China Unicom Limited
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中國聯通股份有限公司
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China Unicom Limited

Annual Report 2001

China Unicom
Linking China to the World

Annual Report 2001

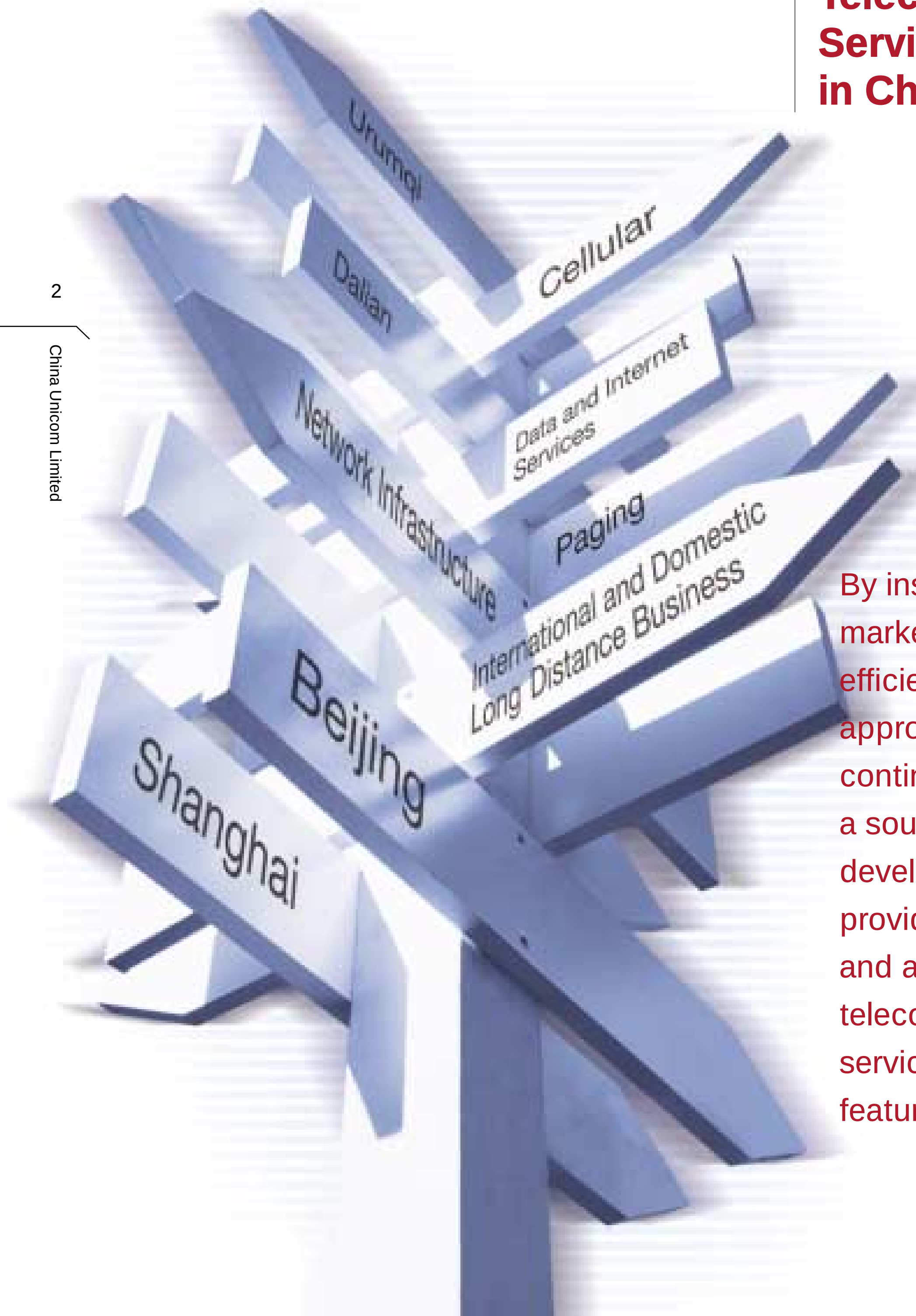
CHINA UNICOM LIMITED

Incorporated in Hong Kong with limited liability under the Companies Ordinance

Contents

All Rounded Services

The only Integrated Telecommunications Services Provider in China



By insisting on a market-oriented and efficiency-focused approach, the Company continues to maintain a sound and rapid development and provides comprehensive and accessible telecommunications services with unique features to the society.

China Unicom Limited (the "Company") was incorporated in Hong Kong in February 2000. All of the assets and businesses of China United Telecommunications Corporation ("Unicom Group") in its GSM cellular business in the twelve provinces and directly administered municipalities of Beijing, Shanghai, Tianjing, Guangdong, jiansu, Zhejiang, Fujian, Liaoning, Shandong, Anhui, Hebei and Hubei (the "Service Areas") and its nationwide long distance telephony network, data network and internet together with its equity interests in Guoxin Paging Corporation Limited which owned the radio paging business, were injected into the Company. Its shares was listed on the New York Stock Exchange, Inc. and The Stock Exchange of Hong Kong Limited on 21 June, 2000 and 22 June, 2000 respectively. On 22 November 2001, the Company's wholly owned subsidiary, China Unicom Corporation Limited had entered into a lease with Unicom Group's wholly owned subsidiary, Unicom New Horizon Mobile Telecommunications Company Limited in respect of leasing capacity of CDMA network in the service areas and the CDMA service had been launched as from 3 January 2002.

China Unicom Corporation Limited, a wholly-owned subsidiary of the Company, operates the aforesaid GSM and CDMA cellular businesses in the services areas and directly administered municipalities, nationwide radio paging business, international and domestic long distance telephone business, data communications including internet and IP telephony business and other related value-added services.

By insisting on a market-oriented and efficiency-focused approach, standardizing the planning of its network construction, rationalizing the use of its network resources and focusing on the utilization of social dynamics, the Company continues to maintain a sound and rapid development and provides comprehensive and accessible telecommunications services with unique features to the society. With leasing CDMA capacity from Unicom Group, the overall strength of the Company has been continuously strengthened.

With respect to cellular communications services, the Company is one of the two largest cellular communications operators in China. At the end of year 2001, the number of our GSM subscribers has reached 27.033 million. We have executed international roaming agreements with over 147 operators in over 56 countries and regions. In response to the needs of the society, we are also actively developing various new services, such as prepaid services ("ru yi tong") and WAP.

With respect to long distance and data services, as of the end of year 2001, the long distance telephone network of the Company covered 304 major cities. We have provided IP telephony services in 320 cities. The broadband data network providing leased lines, Frame Relay ("FR"), Asynchronous Transfer Mode ("ATM"), Virtual Private Network ("VPN") and Internet services, has been expanded to 303 cities.

With respect to radio paging service, the Company is the largest paging service provider in China and possesses a radio paging network with the largest subscribers base in the world. As of the end of year 2001, the number of our paging subscribers has reached 32.907 million.

The Company has completed the construction of the second largest broadband optical fibre transmission network in China, which serves as the common platform supporting the various operating networks of cellular communications, domestic and international long distance, data, internet and paging services. As of the end of year 2001, the optical fibre transmission network reached 333,000km with the long distance optical fibre backbone network reaching 78,000km.

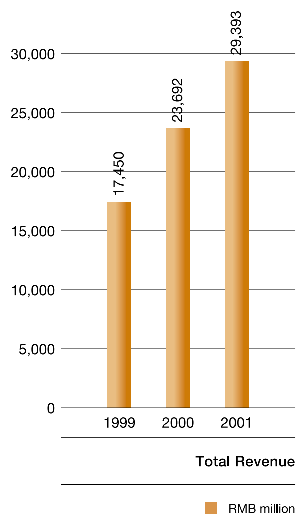
Since its incorporation, the Company is actively promoting its image as an integrated telecommunications services provider. By fully utilizing our ability to provide various kinds of telecommunications services, the asymmetrical tariff regulation policy of the government and the advantage of having a nationwide sales and distribution network, we have provided a "one-stop-shop" services which, together with our approach of combining direct and distribution sales, provides differentiated services in accordance with the needs of different groups of customers.

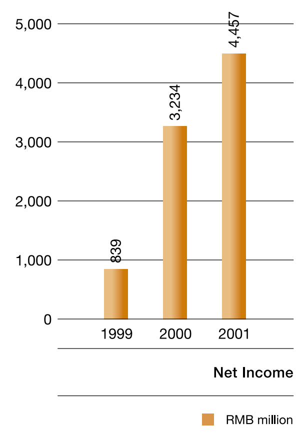
Unicom Group is the substantial shareholder of the Company. As at 31 December 2001, Unicom Group indirectly held 77.47% of the shares in the Company through its wholly-owned subsidiary, China Unicom (BVI) Limited. The remaining 22.53% of the shares were held by public shareholders.

