volume through marketing strategies and continued to increase the proportion of the voice usage volume within the network so that the proportion of interconnection expenses to total operating revenue was maintained at a reasonable level.

The continuing evolution of telecommunication technology and the appearance of a large number of new technologies and new services had a considerable impact on the life of the Group's technologies and the remaining life of certain existing network equipment. The Group consistently performed assessment and evaluation on the utilization of its existing network equipment in accordance with the principle of prudent financial management. In 2006, the Group revised the estimated useful lives of its 2G wireless network equipment from seven years to five years based on the assessment and evaluation, and to better reflect the actual utilization of the assets. As a result, depreciation expenses were RMB64,574 million in 2006, representing an increase of 14.6 per cent. from the previous year. Depreciation expenses accounted for 21.9 per cent. of the total operating revenue, representing a decline of 1.3 percentage points from that of the previous year. The additional depreciation expenses as a result of the revision in the useful lives of the Group's 2G wireless network equipment amounted to RMB11,451 million. In 2007, following the consistent review and assessment on its existing assets with the latest development of telecommunications technologies, the Company plans to revise the estimated useful lives of its switching centre equipment (excluding soft switching equipment that is conformed with the new generation technology) from 7 years to 5 years. However, the effect of such change to depreciation expense for the year ending 31 December 2007 is estimated to be less than that of 2006.

Proportion of Operating Expenses over Operating Revenue



The Group continued to strengthen its highly-efficient staff management and incentive structure, promote human resources management and persistently implement effective and comprehensive budget management and performance-based evaluation, thus maintaining a competitive advantage of human resources. Meanwhile, the percentage increase in personnel expenses from 2005 to 2006 was kept lower than the percentage increase in operating revenue and profit attributable to shareholders during the same period. Personnel expenses were RMB16,853 million, accounted for 5.7 per cent. of the total operating revenue of 2006, representing a slight decline from the previous year. The Group had a total of 111,998 employees as of 31 December 2006.

Other operating expenses (consisting primarily of sales and marketing expenses, customer services, subscriber retention costs, doubtful debts, administration and other general expenses) were RMB100,569 million in 2006, representing an increase of 25.3 per cent. from the previous year, and accounted for 34.0 per cent. of the total operating revenue. In order to further enhance brand awareness and levels of differentiated service offerings, reward and retain high-value customers and increase customer loyalty, the Group increased its efforts in marketing, promotions and customer service. As a result, sales and marketing expenses increased accordingly. In view of the Group's emphasis on rigorous customer credit management and the stringent control over defaults in payment by customers, the Group continued to restrain its bad debt ratio to a relatively low level of 1.30 per cent. in 2006. Furthermore, in order to meet the requirements of new technology and development of new businesses, the Group continued to upgrade certain outdated equipment and wrote off and disposed off corresponding assets of RMB2,903 million in 2006, thus further improving its assets quality and better preparing itself for the transition of its network to the next generation as well as the development of new businesses in the future. In addition, the Group further expanded its scope of centralized equipment procurement and reduced the purchase costs by enhancing its economies of scale to optimum.

The Company determines to continue to pursue refined management methodology, constantly optimize its cost structure, and emphasize cost effectiveness in order to maximize returns.

EBITDA, PROFIT FROM OPERATIONS AND PROFIT ATTRIBUTABLE TO SHAREHOLDERS

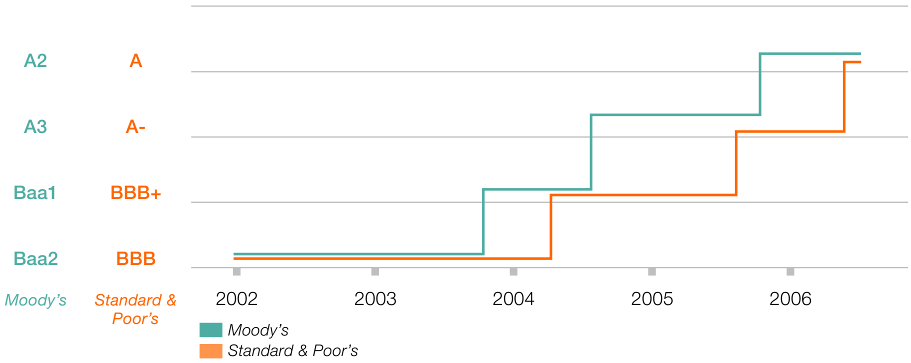
The Group has consistently endeavored to maintain long-term, sustainable and favorable profit growth. Margin of profit attributable to shareholders and EBITDA margin in 2006 remained high at 22.4 per cent. and 54.0 per cent., respectively. Operating profit was RMB92,128 million and maintained at a stable growth. EBITDA was RMB159,574 million, representing an increase of 19.7 per cent. over the previous year. Profit attributable to shareholders was RMB66,026 million, representing an increase of 23.3 per cent. over the previous year. Basic earnings per share was RMB3.32, representing an increase of 22.5 per cent. over the previous year. These commendable earnings performance and the continuous improvement on earnings level reflected the Group's ceaseless efforts in generating greater returns and creating value for its shareholders. Along with the favourable revenue growth, these results also reflected the Group's efforts in strengthening its management efficiencies on operating expenses and economies of scale. This further enhanced the operational efficiency of the Group. The Group will seek to continue to pursue sustainable and steady long-term growth.

