

# Report of the Directors

The Board of Directors (the "Board") of China Telecom Corporation Limited (the "Company") hereby presents its report together with the audited financial statements of the Company and its subsidiaries (collectively, the "Group") prepared in accordance with International Financial Reporting Standards for the year ended 31 December 2008.

## Principal Business

The principal business of the Company and the Group is the provision of basic communications services including comprehensive wireline telecommunications services, mobile telecommunications services, value-added services such as Internet access services, integrated information services and other related services within the service area of the Group.

## Results

Results of the Group for the year ended 31 December 2008 and the financial position of the Company and the Group as at that date are set out in the audited financial statements on pages 90 to 154 in this annual report.

## Dividend

The Board proposes a final dividend in the amount equivalent to HK\$0.085 per share, totalling approximately RMB6,063 million for the year ended 31 December 2008. The dividend proposal will be submitted for consideration at the Annual General Meeting to be held on 26 May 2009. Dividends will be denominated and declared in Renminbi. Dividends on domestic shares will be paid in Renminbi, whereas dividends on H shares will be paid in Hong Kong dollars. The relevant exchange rate will be the average offer rates of Renminbi to Hong Kong dollars as announced by the People's Bank of China for the week prior to the date of declaration of dividends at the Annual General Meeting. The final dividends are expected to be paid around 30 June 2009 after obtaining the shareholders' approval at the Annual General Meeting.

Pursuant to the Enterprise Income Tax Law of the People's Republic of China and the Detailed Rules for the Implementation of the Enterprise Income Tax Law of the People's Republic of China implemented in 2008, beginning from 1 January 2008, any Chinese domestic enterprise which pays dividend to a non-resident enterprise shareholder in respect of accounting periods beginning from 1 January 2008 shall withhold and pay enterprise income tax for such shareholder. Please refer to the relevant announcement to be issued by the Company separately for more details.

## Mobile Services

In the second half of 2008, the Company acquired China Unicom's CDMA mobile business, related assets, liabilities and equity for a consideration of RMB43,800 million. The Company also reached an agreement to lease the CDMA network capacity from China Telecommunications Corporation. In January 2009, the Company was permitted to operate the CDMA2000 3G mobile services. An amendment to the Articles of Association on the scope of business to include the CDMA2000 3G mobile services was approved at the Extraordinary General Meeting held on 12 March 2009. The above arrangement enables the Group to create the synergies with the existing operations by fully leveraging the communication network resources, sales and marketing and operational experience. By quickly accessing the fast developing mobile telecommunication market in the PRC and providing comprehensive services to customers, the Company will enhance the core competitiveness and create more value for our customers and shareholders.

## Directors and Senior Management of the Company

The following table sets out certain information of the Directors and senior management of the Company as at the date of this Report:

Name	Age	Position in the Company	Date of Appointment
Wang Xiaochu	51	Chairman and Chief Executive Officer	20 December 2004
Shang Bing	53	Executive Director, President and Chief Operating Officer	9 September 2008
Wu Andi	54	Executive Director, Executive Vice President and Chief Financial Officer	10 September 2002
Zhang Jiping	53	Executive Director and Executive Vice President	10 September 2002
Zhang Chenshuang	57	Executive Director and Executive Vice President	31 August 2007
Li Ping	55	Executive Vice President	10 September 2002
Yang Xiaowei	45	Executive Director and Executive Vice President	9 September 2008
Yang Jie	47	Executive Director and Executive Vice President	20 October 2004
Sun Kangmin	52	Executive Director and Executive Vice President	20 October 2004
Li Jinming	57	Non-executive Director	20 December 2004
Wu Jichuan	71	Independent Non-executive Director	9 September 2008
Qin Xiao	61	Independent Non-executive Director	9 September 2008
Tse Hau Yin, Aloysius	61	Independent Non-executive Director	9 September 2005
Cha May Lung, Laura	59	Independent Non-executive Director	9 September 2008
Xu Erming	59	Independent Non-executive Director	9 September 2005
Yung Shun Loy, Jacky	46	Assistant Chief Financial Officer, Qualified Accountant and Company Secretary	1 February 2005
Wang Qi	54	Financial Controller	10 September 2002