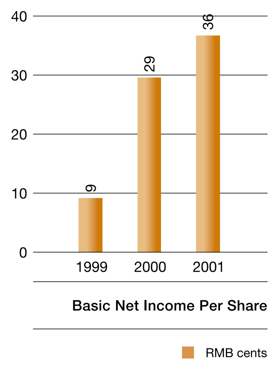
Financial Highlights

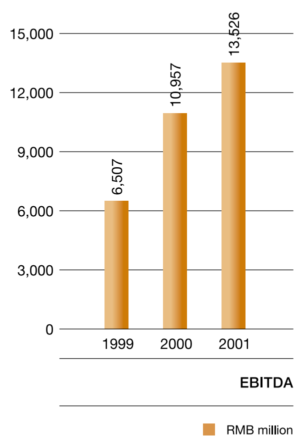
Consolidated Results of Operations

	2001 RMB million	2000 RMB million
Total Revenue	29,393	23,692
Net Income	4,457	3,234
Basic Net Income Per Share	RMB36 cents	RMB29 cents
Diluted Net Income Per Share	RMB36 cents	RMB29 cents
EBITDA	13,526	10,957









Corporate Information

DIRECTORS AND SENIOR MANAGEMENT

Yang Xian Zu
Executive Director, Chairman and Chief Executive Officer

Wang Jianzhou
Executive Director and President

Shi Cuiming
Executive Director and Executive Vice President

Li Zhengmao
Executive Director and Vice President

Tan Xinghui
Executive Director and Vice President

Ge Lei
Non-Executive Director

Craig O. McCaw
Non-Executive Director

Lee Hon Chiu
Independent Non-Executive Director

Wu Jing Lian
Independent Non-Executive Director

C. James Judson
Alternate Director to Craig O. McCaw

Liu Yunjie
Vice President

COMPANY SECRETARY

Ngai Wai Fung

AUDITORS

Arthur Andersen & Co

LEGAL ADVISORS TO THE COMPANY

Freshfields Bruckhaus Deringer
Sullivan & Cromwell

REGISTERED OFFICE

75th Floor, The Center
99 Queen's Road Central
Hong Kong

SUBSIDIARY

China Unicom Corporation Limited
12th Floor, Office Tower 1
Henderson Centre
18 Jianguomennei Avenue
Dongcheng District
Beijing 100005, PRC
Tel: 86-10-65183406

SHARE REGISTRAR

Hong Kong Registrars Limited
2/F., Vicwood Plaza
199 Des Voeux Road Central
Hong Kong

AMERICAN DEPOSITARY RECEIPTS DEPOSITARY

The Bank of New York
101 Barclay Street
New York, NY 10286
USA

PUBLICATIONS

Under the United States securities law, the Company is required to file an annual report on Form 20-F with the United States Securities and Exchange Commission before 30 June, 2002. Copies of the annual report as well as the Form 20-F, once filed, will be available at:

Hong Kong:
China Unicom Limited
75th Floor, The Center
99 Queen's Road Central
Hong Kong

United States:
The Bank of New York
101 Barclay Street
New York, NY 10286
USA

COMPANY WEBSITE

www.chinaunicom.com.hk

Chairman's Statement

The entrance into the WTO will further accelerate the pace of the country's economic growth and generate increasing demand for telecommunications services. It also provides the Company with new opportunities to compete in the international telecommunications market, setting the stage for the realization of the Company's international strategies.

With the Objective to Become a World-Class Integrated Telecommunications Operator

Supported by the rapidly developing Chinese economy, deepening reforms in the telecommunications industry and the standardization and restructuring of the regulatory environment in China, China Unicom's key businesses enjoyed significant growth as evidenced by the remarkable operating results.

Supported by the rapidly developing Chinese economy, deepening reforms in the telecommunications industry and the standardization and restructuring of the regulatory environment in China, China Unicom's key businesses enjoyed significant growth as evidenced by the remarkable operating results achieved in 2001. Both the integrated capabilities and core competitiveness were significantly enhanced with the proactive and consistent application of our strategy – "Establishing New Mechanisms; Constructing New Networks; Adopting High Technologies; Realizing High Growth and Developing Integrated Businesses". Initiatives were undertaken to further reform and enhance our internal management. While China Unicom's cellular business continued its robust growth, international and domestic long distance, data and Internet businesses have also demonstrated an accelerating growth. The market share attributable to various business segments continued to expand, reflecting the uniqueness and advantage of China Unicom that is positioned as the only integrated telecommunications service operator in Mainland China.

Operating results were remarkable in 2001. Total operating revenue for the year was RMB 29.39 billion, representing an increase of 24.1% from the previous year. Of which, the service revenue was RMB 28.16 billion, a 29.3% increase compared with the one in 2000. In the total revenue generated, revenue from the cellular business reached RMB 21.33 billion, up 65.5% from that in 2000. The revenue share from the cellular business increased substantially, up to 72.5% in 2001 as compared with 54.4% in 2000. In addition, the revenue share from the long distance, data and Internet businesses also increased to 11.3% in 2001 as compared with 4.6% in 2000, with the total amount of RMB 3.31 billion, rose 201.8% from the previous year. However, the revenue share of the paging business declined from 41.0% in 2000 to 16.2% in 2001. The EBITDA rose 23.4% to RMB13.53 billion and the margin of EBITDA reached 46.0% in 2001. The Company's net profit in 2001 was RMB 4.46 billion, a 37.8% increase as compared with the one in 2000. Earnings per share rose 24.1% from RMB 0.29 in 2000 to RMB 0.36 in 2001.

China Unicom's key businesses sustained a rapid growth in 2001. Subscribers of GSM cellular continued to grow rapidly to 27.033 million by 31 December 2001, 111.7% higher than the one in 2000. The market share in terms of GSM cellular subscribers in China Unicom's service areas increased from 22.7% in 2000 to 28.5% in 2001, and the market share in terms of net subscriber additions reached 37.2% in 2001. The total usage volume in GSM cellular business reached 38.32 billion minutes in 2001, representing a year-on-year growth rate of 117.4%. Based on the market demand, the Company continued to increase its GSM network capacity and improve its service qualities through constructing new network, adjusting voice traffic and optimizing network. During 2001, our parent company, China United Telecommunications Corporation ("Unicom Group") successfully completed and launched the first phase of CDMA network. In January 2002, China Unicom commenced the lease of CDMA network capacity in the Company's service areas from its parent company. Meanwhile, it adopted a differentiated sale/marketing strategy that is designed to target different customer segments to further increase the Company's market penetration.

China Unicom's long distance, data and Internet networks have reached nationwide coverage. Its transmission capabilities have also been greatly enhanced. The outgoing long distance calls through PSTN and IP telephony services reached 6.41 billion minutes, up 5.9 times from the previous year. Its market share increased from 1.3% in 2000 to 7.7% in 2001. The total international incoming calls were 1.23 billion minutes, up 3.4 times from the previous year.

Accelerating pace of cellular substitution has led to a significant decline of our paging subscriber base. At the end of 2001, the number of paging subscribers of China Unicom decreased from 44.52 million in 2000 to 32.907 million in 2001. Nevertheless, China Unicom still maintained its dominant position in the paging market in Mainland China.

China Unicom's optical fiber transmission network has achieved a rapid expansion. As of 31 December 2001, the Company's network has reached a total length of 333,000 km, representing an increase of 113.5% from the previous year. Of which, the optical fiber backbone transmission network has a total length of 78,000 km, up 39.3% from 2000. China Unicom's optical fiber transmission network provides a solid foundation for the future rapid growth of our businesses.

With the aim of becoming a world-class integrated telecommunications operator, the Company has launched various reform measures to constantly increase our shareholders' value. The organization structure at our provincial branches has been improved, becoming more market-oriented and suitable to meet the requirements for business development. We have established and implemented performance-based evaluation systems with overall appraisal measures based on operating efficiency and profitability, as well as related incentive programs to improve the Company's incentive and restraint mechanisms. Significant efforts were made to attract talents to the Company by conducting open recruitment in both China and abroad in order to increase our competitiveness. Productivity was improved as a result of workforce optimization and streamlining. China Unicom is committed to establish a management team of high caliber. Great

With the aim of becoming a world-class integrated telecommunications operator, the Company has launched various reform measures to constantly increase our shareholders' value.

We will also strengthen the establishment of corporate culture, talents recruitment and staff training in order to build a workforce with high caliber.

emphasis was placed on staff training even at the Company's senior management level. We also implemented international quality assurance system to standardize internal management. We launched a "Servicing Excellence, Customer Satisfaction" campaign that elevated the importance of customer service across the Company. We made further headway in operating profitability by improving financial management, centralizing fund allocations and tightening cost controls. On 1 June 2001, the Company became a constituent stock to Hong Kong Heng Seng Index, highlighting the new achievement of China Unicom and its importance in international capital markets.

China's official accession to the World Trade Organization last December presents unprecedented development opportunities as well as new challenges. The competition between China Unicom and foreign companies on talents and core competitiveness will become the focus of future development after foreign companies entering telecommunications markets in China. The entrance into the WTO will further accelerate the pace of the country's economic growth and generate increasing demand for telecommunications services. It also provides the Company with new opportunities to compete in the international telecommunications market, setting the stage for the realization of the Company's international strategies. Facing the new market environment, we will adopt an active approach to enhance our management standards and core competency, with an aim to build the Company into a world-class integrated telecommunications service operator.