STRONG CASH FLOW AND SOUND CAPITAL STRUCTURE

In 2006, the Group continued generating strong cash flow. The Group's net cash generated from operating activities was RMB149,346 million and free cash flow (net cash generated from operating activities after deduction of capital expenditure incurred) was RMB62,358 million. At the end of 2006, the Group's total cash and bank balances were RMB153,461 million, of which 96.2 per cent., 0.5 per cent. and 3.3 per cent. were denominated in RMB, U.S. dollars and Hong Kong dollars, respectively.

To further reduce the cost of capital, the Group continued to reinforce its centralized treasury function and make appropriate allocations of overall capital, thereby enhancing the Group's ability to deploy internal funds with maximum utility. Robust cash flow and stable capital management have provided a solid foundation for the long-term development of the Group.

At the end of 2006, the Group's long-term loans and short-term loans were RMB38,850 million in aggregate, and its debt to capitalization ratio (with capitalization representing the sum of total debt and total equity) was approximately 10.9 per cent., reflecting the Group's financial position continued to remain at a sound level. Of the total borrowings, 39.2 per cent. were in RMB (consisting principally of RMB bonds, bank loans, etc.), and 60.8 per cent. were in U.S. dollars (consisting principally of the balance of the deferred consideration for the acquisition of the eight and the ten provincial telecommunications operators). Approximately 73.8 per cent. of the Group's borrowings were made at floating interest rates. The actual average interest rate of borrowings (including capitalized interest) of the Group in 2006 was approximately 3.93 per cent., whereas the actual interest coverage multiple (ratio of profit before interest and tax to interest expenses) was 63 times. This position reflects the prudent financial risk management principles consistently adopted by the Group, as well as its solid cash flow and sound repayment capability. In 2006, with the upgrading of China's sovereign credit rating, Standard & Poor's upgraded the Company's corporate credit rating from "A-/Positive Outlook" to "A/Outlook Stable". At the same time, Moody's also upgraded the Company's corporate credit rating from "A2/Outlook Stable" to "A2/Positive Outlook". These ratings demonstrated that the Group's sound financial strengths, huge business opportunities and solid financial management have established wide and deep market recognition.



DIVIDENDS

The Company consistently holds in the highest regard the interests of its shareholders and the returns achieved for them, especially the minority shareholders. In consideration of the Company's remarkable operating results in 2006 and its long-term development in the future, and in accordance with the dividend payout plan for the full year of 2006, the Board recommends payment of an ordinary final dividend of HK$0.763 per share for the financial year ended 31 December 2006. This, together with the ordinary interim dividend of HK$0.62 per share already paid during 2006, amounts 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 per cent. over the annual dividend of HK$1.02 per share for the full year of 2005. Dividend payout ratio for the year 2006 was 42 per cent.. In addition, whilst the profit and dividend per share for the year 2006 continued to maintain a favourable growth, the Board, having taken into account the interest of the Company's shareholders, recommends payments of a special dividend in 2006 of HK$0.069 per share on the effect resultant from revision of the Group's assets depreciable lives. This, together with the special interim dividend of HK$0.09 per share paid during 2006, amounts to a 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 the Group's overall financial condition, cash flow generating capabilities and future continuing development, the Company plans the dividend payout ratio for the full year of 2007 to be 43 per cent.. In addition, the Company will consider distributing a special dividend in 2007 for the effect on the profit attributable to shareholders based on the planned revision of depreciation policy in 2007. The Board is of the view that the Group's strong free cash flow is capable of supporting the investments required to maintain the stable growth of the Company, while providing shareholders with a favorable cash return. The Company will endeavor to achieve a longer term sustainable, steadily increasing dividend, with a view to generating the best possible return for shareholders.

The Group will continue to pursue prudent financial principles, strictly control financial risk, maintain its robust cash-flow generating capability, allocate its resources in an efficient manner, maintain debt at a sustainable level and reinforce and develop favorable economic efficiency, with a view to continue generating greater returns for its shareholders.