On 9 September 2008, the second session of the Board expired. Mr. Leng Rongquan, Mr. Li Ping, Mr. Zhang Youcai, Mr. Lo Hong Sui, Vincent and Mr. Shi Wanpeng no longer served as directors of the Company. The remaining directors from the second session of the Board continue to serve their duties for the third session of the Board after election at the Extraordinary General Meeting held on 5 September 2008. On the same day, Mr. Shang Bing, Mr. Yang Xiaowei, Mr. Wu Jichuan, Mr. Qin Xiao and Madam Cha May Lung, Laura were elected to the third session of the Board of Directors.

## Supervisors of the Company

The following table sets out certain information of the supervisors of the Company as at the date of this Report:

Name	Age	Position in the Company	Date of Appointment
Xiao Jinxue	45	Chairman of the Supervisory Committee	29 May 2007
Zhu Lihao	68	Independent Supervisor	10 September 2002
Ma Yuzhu	55	Supervisor (Employee Representative)	9 September 2005
Xu Cailliao	45	Supervisor	9 September 2005
Han Fang	36	Supervisor	9 September 2008

On 9 September 2008, the second session of the Supervisory Committee expired. Ms. Wang Haiyun no longer served in the position of Supervisor of the Company. Mr. Xiao Jinxue, Madam Zhu Lihao and Mr. Xu Cailliao, Supervisors of the second session of the Supervisory Committee, continue to serve for the third session of the Supervisory Committee after election at the Extraordinary General Meeting held on 5 September 2008. On the same day, Ms. Han Fang was elected as Supervisor of the Company for the third session of the Supervisory Committee starting from 9 September 2008. Mr. Ma Yuzhu continued to assume the position of Supervisor acting as the Employee Representative.

## Report of the Directors

### Share Capital

The share capital of the Company as at 31 December 2008 was RMB80,932,368,321, divided into 80,932,368,321 shares of RMB1.00 each. As at 31 December 2008, the share capital of the Company comprised:

Share category	Number of shares as at 31 December 2008	Percentage of the total number of shares in issue as at 31 December 2008 (%)
Domestic shares (total):	67,054,958,321	82.85
Domestic shares held by:		
China Telecommunications Corporation	57,377,053,317	70.89
Guangdong Rising Assets Management Co., Ltd.	5,614,082,653	6.94
Zhejiang Financial Development Company	2,137,473,626	2.64
Fujian State-owned Assets Investment Holdings Co., Ltd.	969,317,182	1.20
Jiangsu Guoxin Investment Group Co., Ltd.	957,031,543	1.18
Total number of H shares (including ADSs)	13,877,410,000	17.15
Total	80,932,368,321	100.00

## Material Interests and Short Positions in Shares and Underlying Shares of the Company

As at 31 December 2008, the interests or short position of persons who are entitled to exercise or control the exercise of 5% or more of the voting power at any of the Company's general meetings (excluding the Directors and Supervisors) in the shares and underlying shares of equity derivatives of the Company as recorded in the register required to be maintained under Section 336 of the Securities and Futures Ordinance (the "SFO") are as follows:

Name of shareholder	Number of shares held	Type of Shares	Percentage of the respective type of shares	Percentage of the total number of shares in issue	Capacity
China Telecommunications Corporation	57,377,053,317 (Long position)	Domestic shares	85.57%	70.89%	Beneficial owner
Guangdong Rising Assets Management Co., Ltd.	5,614,082,653 (Long position)	Domestic shares	8.37%	6.94%	Beneficial owner
RFS Holdings B.V.	907,191,530 (Long position)	H shares	6.54%	1.12%	Interest of controlled corporation
	1,180,327,134 (Short position)	H shares	8.51%	1.46%	Interest of controlled corporation
JPMorgan Chase & Co.	836,933,193 (Long position)	H shares	6.03%	1.03%	177,814,577 shares as beneficial owner, 90,202,000 shares as investment manager and 568,916,616 shares as security interest holder/approved lending agent
	98,549,345 (Short position)	H shares	0.71%	0.12%	Beneficial owner
	568,916,616 (Shares available for lending)	H shares	4.10%	0.70%	Security interest holder/ approved lending agent
Barclays PLC	828,576,318 (Long position)	H shares	5.97%	1.02%	Interest of controlled corporation
	2,052,000 (Short position)	H shares	0.01%	0.003%	Interest of controlled corporation