To accelerate cellular business in 2002, we will adopt new technology, identify new business and apply a differentiated business strategy that is based on different market needs for cellular services. The differentiated strategy will ensure us with a coordinating growth between CDMA and GSM networks. It will also ensure us with a continuous high growth rate in terms of cellular subscriber numbers as well as our operating efficiency. We will continue our efforts to ensure the success of CDMA business development by enhancing network coverage, technology upgrade, sales and marketing and customer services. While operating CDMA network, the Company will also focus on optimizing its GSM network, improving coverage quality, increasing network utilization, upgrading sale and marketing and improving service standards.

In order to fully leverage the advantage of having a uniform network platform for various businesses, we will ensure the unity, completeness and technology advancement of our optical fiber transmission network. This can be achieved by optimizing the network structure and facilities, strengthening the network maintenance and management, so as to provide an underlying network platform for the Company's various businesses. We will devote great efforts to develop data and long distance businesses with an emphasis on Internet and e-commerce development. It is our objective to significantly expand our market share, customer base, revenue and profit from the long distance, the data and the Internet businesses, making it an important driver for the further growth of the Company's revenue.

Based on the purpose to sustain and expand the traditional paging market, we will actively develop new services in the paging business. Measures such as adjusting the network structure, streamlining staff and restructuring the operational system, as well as stringent control of capital expenditure will be implemented to address the concern of slowdown in the paging business. We will also optimize the network and staff resources to stabilize the operating efficiency in the paging business.

With the objective to become a world-class integrated telecommmunications operator and to maximize our shareholders' value, we will establish a more effective corporate governance structure and deploy human resources. This will allow us to best address the need of business growth and provide

We will take proactive steps to deepen and broaden the overall cooperation with foreign companies so as to strengthen our market competitiveness.

more market-oriented services. We will focus our efforts on improving the return on investments and the return on equity. We will actively implement the comprehensive budget management and stringent control over the Company's operating expenses. Mechanisms will be established to optimize the Company's organizational structure and facilities, establish and improve the internal control system and incentive mechanisms that meet international standards to improve the Company's operating efficiency. We will promote the application of information technology throughout the Company, and enhance the management expertise. We will also strengthen the establishment of corporate culture, talents recruitment and staff training in order to build a workforce with high caliber.

China Unicom is considering the acquisition of GSM cellular businesses and other assets in the remaining 18 provinces in Mainland China from its parent company at an appropriate time. This will assist the Company to set up a solid foundation for its future business development.

We will take proactive steps to deepen and broaden the overall cooperation with foreign companies in ways that are mutually beneficial. We believe it will strengthen our market competitiveness in the world.

Looking ahead, we have full confidence in the future prospects of the Company. Given the Company's significant growth potential, the Board of Directors believes that the Company is well positioned to create new value for our shareholders.

On behalf of the Board of Directors, I would like to express my sincere thanks for the interests and supports from both shareholders and the society at large. I would also like to express my thanks to both the management team and employees of the Company for their consistent hard work.

Yang Xian Zu
Chairman

Hong Kong
27 March 2002

Biographical Details of Directors and Senior Management

Tan Xinghui / Executive Director
Liu Yunjie / Senior management
Wang Jianzhou / Executive Director
Yang Xian Zu / Executive Director
Shi Cuiming / Executive Director
Li Zhengmao / Executive Director
Ge Lei / Non-Executive Director
Wu Jing Lian / Independent Non-Executive Director
Lee Hon Chiu / Independent Non-Executive Director

Yang Xian Zu / Executive Director

Aged 62, was appointed in April 2000 as an Executive Director and subsequently as the Chairman of the Board of Directors and Chief Executive Officer of the Company responsible for the overall management. Mr. Yang, a senior engineer, graduated in 1965 from the Department of Telephone and Telegraph at the Wuhan College of Posts and Telecommunications. From 1983 to 1990, Mr. Yang served as Deputy Director General of the Posts and Telecommunications Administration of Hubei Province and as Director General of the Posts and Telecommunications Administration of Henan Province. From 1990 to early 1999, Mr. Yang served as Vice Minister of the Ministry of Posts and Telecommunications and later as Vice Minister of the Ministry of Information Industry. In these capacities, Mr. Yang was involved in the management of China United Telecommunications Corporation from a strategic level. Since 1999, Mr. Yang has served as Chairman of the Board of Directors and President of China United Telecommunications Corporation and was re-appointed as the Chairman in February 2001. With thirty-six years of experience in the telecommunications industry in China, Mr. Yang has extensive knowledge and experience in telecommunications operations, technology and management.

Wang Jianzhou / Executive Director

Aged 53, was appointed in April 2000 as an Executive Director and subsequently as the President of the Company responsible for day-to-day management and operations. Mr. Wang, a senior engineer, graduated in 1985 from the Department of Management Engineering at Zhejiang University with a master's degree. From 1992 to 1996, Mr. Wang served as Deputy Director General and later Director General of the Posts and Telecommunications Bureau of Hangzhou City and as Deputy Director General of the Posts and Telecommunications of Zhejiang Province. From 1996, Mr. Wang has served as Director General of the Department of Planning and Construction of the Ministry of Posts and Telecommunications and later as Director General of the Department of General Planning of the Ministry of Information Industry. In these capacities, Mr. Wang was involved in the management of China United Telecommunications Corporation from a strategic level. Since early 1999, Mr. Wang has served as Director and Executive Vice President of China United Telecommunications Corporation and was appointed as President and re-appointed as Director in February 2001. With many years of experience in the telecommunications industry in China, Mr Wang has extensive knowledge and experience in telecommunications operations and management.

Shi Cuiming / Executive Director

Aged 62, was appointed in April 2000 as an Executive Director and subsequently as Executive Vice President of the Company. Mr. Shi assists the Chairman of the Board of Directors and the President in managing day-to-day operations and also is responsible for finance. Mr. Shi, a senior economist, graduated in 1963 from the Department of Management Engineering at the Beijing University of Posts and Telecommunications. From 1981 to 1987, Mr. Shi served as Deputy Director of Postal Economic Research of Ministry of Posts and Telecommunications and as Deputy Director General of the Bureau of finance of the Ministry of Posts and Telecommunications. From 1987 to 1997, Mr. Shi served as Director General of the Bureau of Finance, Director General of the Department of Operations and Finance and Director General of the Department of Finance of the Ministry of Posts and Telecommunications. From 1997 to early 1999, Mr. Shi served as Chairman of the Board of Directors of China Telecom (Hong Kong) Group Limited and Chairman of the Board of Director of China Telecom (Hong Kong) Limited. Since early 1999, Mr. Shi has served as Director and Vice President of China United Telecommunications Corporation and was reappointed as Director of the Company in September 2000. With thirty-eight years of experience in the telecommunications industry in China, Mr. Shi has extensive knowledge and experience in telecommunications operations and management.

Li Zhengmao / Executive Director

Aged 39, was appointed in April 2000 as an Executive Director and subsequently as Vice President and Company Secretary of the Company. Mr. Li assists the President in managing technology and is also responsible for investor relations. Mr. Li graduated in 1988 from the Department of Radio Technology at Southeast University with a Ph.D in Electronic Engineering. He was a professor at the University of Electronic Science and Technology of China from 1992 to 1994. Since 1994, Mr. Li has served in various senior positions within China United Telecommunications Corporation, including Deputy Director of the Technology Department and Director of the Wireless Communications Department and later Director of the Technology Department and Deputy Chief Engineer of China United Telecommunications Corporation. Mr. Li has considerable experience in technology management in the telecommunications industry.

Tan Xinghui / Executive Director

Aged 40, was appointed in September 2000 as an Executive Director and Vice President of the Company. Mr. Tan assists the President in administration and maintaining public relations with media. Mr. Tan, a senior engineer,graduated from the Department of Microwave Communications at the Beijing University of Posts and Telecommunications in 1983. From 1987 to early 1996, Mr. Tan served as an engineer in the Department of Transportation Project of China International Engineering Consulting Corporation and Deputy General of the Bureau of Transportation and Energy of the State Planning Committee. Since early 1996, he has served as Deputy Director and later Director of the Planning and Marketing Department and General Manager of the Department of Operation Maintenance and Interconnection of China United Telecommunications Corporation. Mr. Tan has considerable experience in planning and management in the telecommunications industry.

Ge Lei / Non-Executive Director

Aged 61, was appointed in April 2000 as a Non-Executive Director of the Company. Mr. Ge is a senior engineer and graduated from the Telecommunications Engineering Department at the Beijing University of Posts and Telecommunications in 1962. Since 1974, he has held numerous positions including Deputy Director of the Equipment Maintenance Bureau, Chairman of the Department of Management Engineering of the Beijing Posts and Telecommunications University, and Deputy Director of the Planning Office, Director of Planning Department, Director of the Education Department, and Director of the Telecommunications Administrative Department of the Ministry of Posts and Telecommunications. Since August 1998, Mr. Ge was the Chairman and General Manager of Guoxin Paging. In February 2000, he was appointed as a director of China United Telecommunications Corporation. With thirty-nine years of experience in the telecommunications industry in China, Mr. Ge has extensive expertise and management experience in the telecommunications industry.

Craig O. McCaw / Non-Executive Director

Aged 52, was appointed in May 2000 as a Non-Executive Director of the Company. Mr. McCaw is Chairman and Chief Executive Officer of Eagle River Investment LLC, a private company that makes strategic investments in telecommunications ventures, and a director of Nextel Communications, Inc., as well as the Chairman of its executive committee. He is also a director of XO Communications, Inc., Chairman of the boards of Teledesic Corporation and ICO-Teledesic Global Limited. Mr. McCaw established McCaw Cellular Communications,Inc.and XO Communications, Inc. Mr. McCaw has actively participated in both cellular and cable television trade associations over the years and is a member by Presidential appointment of the United States National Security Telecommunications Advisory Committee. Mr. McCaw graduated from Stanford University in 1973.

Lee Hon Chiu / Independent Non-Executive Director

Aged 73, was appointed in April 2000 as an Independent Non-Executive Director of the Company. Mr. Lee serves as member of the Process Review Panel for the Securities and Futures Commission and Chairman of the Standing Committee on Directorate/Judicial Salaries and Conditions of Service appointed by the Hong Kong Government. Mr. Lee is also Chairman of the Council of the Chinese University of Hong Kong and a member of the National Committee of the Chinese People's Political Consultative Conference. Mr. Lee is the Chairman of Hysan Development Company Limited, Deputy Chairman of the Garden Hotel, Guangzhou, a non-executive director of Cathay Pacific Airways Limited, Hang Seng Bank Limited, The Hong Kong & China Gas Company Limited and a number of other Hong Kong companies. Mr. Lee obtained a Bachelor of Science degree in Electrical Engineering at Massachusetts Institute of Technology in 1952. He later obtained a Master of Science degree in Electronics at Stanford University in 1953.

Wu Jing Lian / Independent Non-Executive Director

Aged 72, was appointed in April 2000 as an Independent Non-Executive Director of the Company Mr. Wu is a senior researcher at the Development Research Center of the State Council and a professor at the Graduate School of the Chinese Academy of Social Sciences. Mr. Wu graduated from Fudan University, and was previously a Deputy Director of the Programming Office for Economic Reform of the State Council. Mr. Wu was also a visiting scholar at Yale University, a visiting professor at the Asia-Pacific Research Center of Stanford University and a visiting researcher at the Massachusetts Institute of Technology.

C. James Judson / Alternate Director

Aged 57, was appointed in March 2001 as an Alternate Director to Craig O. McCaw of the Company. Mr. Judson is the Vice President and General Counsel of Eagle River. Inc. and a

member of Eagle River Investments, LLC, a Kirkland–based venture capital fund formed by Craig O. McCaw to focus on investment opportunities in communications. Mr. Judson serves as a Director of Nextel International, Inc. and a member of the Plan Administration Committee, Mr. Judson also serves on the boards of Port Blakely Farms, LP, Garrett and Ring. Inc., The Joshua Green Corporation, and Airbiquity, Inc. Prior to joining Eagle River, Mr. Judson was a partner at Davis Wright Tremaine, a Seattle–based law firm with twelve offices worldwide. Mr. Judson attended Stanford University, B.A. cum laude 1966, and Stanford Law School, LLB. 1969 and was the Executive Editor of the Stanford Law Review.

Liu Yunjie / Senior Management

Aged 59, was appointed in May 2000 as the Vice President of the Company. Mr. Liu assists the President in managing the technology and operations relating to data communications services. Mr. Liu, a senior engineer, graduated from the Department of Applied Physics at Beijing University in 1968. From 1983 to 1995, Mr. Liu served as Deputy Director General and later Director General of the Institute of Data of the Ministry of Posts and Telecommunications and as Director General of the Bureau of Data Communications of the Ministry of Posts and Telecommunications. From 1995 to 1998, Mr. Liu served as Deputy Director General of the Directorate General of Telecommunications and as Director General of the Bureau of Data Communications of the Ministry of Posts and Telecommunications. Mr. Liu was also President of the Institute of Postal Science Research and Planning of the Ministry of Posts and Telecommunications from 1998 to 1999. Since April 1999, Mr. Liu has served as the Chief Engineer and later Vice President of China United Telecommunications Corporation. Mr. Liu has thirty years of experience in management and business operations in the telecommunications industry, with expertise in data communications technology.

The management believes that the enormous potential of China's telecommunications market and the diversified demand of its subscribers create excellent opportunities for the Company to attract more quality customers and maintain its fast growing trend in the future.

High Growth

Rapidly Rising Market Shares

I. SUMMARY

The Company is the only integrated telecommunications operator in China, engaging in a wide range of telecommunications businesses, covering cellular communication, international and domestic long distance, data, Internet and paging. Since the listing of its shares in 2000, the Company has vigorously developed its telecommunications services. Its market shares rose substantially, and its position as a leading integrated operator was further strengthened.

The Company's cellular communication business sustained its recent trend of strong growth. As of 31 December 2001, there were 27.033 million GSM subscribers, up 14.261 million or 111.7% year-on-year (the end of 2000: 12.772 million subscribers). The Company's market share in its service areas increased to 28.5% (2000: 22.7%) and its share in net addition market increased to 37.2% (2000: 32.0%). The Company devoted ample resources to expand wireless data service. In 2001, the volume of short messages transmitted reached 1.08 billion. The Company has entered into GSM international roaming agreements with 147 operators in 56 countries and regions. With effect from January, 2002, the Company leased capacity of the CDMA network from its parent company on an exclusive basis. The CDMA network was constructed by the parent company as authorized by the Chinese Government.

The Company's international and domestic long distance business grew rapidly. The number of usage duration for outgoing international and domestic long distance calls increased 5.9 times year-on-year to 6.41 billion minutes (2000: 0.93 billion minutes). Of which, the number of usage duration for outgoing PSTN long distance calls increased to 2.72 billion minutes (2000: 0.24 billion minutes), whilst the number of usage duration for outgoing IP calls increased to 3.69 billion minutes (2000: 0.69 billion minutes). The number of usage duration for incoming international long distance calls increased 3.4 times year-on-year to 1.23 billion minutes (2000: 0.28 billion minutes). The Company offers leased line services, and a total of 2350 x 2Mbps bandwidth were leased out on an accumulated basis.

Data and Internet businesses also witnessed swift expansion. The Company offers data carrier services through asynchronous transfer mode ("ATM") and frame relay ("FR"). A total of 826 x 2Mbps bandwidth were leased out on an accumulated basis. The Company also provides dedicated line and dial-up Internet access, Internet data centre ("IDC") and other e-Commerce services. Internet subscribers increased to 3.544 million (2000: 415 thousand).

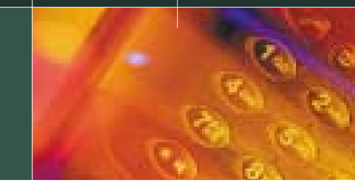
Although a substantial decrease in the number of paging subscribers was recorded for the year under review, the Company was able to maintain its dominant position in the market with a paging subscribers base of 32.907 million as of 31 December 2001.

The Company has a state-of-art broadband optical fibre transmission network with nationwide coverage. The network, together with the core ATM+IP switching network , provides a powerful platform that supports the extensive telecommunications services of the Company. As of 31 December 2001, the Company's long distance optical fibre backbone transmission network reached 78 thousand kilometers in length, covering 303 cities across the country, and the total length of its optical fibre transmission network reached 333 thousand kilometers.

The Company offers high quality and efficient customer services. Through a series of efforts from establishing the brand name as an integrated telecommunications operator, the setting up of sales and marketing teams targeting major customers and the launching of nationwide customer service hotline "1001", the Company offers differentiated and competitive services. By strengthening customer services management, quality of service and the customer satisfaction towards the Company's services were enhanced.

The Company always emphasizes on research and development of new technologies and new businesses. Latest trends in the development of telecommunications technologies are closely monitored. Cooperation with telecommunications operators within and outside the PRC has been bolstered. An integrated business platform is being actively developed while research and development are committed to the exploring of telecommunications businesses with high profitability and growth potential. In 2001, the Company established a new business development center and a wireless data services research center, which were responsible for the successful development of new businesses such as unified account service based on integrated intelligent network, consolidated virtual private network ("VPN") and wireless data service "UNI-INFO".

The management of the Company believes that the enormous potential of China's telecommunications market and the diversified demand of its subscribers create excellent opportunities for the Company to attract more quality customers and maintain its fast growing trend in the future.



Cellular

The rapid growth in GSM subscribers was mainly attributable to continuous enhancement of network quality, tailor-made services for different segments of customers, cancellation of connection fee and the continuous fall of handset prices.