Save as stated above, as at 31 December 2008, in the register required to be maintained under Section 336 of the SFO, no other persons were recorded to hold any interests or short positions in the shares or underlying shares of the equity derivatives of the Company.

## Report of the Directors

### Directors' and Supervisors' Interests and Short Positions in Shares, Underlying Shares and Debentures

As at 31 December 2008, none of the directors and supervisors of the Company had any interests or short positions in the shares, underlying shares of equity derivatives or debentures of the Company or its associated corporations (as defined in Part XV of the SFO) as recorded in the register required to be maintained under section 352 of the SFO or as otherwise notified to the Company and The Stock Exchange of Hong Kong Limited pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers.

42

As at 31 December 2008, the Company had not granted its directors or supervisors, or their respective spouses or children below the age of 18 any rights to subscribe for the shares or debentures of the Company or any of its associated corporations and none of them has ever exercised any such right.

### Directors' and Supervisors' Interests in Contracts

For the year ended 31 December 2008, none of the directors and supervisors of the Company had any material interest, whether directly or indirectly, in any of the contracts of significance entered into by the Company, any of its holding companies or subsidiaries or subsidiaries of the Company's holding company, apart from their service contracts. None of the directors and supervisors of the Company has entered into any service contract which is not determinable by the Company within one year without payment compensation (other than statutory compensation).

### Emoluments of the Directors and Supervisors

Please refer to note 27 of the audited financial statements for details of the emoluments of all Directors and Supervisors of the Company in 2008.

### Purchase, Sale and Redemption of Shares

Neither the Company nor any of its subsidiaries has purchased, sold or redeemed any securities of the Company during the reporting period.

### Public Float

As at the date of this Report, based on the information that is publicly available to the Company and within the knowledge of the Directors, the Company has maintained the prescribed public float under the Listing Rules and as agreed with The Stock Exchange of Hong Kong Limited.

### Summary of Financial Information

Please refer to pages 155 to 156 of this annual report for a summary of the operating results, assets and liabilities of the Group for each of the years in the five-year period ended 31 December 2008.

### Bank Loans and Other Borrowings

Please refer to note 15 of the audited financial statements for details of bank loans and other borrowings of the Group.

## Capitalised Interest

Please refer to note 25 of the audited financial statements for details of the Group's capitalised interest for the year ended 31 December 2008.

## Fixed Assets

Please refer to note 3 of the audited financial statements for movements in the fixed assets of the Group for the year ended 31 December 2008.

## Reserves

Pursuant to Article 147 of the Company's articles of association (the "Articles of Association"), where the financial statements prepared in accordance with PRC accounting standards and regulations materially differ from those prepared in accordance with either International Financial Reporting Standards or those prepared in accordance with the place outside the PRC where the Company's shares are listed, the distributable profit for the relevant accounting period shall be deemed to be the lesser of the amounts shown in those respective financial statements. Distributable reserves of the Company as at 31 December 2008, calculated on the above basis and before deducting the proposed final dividends for 2008, amounted to RMB35,173 million.

As the Company has incurred net loss for the year of 2008, according to the PRC accounting standards, the Company did not transfer any funds to the statutory surplus reserve and the discretionary surplus reserve.

Please refer to note 20 of the audited financial statements for details of the movements in the reserves of the Company and the Group for the year ended 31 December 2008.

## Donations

For the year ended 31 December 2008, the Group made charitable and other donations with a total amount of RMB42 million.

## Subsidiaries and Associated Companies

Please refer to note 7 and note 8 of the audited financial statements for details of the Company's subsidiaries and the Group's interests in associated companies as at 31 December 2008.

## Changes in Equity

Please refer to the consolidated statement of changes in equity contained in the audited financial statements (page 95 of this annual report).

## Retirement Benefits

Please refer to note 36 of the audited financial statements for details of the retirement benefits provided by the Group.

## Stock Appreciation Rights

Please refer to note 37 of the audited financial statements for details of the stock appreciation rights offered by the Company.

## Report of the Directors

### Pre-Emptive Rights

There are no provisions for pre-emptive rights in the Articles of Association requiring the Company to offer new shares to the existing shareholders in proportion to their shareholdings.

### Major Customers and Suppliers

For the year ended 31 December 2008, sales to the five largest customers of the Group accounted for an amount no more than 30% of the operating revenue of the Group.

For the year ended 31 December 2008, purchases from the five largest suppliers of the Group accounted for an amount no more than 30% of the total annual purchase of the Group.

To the knowledge of the Board, no director of the Company, their associates, or any person holding more than 5% of the issued share capital in the Company has any interests in such suppliers.

### Continuing Connected Transactions

The following table sets out the amounts of continuing connected transactions of the Group for the year ended 31 December 2008:

Transactions	Group (RMB millions)	Annual monetary cap for continuing connected transactions (RMB millions)
Portion of expenses for centralised services	250	500
Net expenses for interconnection settlement	599	N/A <sup>1</sup>
Provision of comprehensive services by China Telecommunications Corporation <sup>2</sup> and its subsidiaries (the "China Telecom Group")	1,190	1,600
Mutual leasing of properties	388	510
Provision of IT services by China Telecom Group	457	490
Provision of engineering services by China Telecom Group	7,877	8,327
Provision of community services by China Telecom Group	2,297	2,500
Provision of ancillary telecommunications services by China Telecom Group	4,536	4,850
CDMA network capacity lease fee	1,397 <sup>3</sup>	4,000

<sup>1</sup> According to the waiver letter issued to the Company by The Stock Exchange of Hong Kong Limited on 31 July 2008, the Company is not required to set an annual monetary cap for the total amount under interconnection settlement agreements.

<sup>2</sup> China Telecommunications Corporation is a controlling shareholder of the Company. Each of China Telecommunications Corporation and its subsidiaries constitutes a connected person of the Company under the Listing Rules.

<sup>3</sup> The CDMA network capacity lease fee has already deducted the capacity maintenance related costs of CDMA network payable to the Company by China Telecommunications Corporation amounted to RMB107 million.

### Centralised Services Agreement

Centralised services includes the provision of management and operational services by the Company to China Telecommunications Corporation in relation to key corporate customers, its network management centre and business support centre, and also the provision of certain premises by the China Telecommunications Corporation to the Group. In addition, centralised services also include the common use of international telecommunications facilities between both parties. The aggregate costs incurred by the Company and China Telecommunications Corporation for the provision of management and operation services will be apportioned between the Company and China Telecommunications Corporation on a pro rata basis according to the revenues generated by each party. In relation to the common use of international telecommunications facilities, the Company and China Telecommunications Corporation have agreed to apportion the costs associated with operating such assets on a pro rata basis according to the aggregate volume of the inbound international calls terminated by, and outbound international calls originating from, the Company and China Telecommunications Corporation, respectively.

On 26 December 2007 and 31 March 2008, the Company and China Telecommunications Corporation entered into Supplemental Agreements related to the Centralised Services Agreement. Pursuant to the Supplemental Agreements, in the situation where the Company uses the premises provided by China Telecommunications Corporation, the Company shall pay premises usage fees to China Telecommunications Corporation on a pro rata basis according to the actual apportioned used areas on the venues. The premises usage fees shall be determined through negotiation between the two parties based on comparable market rates. In the situation where both parties use third-party international telecommunications facilities and accept third-party services such as the costs of restoration maintenance, the annual utilisation fee shall be determined on a pro rata basis according to the actual utilisation each year. In the situation where both parties use the international telecommunications facilities of China Telecommunications Corporation, the associated costs shall be determined on a pro rata basis according to volume of the inbound and outbound voice calls to and from international regions, Hong Kong, Macau and Taiwan originating from each party divided by the aggregate volume of the inbound and outbound voice calls to and from international regions, Hong Kong, Macau and Taiwan originating from both parties. The utilisation fee shall be determined through negotiation between the two parties based on market rates.