II. BUSINESS REVIEW

1. Fast growing cellular communication business

Products and services

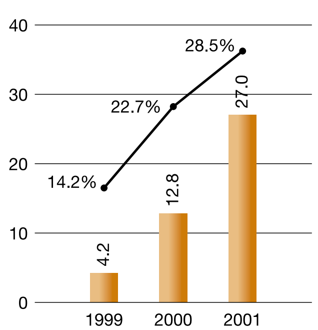
The Company offers premium post-paid and pre-paid GSM cellular communication services. Apart from basic voice services, the Company also offers new services such as SMS, WAP, GPRS (commercial pilot scheme), "UNI-INFO", and bundled services with PSTN/VoIP long distance.

In 2001, "UNI-INFO" was launched as the unified brand for the wireless data business, which at the present offers, mainly, information subscriptions and broadcasting requests through the SMS platform. Through the Company's Internet platform with "165" as dial-up access number, and a close co-operation with Internet content providers ("ICP") and Internet service providers ("ISP"), such as Sina, Sohu and Netease, the Company offers value-added wireless data services to its customers in six major categories, namely news, personal information management, stock trading, entertainment, location-oriented services and industry applications.

The Company has a high quality GSM network. In 2001, call-completion rate and call-drop rate of the Company's GSM network were 97.0% and 0.2%, respectively.

Subscriber base

As of 31 December 2001, the Company had a total of 27.033 million GSM cellular subscribers, up 14.261 million or 111.7% year-on-year (the end of 2000: 12.772 million). The Company's market share in its service areas increased to 28.5% (2000: 22.7%), whilst the market share in net addition market increased to 37.2% (2000: 32.0%). Of which, post-paid subscribers reached 16.489 million, an increase of 5.888 million or 55.5% year-on-year (the end of 2000:10.601 million). Pre-paid subscribers increased by 8.374 million or 3.9 times to 10.544 million (the end of 2000: 2.170 million). The proportion of pre-paid subscribers to the total number of subscribers increased to 39.0% (2000: 17.0%).



GSM Subscribers and Market Share

Subscribers (In million)
Market Share (%)

The rapid growth in GSM subscribers was mainly attributable to continuous enhancement of network quality, tailor-made services for different segments of customers, cancellation of connection fee and the continuous fall of handset prices.

Minutes of usage

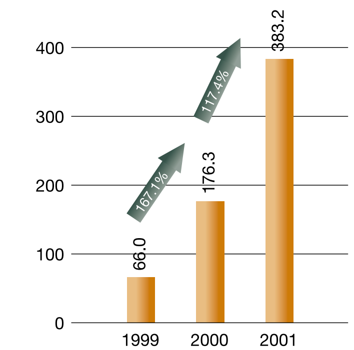
Following a substantial increase in the number of subscribers, total minutes of usage ("MOU") for GSM subscribers in 2001 reached 38.32 billion minutes, an increase of 117.4% year-on-year (2000: 17.63 billion minutes).

As of 31 December 2001, the volume of short messages transmitted reached 1.08 billion. The SMS business has assumed an important role to attract customers to the Company's services, and has contributed to the increase in the Company's MOU. With the interconnection between the Company's SMS platform and other operators' platform, the Company's SMS service is expected to continue rapid growth.

Average MOU and average revenue per subscriber per month ("ARPU")

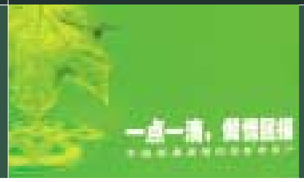
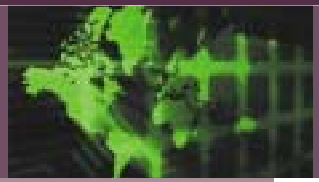
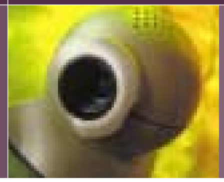
In 2001, the average MOU per subscriber per month for the Company was 161.2 minutes, fell 18.3 minutes or 10.2 % year-on-year (2000: 179.5 minutes), and fell only 0.9 minutes from 162.1 minutes in the first half of 2001 as mentioned in the interim report. Of which, post-paid MOU was 187.8 minutes, fell 0.3 minutes year-on-year (2000: 188.1 minutes), whilst pre-paid MOU was 89.9 minutes, fell 1.0 minutes year-on-year (2000: 90.9 minutes). Since pre-paid subscribers accounted for a higher percentage of the total number of new subscribers, and pre-paid MOU was lower than the post-paid MOU, blended MOU for new subscribers was thus lower, which was attributable to the fall in blended MOU.

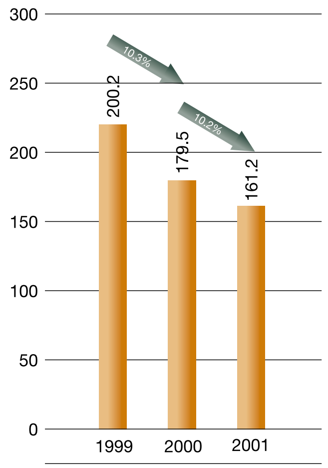
In 2001, the average revenue per subscriber per month ("ARPU") for the Company was RMB 86.3, less RMB 38.0 or 30.6% (2000: RMB 124.3), and RMB 6.2 less than that in the first half of 2001 as mentioned in the interim report. Of which, ARPU for post-paid subscribers was RMB 94.8, less RMB 34.2



GSM Minutes of Usage

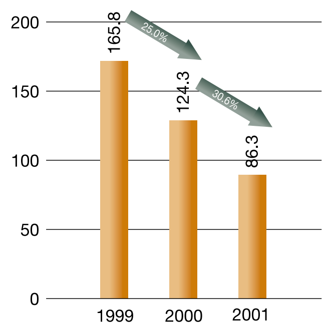
MOU (100 million)
Growth Rate (%)



MOU

MOU (minutes)



ARPU

ARPU (RMB)

(2000: RMB 129.0). ARPU for pre-paid subscribers was RMB 63.4, less RMB 11.7 (2000: RMB 75.1). The decrease in ARPU was attributable to, first, an increase in the proportion of pre-paid subscribers to the total number of subscribers and a fall in the average MOU, second, competition in the market being increasingly intensive, and, third, cancellation of connection fee and additional telecommunications surcharges.

During the second half of the year, the declining rate in ARPU had substantially slowed down. The Company believes that its cellular business income will continue to grow steadily.

Churn rate

In 2001, the churn rate of the Company was 16.3%, up significantly when compared with 9.5% in 2000. The increase was attributable to changes in the demand of subscribers for communication services, with some subscribers switching to pre-paid services. On the other hand, individual consumers are spending their money in a more mature manner. With the reduction in the connection fee, the switching cost became much less than before, resulting in more frequent switches between networks.

Development strategies

In 2002, the development of the Company's GSM cellular communication network will be focused on the optimization of the network, enhancement of the network operation quality, and the development of wireless data business and other value-added businesses. In order to increase its market share for GSM subscribers and realize growth in both subscribers and profitability, the Company will adopt sales and marketing strategies concentrating on market segmentation and bundled sales, introduce retention programs focusing on quality service and wireless data service to promote customer loyalty and satisfaction and secure relationships with high usage subscribers, and at the same time seek to expand in the mass market through pre-paid services.

In January 2002, the Company started to lease capacity of the CDMA network in the Company's service areas from the parent company on an exclusive basis. By the adoption of different sales and marketing strategies for different customer segments, provision of quality voice and customer services, as well as new wireless data services to attract high usage customers, the Company will obtain more competitive advantages in the cellular market in the PRC. The Company believes that, the cellular market in the PRC, characterized by its enormous scale and diversified demand of subscribers, will be able to support the parallel development of both GSM and CDMA technologies. The operation of the CDMA network is in line with the development strategies of the Company.

International and Domestic Long Distance Business

2. Swift development in international and domestic long distance business

International and domestic long distance business

The total minutes of the Company's outgoing international and domestic long distance calls increased to 6.41 billion minutes, up 5.9 times year-on-year (2000: 0.93 billion minutes). Total minutes of the international incoming calls were 1.23 billion minutes, up 3.4 times year-on-year (2000: 0.28 billion minutes). Both international and domestic long distance businesses posted strong growth.

PSTN long distance business

The Company's PSTN long distance business recorded robust growth. As of 31 December 2001, PSTN long distance business covered 304 cities, representing 90% of 338 cities across the country. There were a total of 4.528 million registered subscribers.

In 2001, the total minutes of PSTN outgoing long distance calls increased by 10.3 times year-on-year to 2.72 billion minutes (2000: 0.24 billion minutes). Of which, domestic long distance calls reached 2.64 billion minutes, whilst international, together with Hong Kong, Macau and Taiwan long distance calls reached 80 million minutes. The total minutes of incoming international calls reached 1.16 billion minutes.

IP telephony

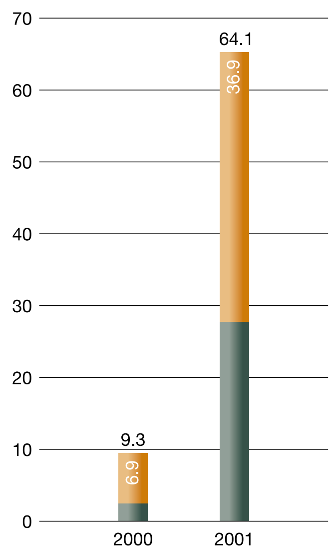
The Company's IP telephony business continued to grow rapidly. As of 31 December 2001, the number of cities covered by the Company's IP telephone network increased to 320 (the end of 2000: 231), and international roaming was available in 50 countries and regions.

In 2001, the total minutes of IP outgoing long distance calls increased by 4.3 times year-on-year to 3.69 billion minutes (2000: 0.69 billion minutes). Of which, domestic long distance calls reached 3.52 billion minutes, whilst international, together with Hong Kong, Macau and Taiwan long distance calls reached 0.17 billion minutes. The total minutes of incoming international calls reached 70 million minutes.

Leased line business

The Company offers leased line services to its subscribers. The Company may provide leased lines of different bandwidth according to the requirements of the subscribers. As of 31 December, 2001, total bandwidth leased amounted to 2350 x 2Mbps.

The Company will vigorously implement a corporate customer-oriented marketing strategy and provide high quality and inexpensive communication services to increase the Company's market share for the long distance business.



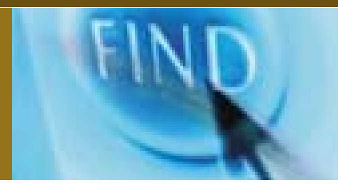
International & Domestic Long Distance Calls

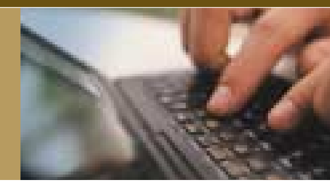
IP Telephony (100 million minutes)
PSTN Long Distance (100 million minutes)

Development strategies

The Company will vigorously implement a corporate customer-oriented marketing strategy and provide high quality and inexpensive communication services to increase the Company's market share for the long distance business. In order to rapidly develop the Company's long distance business with limited access resources, the Company's direct sales force will provide tailor-made services and innovative communication solutions to corporate customers so as to satisfy their diverse and increasing communication needs. As to the mass market, the Company will seek expansion through contract and prepaid services, as well as expansion in the sales channel by way of distributorship. At the same time, the Company will explore opportunities to increase incoming calls from Hong Kong, Macau, Taiwan and international markets, so as to fully capitalize on the Company's network capacity.

Network Infrastructure





Data and Internet Services

As the state government is encouraging the use of information technology and e-Commerce among enterprises and government organizations, the Company will actively develop the e-Commerce through extensive cooperation.

3. Characteristic data and Internet businesses

Data business

The Company employs the technologies of asynchronous transfer mode ("ATM") and frame relay ("FR") to provide data carrier service, as part of its data service expansion. As of 31 December 2001, total bandwidth leased for ATM and FR carrier operations amounted to 826 x 2Mbps.

Internet business

The Internet related services that the Company currently provides include dedicated line Internet access, dial-up Internet access, Internet data center ("IDC") and international roaming of Internet access. In addition, the Company actively develops other Internet application businesses, including ICP services and e-Commerce services.

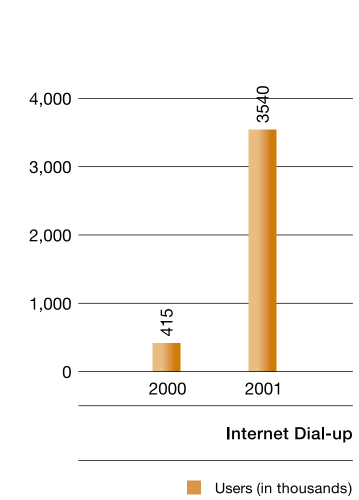
As of 31 December 2001, Internet subscribers increased to 3.544 million, up 7.5 times (2000: 415 thousand). Of which, the number of dedicated line subscribers amounted to 4,555, and the number of dial-up subscribers reached 3.540 million.

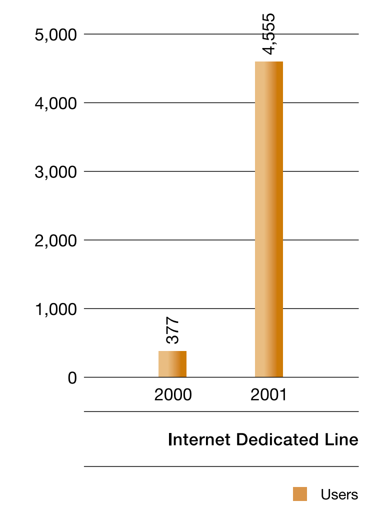
As at the date of this report, the Company provides incoming international roaming Internet services for a total of 148 countries and regions, while outgoing international roaming Internet services are available in 103 countries and regions.

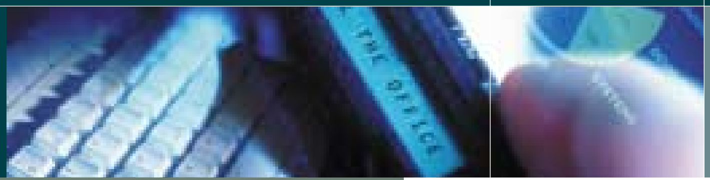
Development strategies

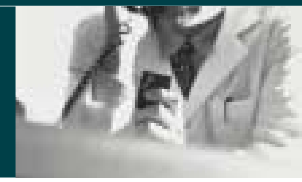
With regard to data communication, the Company's focus is optimization of its network. The Company intends to set up an international first-class carrier platform for the Company's integrated businesses through enhancing the security and reliability of the network, timely upgrade and expansion of the network, and refining the MPLS function. The Company will also introduce various data services and multi-media value-added services, such as video conferencing system on the IP platform, QoS guaranteed ATM / FR operations, and circuit simulation by connecting the PSTN with packet switch network.

As for Internet business, the Company will continue to increase the number of subscribers for its dedicated line and dial-up Internet access and, at the same time, the Company will leverage on the comprehensive and integrated network with cutting edge technology to focus on the development of national corporate customers and to expand IP-VPN, VISP, IDC, and international incoming and outgoing roaming businesses when appropriate. By utilizing the CDMA 1x network, the Company's Internet platform will function as an integrated gateway for handling all incoming Internet messages, which will in turn facilitate the development of mobile Internet business. As the state government is encouraging the use of information technology and e-Commerce among enterprises and government organizations, the Company will respond by identifying the business models for e-Commerce, and actively develop the e-Commerce business through extensive cooperation.









Paging

While applying stringent measures to tighten the capital expenditure for the paging business, the Company intends to rationalize the network infrastructure and reduce staff size and costs.

4. Maintaining dominant position in paging business

Products and services

The Company offers numeric paging and Chinese paging services on local, provincial and national levels.

The Company has introduced two-way paging services, and provides wireless data services including stock quotation, flight information, weather, news and entertainment through the paging network. With the launch of paging-cellular bundled services, short messages can be available through both pagers and handsets which have the SMS function. This in turn has brought much convenience to the subscribers.

Subscriber base

The Company has added 11.186 million new subscribers. As of 31 December 2001, the number of pager subscribers reached 32.907 million, falling by 11.613 million or 26.1% year-on-year (the end of 2000: 44.520 million). Of which, 287 thousand were information pager users.

As paging adopts the transmission method by way of broadcasting, it is inexpensive, and will continue to enjoy some irreplaceable advantages over other technologies in the development of certain value-added services. The Company believes that there will be a basically steady paging subscriber base in the foreseeable future.

Average revenue per subscriber per month ("ARPU")

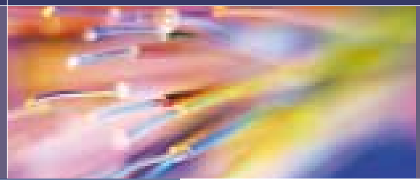
In 2001, the average revenue per paging subscriber per month was RMB 9.4, a decline of RMB 5.9 or 38.6%, compared to RMB 15.3 for 2000. The decline was attributable to the decreasing up-front fee for cellular communication and other telecommunications businesses. The Company will seek to introduce more value-added service, and to jointly develop the paging market with other operators, thereby seeking to stabilize the average revenue per paging subscriber per month.

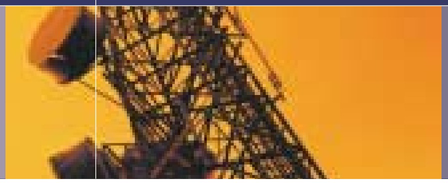
Churn rate

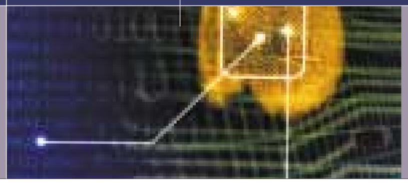
In 2001, the churn rate of paging business increased to 57.6% (2000: 28.4%). The increase in churn rate was mainly due to the migration of paging subscribers to cellular communication and other telecommunications services, and the continued structural changes in the paging subscriber base.