The Centralised Services Agreement was renewed on 15 December 2008 with expiration on 31 December 2009, and may be renewed for further periods of one year upon expiration without limit in the number of renewals, unless the Company provides a notice of non-renewal in writing to the China Telecommunications Corporation three months prior to the end of the relevant term.

### Comprehensive Services Framework Agreement

The Comprehensive Services Framework Agreement was signed in relation to the integrated services provided by China Telecommunications Corporation to the Company. Such integrated services include procurement of telecommunications equipments such as optic fibre, network design, software upgrade, system integration, the manufacture of calling cards and so on. Prices under such agreement shall be determined in accordance with the following: (1) government-prescribed prices; (2) in the absence of government-prescribed prices, the government-guided prices shall apply; (3) in the absence of both government-prescribed prices and government-guided prices, the market prices shall apply, that is, the prices at which the same types of services are provided by independent third party in the ordinary course of business; (4) if none of the above prices is applicable, the prices shall be determined through negotiation between the parties based on reasonable costs plus reasonable profit, where "reasonable costs" shall mean the costs determined by the parties after negotiations.

The Comprehensive Services Framework Agreement expired on 31 December 2008. In order to simplify the management of connected transactions after the acquisition of the CDMA business, both parties decided not to renew this agreement after friendly negotiation between the Company and China Telecommunications Corporation. The various types of cross-provincial transactions set out under the Comprehensive Services Framework Agreement have been classified into other existing connected transactions based on the nature of such transactions.

### Interconnection Settlement Agreement

Pursuant to the Interconnection Settlement Agreement, the telephone operator terminating a telephone call made to its local access network shall be entitled to receive from the operator from which the telephone call originated, a fee of RMB0.06 per minute as currently prescribed by the Ministry of Industry and Information Technology.



## Report of the Directors

The Company and China Telecommunications Corporation have signed a supplementary agreement on interconnection settlement on 27 July 2008. The supplementary agreement prescribed that the Company, when originating a telephone call, shall pay RMB0.06 per minute to China Telecommunications Corporation. At the same time, the agreed settlement also prescribed that Tianjin city, Hebei province, Heilongjiang province, Jilin province, Liaoning province, Shanxi province, Henan province, Shandong province, Inner Mongolia Autonomous Region and Tibet Autonomous Region be covered as settlement regions.

The Agreement was renewed on 31 December 2008 for another two years with expiration on 31 December 2010 and will be automatically renewed for a period of three years upon expiration without limit in the number of renewals, unless the Company provides notice of non-renewal in writing to the China Telecommunications Corporation three months prior to the end of the relevant term.

### Property Leasing Framework Agreement

The Property Leasing Framework Agreement was signed between the Company and China Telecommunications Corporation and/or its associates in relation to the lease of property between the two parties.

The rental charges rents under the Property Leasing Framework Agreement were determined according to market rates, with reference to the fees standards of the local price authority and the specific needs of both parties at the time of property leasing. The property rents are subject to review every three years.

The Property Leasing Framework Agreement was renewed on 15 December 2008 with expiration on 31 December 2009 and may be renewed for further periods of one year upon expiration without limit in the number of renewals, unless the Company provides notice of non-renewal in writing to the China Telecommunications Corporation three months prior to the end of the relevant term.

### IT Services Framework Agreement

The IT Services Framework Agreement was signed in respect to the information technology services provided by China Telecommunications Corporation and/or its associates to the Company. Such services include office automation and software testing.

China Telecommunications Corporation and/or its associates is entitled to participate in the bidding for the right to provide services under the agreement. The charges payable for such services shall be determined by reference to market rates obtained through the tender process. If China Telecommunications Corporation and/or its associates offer terms and conditions that are at least the same as those offered by an independent third-party provider, the Group may give priority to using the services provided by China Telecommunications Corporation and/or its associates.