Development strategies

While applying stringent measures to tighten the capital expenditure for the paging business, the Company intends to rationalize the network infrastructure and reduce staff size and costs. The Company will seek to expand value-added services for paging, and promote information paging and two-way wireless personal digital assistant services, so as to maintain the Company's paging market scale. In order to ensure the efficiency of the paging business, the Company will fully utilize the resources of the paging business, develop operator-assisted short messages, enhance customer services, and outsource the call centre business. Leveraging on the advantages derived from an integrated business profile, the Company will actively lead paging subscribers to use the Company's cellular communication services through the paging-cellular bundled service.







Network Infrastructure

Emphasis will be put to increase the transmission capacity and reliability, enhance network self-healing capability and transmission reliability, so as to improve the technological levels and communication capabilities of the network of the Company.

5. Network infrastructure

Network construction

The Company has a state-of-art broadband optical fibre transmission network with nationwide coverage. The network utilizes cutting edge technologies of self-healing SDH structure and DWDM. Together with the core switching network based on ATM + IP technologies, they serve as the common network platform supporting various telecommunications operations of the Company, including cellular communication, international and domestic long distance, data, Internet and paging. Thus, highly secure and reliable communication services are offered to the subscribers at a relatively lower cost.

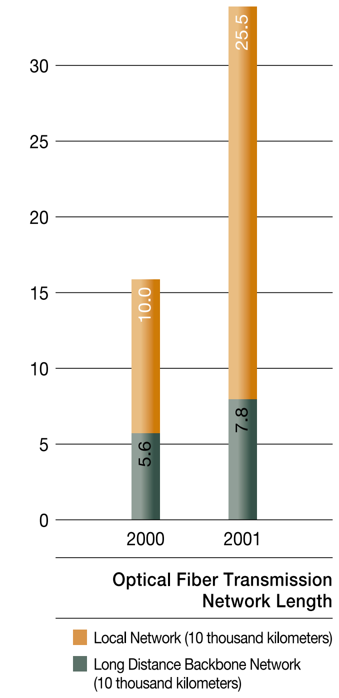
As at 31 December 2001, the Company had completed a high speed and reliable inter-provincial long distance backbone transmission network comprising of a number of fibre rings and certain branch network systems. The Company's optical fibre transmission network reached 333 thousand kilometres in length covering 303 cities, of which its optical fiber backbone transmission network accounted for 78 thousand kilometres. Apart from satisfying self transmission demand, the Company commenced leasing of sections of the network and fibers to other telecom operators and corporate customers.

Parallel to construction of the domestic optical fibre backbone transmission network, the Company has also actively participated in the construction of an international backbone transmission network. In April 2000, the Company entered into an agreement for the construction of Asia Pacific Cable Network No. 2 Project ("APCN2"). By the end of 2001, the Company had obtained 4 x 155Mbps half circuit capacity from the Project. The Company had also provided the full circuit service between mainland China and Hong Kong.

In order to expand the Company's long distance, data, Internet, and cellular communication businesses, targeting major corporate customers, the Company has formulated the "Ten Thousand Office Building Connection Project" in the construction of networks for metropolitan areas. As of 31 December 2001, the Company connected 11,726 office buildings with broadband transmission network, mainly comprised of optical fiber.

Development strategies

In 2002, the Company will improve the wavelength division multiplexing ("WDM") platform for the inter-provincial backbone transmission network, whilst improving the inter-provincial and intra-provincial long distance backbone optical fiber transmission network. The Company also expects to roughly complete the long distance backbone maintenance and support system. Emphasis will be put on increasing the transmission capacity and reliability, as well as enhancing the network self-healing capability and transmission reliability, so as to improve the technological levels and communication capabilities of the network of the Company. The Company will expedite the construction of an international transmission gateway, laying the foundation for the expansion of international businesses.



Optical Fiber Transmission Network Length

III. SALES AND MARKETING

1. Operating principles

Under the "Customer First" principle, the Company is dedicated to uphold the "market-oriented and customer-focused" rationale, and fully capitalize on the advantages of an integrated telecommunications operator. Leveraging on the government's preferential tariff policy, the Company flexibly adjusts its sales and marketing strategies for different geographical regions, market segments and customer bases to fully satisfy the varied needs of customers. The Company also enhances the depth and coverage of its sales and marketing activities and provides customer services of high quality and efficiency.

2. Sales and marketing strategies

Steps have been taken to establish a marketing management system with strong planning capabilities and responsive to market changes. The Company pursues its sales and marketing activities through market survey, market segmentation, market positioning, marketing planning, pricing, profit and loss analysis, branding, sales and marketing channel, customer relationship management, and customer services to improve the Company's market competitiveness.

The Company capitalizes on the advantages of an integrated telecommunications operator, and applies different sales and marketing strategies for different market segments. The Company offers different services at different regions to different customer groups by ways of different bundles of services in accordance with market demand. Sales for cellular, international and domestic long distance, data, Internet and paging services are conducted on an integrated basis. The Company is already offering services in bundles such as "Liang Wang Tong" as a bundle of cellular and paging services, "Yi Ji Liang Wang" as a bundle of cellular and IP telephony, as well as bundling of cellular, "193" long distance service, and "165" Internet service.

3. Brand building strategies

The Company continues to build a brand image as an integrated telecommunications operator. The Company considers that brand name is the most valuable intangible asset of the Company. By building the awareness, recognition, and loyalty of the brand name among its customers, the Company can increase the demand of its services and uplift its enterprise value. The integrity and consistency of the Company's brand name and profile is maintained through consolidation of its brand and central coordination in management, planning and implementation. The advantages of the Company's integrated telecommunications operation will be facilitated and optimized accordingly.

4. Customer services

A lot of emphasis has been put to customer service, and substantial investment has been made in the customer service system. The "1001" customer service system which unified the access number and standard of customer service across the country is now in full operation. The system coordinates customer service on a central and unified basis, offering services including handling customer enquiry, bill enquiry, complaints, sales, payment reminder and emergency services. The Company also implements an Enquiry Accountability System and standard procedures for the effective handling of enquiries to ensure that all customer enquiries will be answered within a specified period of time. Customer satisfaction is thus enhanced, and the quality of the Company's customer service program is improved. The Company also introduced the "one-stop" solution for sales and payment to ensure that customers enjoy unrivalled convenience and quality services.

5. Sales channel

The Company has established a nationwide sales network, which comprises sales outlets, agents, distributors, joint sales outlets, direct sales team and agents for major customers. The Company markets its products and services to the mass market through its own sales outlets, together with agents, distributors and joint sales outlets. Customers will benefit from the extensive coverage of the Company's sales channel, which in turn will increase the penetration of the Company's services. With regard to corporate customers, the Company adopts a two-prong strategy through its direct sales team and agents to conduct sales on a one-to-one basis to increase penetration. The Company has also established a direct sales and customer service team targeting high usage corporate customers.

In February 2001, Unicom Group entered into a strategic cooperation agreement with China Post, allowing it to leverage on China Post's nationwide outlets network to market the Company's services as well as allowing China Post to collect fees from customers on the Company's behalf.

The Company has established a nationwide sale and marketing network. As of 31 December, 2001, the Company has over 3500 sales outlets, and a total of over 37000 agencies and distributors. Of which, over 9000 sales outlets were under the joint-venture with China Post.

IV. TARIFF

1. Tariff strategies

As a newly emerged telecommunications operator, the Company has always complied with various tariff and regulatory policies as promulgated by the relevant government regulatory authorities in the PRC. The Company has always been cautious towards its preferential tariff treatment given by the government regulatory authorities in the PRC. The Company still insists that in order to satisfy the diverse needs of customers, increase market share and improve the Company's competitiveness, the Company should offer secure and reliable communication services, enhance customer services quality, and introduce innovative services. Increasing profitability is the ultimate objective of the Company's tariff strategies. The Company's preferential tariff treatment given by the government regulatory authorities in the PRC should not be interpreted as a major competitive advantage of the Company.

2. Tariff adjustment

The Company adjusted its tariff with regard to the international and domestic long distance business, leased line, and data in accordance with the relevant government regulatory authorities in the PRC, subject to the approval of the relevant government regulatory authorities, with effect from midnight on 21 February 2001.

On 30 June 2001, the Company received a notice from the relevant government regulatory authorities in the PRC, requiring the company to cancel the connection fee for cellular services and other surcharges for government funds imposed on telecommunications services, with effect from 1 July 2001.

Management's Discussion and Analysis of Financial Condition and Results of Operations

Our objective in 2001 was to become a first class international telecommunications company by: providing superior service through a quality network; optimizing the allocation and integrated usage of telecommunications resources in the pursuit of technological leadership and operational innovation; proactively mobilizing the expansion of various businesses at low cost to enhance our ability to create revenue and improve operational efficiency; and consistently reinforcing our long term competitiveness. We also emphasized the improvement of key economic indicators, such as cash flows and return on investment, in order to achieve high efficiency on the basis of high growth. At the same time, we also employed prudent financial policies and cash management strategies to preserve a stable capital and financial structure in order to consistently improve efficiency and create value for our shareholders.