The Company and China Telecommunications Corporation signed a supplementary agreement relating to the IT Services Framework Agreement on 15 December 2008 to amend certain terms of the Framework Agreement to enable the provisions of, among others, cross-provincial information technology services by the Group to China Telecommunications and/or its associates and vice versa.

The IT Services Framework Agreement was renewed on 15 December 2008 with expiration on 31 December 2009 and may be renewed for further periods of one year upon expiration without limit in the number of renewals, unless the Company provides notice of non-renewal in writing to the China Telecommunications Corporation three months prior to the expiry of the relevant term.

### Supplies Procurement Services Framework Agreement

Pursuant to the Supplies Procurement Services Framework Agreement, the China Telecommunications Corporation and/or its associates has agreed to provide comprehensive procurement services, including management of tenders, verification of technical specifications and installation services. The maximum commission for such procurement services shall be calculated based on the following: (1) not more than 1% of the contract value for procurement of imported telecommunications equipment; or (2) not more than 3% of the contract value for the procurement of domestic telecommunications equipment and other domestic non-telecommunications materials.

The Company and China Telecommunications Corporation signed a supplementary agreement relating to the Supplies Procurement Services Framework Agreement on 15 December 2008 to amend certain terms of the Agreement to enable provision of cross-provincial comprehensive procurement services by the Group to China Telecommunications Corporation and/or its associates and vice versa. At the same time, such supplies procurement services can extend to integrated supplies procurement services, the sale of proprietary telecommunication equipment, resale of third party equipment, management of tender, review of technical specification, storage, transport and installation services.

The Supplies Procurement Services Framework Agreement was renewed on 15 December 2008 with expiration on 31 December 2009 and may be renewed for further periods of one year upon expiration without limit in the number of renewals, unless the Company provides notice of non-renewal in writing to the China Telecommunications Corporation three months prior to the expiry of the relevant term.

### Engineering Framework Agreement

The Engineering Framework Agreement sets out the terms in respect of the supervision and management of services relating to construction, design, equipment installation and testing and/or services as the main contractors for the construction and supervision of engineering projects, provided to the Company through bids made by China Telecommunications Corporation and/or its associates. The charges payable for such engineering services shall be determined by reference to the market rates. The charges payable for the design or supervision of engineering projects with a value over RMB500,000, or construction of engineering projects with a value over RMB2 million shall be determined by referring to the tender price.

The Company and China Telecommunications Corporation signed a supplementary agreement relating to the Engineering Framework Agreement on 27 July 2008 to amend the terms of the Agreement to expand the scope of services provided to the Group by China Telecommunications Corporation and/or its associates including cross-provincial level engineering construction and design services.

The Engineering Framework Agreement was renewed on 31 December 2008 with expiration on 31 December 2009 and may be renewed for further periods of three years upon expiration without limit in the number of renewals, unless the Company provides notice of non-renewal in writing to the China Telecommunications Corporation three months prior to the expiry of the relevant term.

### Community Services Framework Agreement

The Community Services Framework Agreement was signed in respect to the services relating to culture, education, property management, vehicle service, health and medical care, hotel and conference service, community and sanitary service provided by the China Telecommunications Corporation and/or its associates to the Company. The pricing terms for such services are the same as those set out in the Comprehensive Services Framework Agreement.

The Company and China Telecommunications Corporation signed a supplementary agreement of the Community Services Framework Agreement on 15 December 2008 to amend a number of provisions, enabling China Telecommunications Corporation and/or its associates to provide the cross-provincial community services to the Company.

The Community Services Framework Agreement was renewed on 15 December 2008 with expiration on 31 December 2009 and may be renewed for further periods of three years upon expiration without limit in the number of renewals, unless either party provides notice of non-renewal in writing to the other party three months prior to the expiry of the relevant term.

### Ancillary Telecommunications Services Framework Agreement

The Ancillary Telecommunications Services Framework Agreement was signed in respect to the terms and conditions of certain repair and maintenance services, including repair of telecommunications equipment, maintenance of fire equipment and telephone booths, as well as other customer services that are provided by the China Telecommunications Corporation and/or its associates to the Company. The pricing terms for ancillary telecommunications services in the Ancillary Telecommunications Services Framework Agreement are the same as those set out in the Comprehensive Services Framework Agreement.

## Report of the Directors

The Company and China Telecommunications Corporation signed a supplementary agreement relating to the Ancillary Telecommunications Services Framework Agreement on 27 July 2008 to amend the terms of the Agreement, enabling China Telecommunications Corporation and/or its associates to provide ancillary telecommunications services including cross-provincial services to the Company.

The Ancillary Telecommunications Services Framework Agreement was renewed on 31 December 2008 with expiration on 31 December 2009 and may be renewed for further periods of three years upon expiration without limit in the number of renewals, unless either party provides notice of non-renewal in writing to the other party three months prior to the expiry of the relevant term.

### 48 CDMA Network Capacity Lease Agreement

Pursuant to the "CDMA Network Capacity Lease Agreement" signed between the Company and China Telecommunications Corporation on 27 July 2008, China Telecommunications Corporation agreed to lease its CDMA network capacity under the CDMA network to the Company and the Company shall have the exclusive right to use and operate the CDMA network to provide CDMA services in its service areas. The lease fee is based on 28% of the audited CDMA service revenue (which is calculated by the total revenue from the CDMA services operations minus any upfront non-refundable revenue arising out of the CDMA operations and any revenue from sale of telecommunication products in connection with the CDMA operations) per year. For the year ended 31 December 2008 and for the year ending 2009, there is no minimal annual lease fee. For the year ending 31 December 2010, the minimum annual lease fee shall be 90% of the total amount of the lease fee paid by the Company to China Telecommunications Corporation in the year ending 31 December 2009. The cost of network construction shall be borne by China Telecommunications Corporation, while the maintenance-related costs shall be shared as agreed between the two parties.

Pursuant to the CDMA Network Capacity Lease Agreement, China Telecommunications Corporation has granted to the Company an option to purchase the CDMA network. The option may be exercised, at the discretion of the Company, at any time during the term of the lease or within one year after the expiry of the lease. No premium has been paid or will be payable by the Company for the grant of the option.

The CDMA Network Capacity Lease Agreement is effective till 31 December 2010 and may be renewed for further periods as agreed by both parties on similar terms.

### Strategic Agreement and its Supplemental Agreement

Independent shareholders of the Company approved in the Extraordinary General Meeting the signing of a Strategic Agreement between the Company and China Communications Services Corporation Limited ("China Communications Services") on 30 August 2006 and the signing of a Supplemental Agreement ("Strategic Agreement and its Supplemental Agreement") on 15 June 2007.

Pursuant to the Strategic Agreement and its Supplemental Agreement, the Company agreed that, in the period between 1 January 2007 and 31 December 2009, if service terms related to the design, implementation and supervision of the communications engineering provided by China Communications Services are basically the same as those of other service providers, the subsidiaries of the Company (and their successors) in the service area of China Communication Services shall annually receive such services from the wholly-owned subsidiaries of China Communications Services with total value no less than 10.6% of total annual capital expenditure of the related subsidiaries of the Company in that year. Meanwhile, pursuant to the Strategic Agreement and its Supplemental Agreement, the Company pledged that, in the period between 1 January 2007 and 31 December 2009, if the terms related to certain maintenance management services provided by China Communications Services are basically the same as those of other service providers, the subsidiaries of the Company (and their successors) in the service area of China Communication Services shall annually receive such services from the wholly-owned subsidiaries of China Communications Services with total value no less than RMB1,780 million.

The business areas of the strategic alliance between the two parties governed by the terms and conditions in the Strategic Agreement and its Supplemental Agreement include: design, implementation and supervision of the communications engineering, maintenance management service, contents application service, sales channel service, usage of telecommunications and other new businesses arising from time to time which are appropriate for the collaboration between the two parties. China Communications Services pledges its support to the strategic transformation of the Company from a traditional basic telecommunications operator to an integrated information service provider, its active support to the Company's business development, and its active use of the

Company's products and services in its own business. Such services shall comply with the related standards of China or the standards agreed by both parties, and shall be on terms no less favourable than those available to any third parties to which the same or similar services are provided by either party. Without breaching the requirements governed by PRC laws, in respect of the same services, where the terms and conditions of services provided by either party to the Strategic Agreement and its Supplemental Agreement are the same as those provided by an independent third party, the party under the Strategic Agreement and its Supplemental Agreement shall have the priority to be appointed as the service provider by the other party.

Pursuant to the Strategic Agreement and its Supplemental Agreement, with the term covered from 1 January 2007 to 31 December 2009, both parties may negotiate the renewal of the Strategic Agreement upon its expiration, and the renewal is subject to the requirements of Chapter 14A of the Listing Rules (including disclosure and independent shareholders' approval requirements).

Neither the Strategic Agreement nor Supplemental Agreement sets out any annual caps for the transactions thereunder as China Telecommunications Corporation, the holding company of China Communications Services, has signed certain framework agreements for continuing connected transactions with the Company and the transactions contemplated under the Strategic Agreement and Supplemental Agreement are covered by these framework agreements. These framework agreements are already subject to annual caps and the proposed annual caps for the transactions under the Strategic Agreement (as amended by the Supplemental Agreement) are subsumed under the annual caps of those framework agreements between the Company and China Telecommunications Corporation (including the Engineering Framework Agreement, the Ancillary Telecommunications Services Framework Agreement and the Community Services Framework Agreement).

The Company confirms that it has complied with the disclosure requirements in accordance with Chapter 14A of the Listing Rules in respect of the above connected transactions.

The Independent Non-Executive directors of the Company have confirmed that all continuing connected transactions for the year ended 31 December 2008 to which the Group was a party:

1. had been entered into, and the agreements governing those transactions were entered into, by the Group in the ordinary and usual course of business;
2. had been entered into either:
  - (i) on normal commercial terms; or
  - (ii) if there are not sufficient comparable transactions to judge whether they are on normal commercial terms, on terms no less favourable to the Company than those available to or (if applicable) from independent third parties; and
3. had been entered into in accordance with the relevant terms that are fair and reasonable and in the overall interests of the shareholders of the Company as a whole.

The Independent Non-Executive directors have further confirmed that:

The values of continuing connected transactions entered into between the Group and its connected persons which are subject to annual caps have not exceeded their respective annual caps.

The auditors of the Group have reviewed the continuing connected transactions of the Group and have confirmed to the Board that the transactions:

1. have received the approval of the Board;
2. have been entered into in accordance with the pricing policies as stated in the relevant agreements; and
3. have been entered into in accordance with the terms of the agreements governing such transactions; and the values of continuing connected transactions entered into between the Group and its connected persons which are subject to annual caps have not exceeded their respective annual caps.

## Report of the Directors

### Compliance with Code on Corporate Governance Practices

Please refer to the “Corporate Governance Report” set out in page 56 of this 2008 annual report of the Company for details of our compliance with the Code on Corporate Governance Practices.

### Material Legal Proceedings

As at 31 December 2008, the Company was not involved in any material litigation or arbitration, and as far as the Company is aware, no material litigation or claims were pending or threatened or made against the Company.

### Auditors

KPMG and KPMG Huazhen were appointed as the international and domestic auditors of the Company for the year ended 31 December 2008. KPMG has audited the accompanying financial statements, which have been prepared in accordance with International Financial Reporting Standards. The Company has engaged KPMG and KPMG Huazhen since the date of its listing. A resolution for the reappointment of KPMG and KPMG Huazhen as the international and domestic auditors of the Company for the year ending 31 December 2009 will be proposed at the Annual General Meeting of the Company to be held on 26 May 2009.

By Order of the Board

**Wang Xiaochu**

*Chairman and Chief Executive Officer*

Beijing, PRC

24 March 2009