In 2001, we achieved sound financial results. Annual revenue reached RMB29.39 billion, an increase of 24.1% from the previous year. Total service revenue (which excluded proceeds generated by sales of telecommunications products) grew by 29.3% from the previous year. EBITDA[1] increased by 23.4% from the previous year to RMB13.53 billion, and EBITDA margin maintained at a relatively high level of 46.0%. Net income increased by 37.8% to RMB4.46 billion and net income margin increased by 1.5% to 15.2%. Net income per share climbed up 24.1% to RMB0.36.

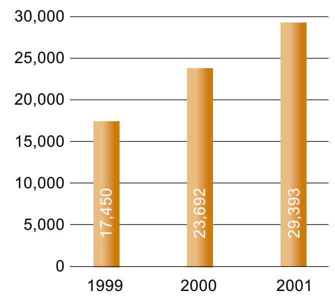
Our Cellular Business revenue maintained a high growth rate of 65.5% in 2001, and continued to be our key driver of growth in revenue and earnings. Our Long distance, Data and Internet Business recorded even more robust growth as revenue from these businesses increased by more than twofold, reflecting our market advantage as an integrated telecommunications operator. As the share of our revenue from the Cellular Business in total revenue increased and as we further increased our economies of scale, we not only maintained a stable EBITDA margin, but also improved our net income as compared to the previous year.

[1] EBITDA represents income before financial income and expense, net other income, taxation, depreciation and amortization. For corresponding year of 2000, EBITDA represented income before the aforesaid items and loss arising from terminations of CCF Arrangements.

I. TOTAL REVENUE

Continuous rapid growth of total revenue

In 2001, the Company continued our strong revenue growth trend. Our annual revenue increased 24.1% to RMB29.39 billion from RMB23.69 billion in 2000. Of this amount, our service revenue increased 29.3% to RMB28.16 billion from RMB21.77 billion in 2000. As our Cellular Business continued its rapid growth and as our Long Distance, Data and Internet Business boomed, our overall competitiveness strengthened significantly.

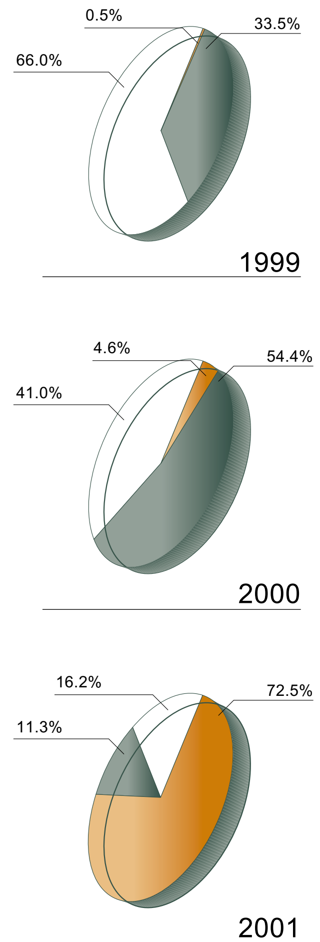


Total Revenue

RMB million

Further rationalization of revenue structure

At the same time that our total revenue increased significantly, our revenue structure continued to change. We became more focused on network build-out and management, while reducing sales of telecommunications products, such as pagers. The share of service revenue in total revenue increased from 91.9% in 2000 to 95.8% in 2001. The Cellular Business, which increased its share of our total revenue from 54.4% in 2000 to 72.5% in 2001, continued its strong performance and boosted the rapid growth of our total revenue. Our Long Distance, Data and Internet Business have gradually become important sources of revenue for us, rapidly increasing their share of total revenue from 4.6% in 2000 to 11.3% in 2001. At the same time, the Paging Business's share of total revenue decreased from 41.0% in 2000 to 16.2% in 2001. These changes in the structure of our total revenue, while reflecting the decline of the paging market, demonstrate our strategy of focusing on high growth and high profit businesses to achieve more stable earnings growth.



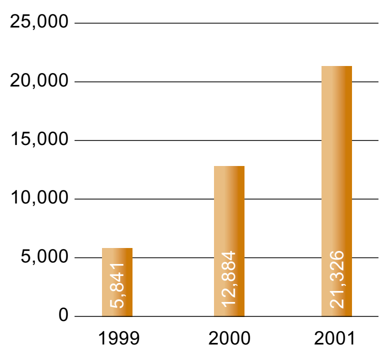
Revenue Structure

Cellular
Long Distance, Data and Internet
Paging

The following table shows the major revenue items and their respective percentage in total revenue in 1999, 2000 and 2001:

	1999		2000		2001	
	RMB in million	As percentage of total	RMB in million	As percentage of total	RMB in million	As percentage of total
Total Revenue	17,450	100%	23,692	100%	29,393	100%
(1) Service Revenue	14,440	82.8%	21,767	91.9%	28,156	95.8%
include:						
Cellular	5,314	30.5%	12,188	51.5%	20,505	69.8%
Paging	9,047	51.8%	8,483	35.8%	4,342	14.8%
Long Distance, Data and Internet	79	0.5%	1,096	4.6%	3,309	11.2%
(2) Sales of Telecommunications Products	3,010	17.2%	1,925	8.1%	1,237	4.2%
include:						
Cellular	527	3.0%	696	2.9%	821	2.8%
Paging	2,483	14.2%	1,229	5.2%	416	1.4%

Sustained steady growth of revenue from cellular business

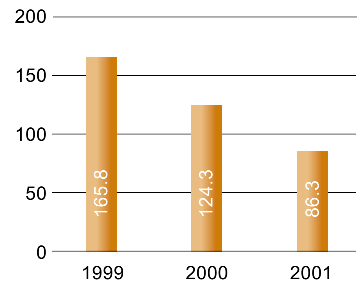


Revenue of Cellular Business

RMB million

As our cellular subscriber base and total usage of our cellular services expanded significantly, our Cellular Business continued its robust growth trend. Continuing its increasing contribution to our total revenue, revenue from the Cellular Business increased 65.5% to RMB21.33 billion from RMB12.88 billion in 2000. Of this amount, service revenue increased by 68.2% to RMB20.51 billion from RMB12.19 billion in 2000.

The average revenue per user (ARPU) dropped from RMB124.3 in 2000 to RMB86.3 in 2001, due to expanding market penetration, a higher portion of low usage and pre-paid usage subscribers among new subscribers, discontinuation of connection fees and additional fees and the reduction of long distance tariffs and increasing market competition. Post-paid ARPU was RMB94.8 in 2001, a decrease of 26.5% from RMB129.0 in 2000; on the other hand, pre-paid ARPU reached RMB63.4, a decrease of 15.6% from RMB75.1 in 2000. The drop in ARPU reflects the market wide trend of expansion of cellular service deeper into the mass market and allows our current subscriber load per channel to increase with decreasing average minutes of usage per subscriber per month (MOU), thus directly reducing the capital expenditure per user.



ARPU

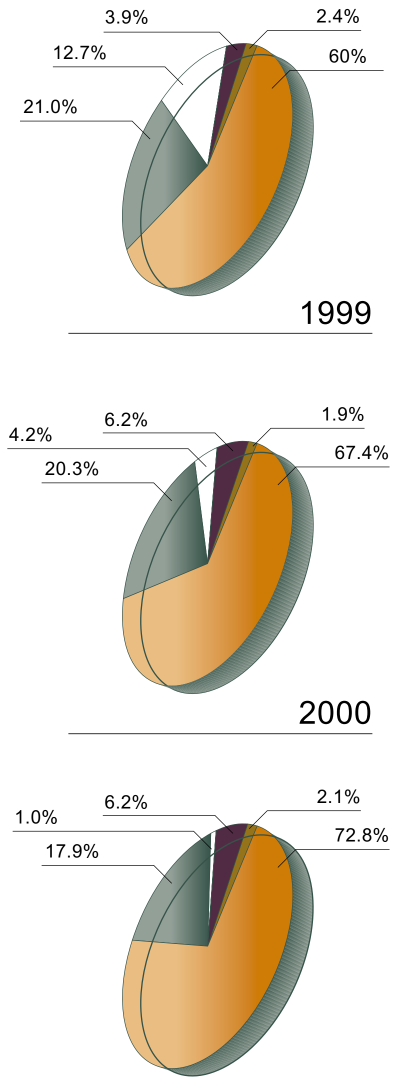
RMB

The following table illustrates the major revenue items from our Cellular Business in 1999, 2000 and 2001 and their respective percentage in Cellular Business revenue:

	1999		2000		2001	
	RMB in million	As percentage of Total	RMB in million	As percentage of Total	RMB in million	As percentage of Total
Revenue	5,841	100%	12,884	100%	21,326	100%
(1) Service Revenue	5,314	91.0%	12,188	94.6%	20,505	96.2%
include:						
Usage Fee	3,189	54.6%	8,212	63.7%	14,938	70.0%
Monthly Fee	1,116	19.1%	2,476	19.2%	3,660	17.2%
Connection Fee	674	11.5%	518	4.0%	205	1.0%
Interconnection Revenue	208	3.6%	754	5.9%	1,262	5.9%
Others	127	2.2%	228	1.8%	440	2.1%
(2) Sales of Cellular-Related Telecommunications Products	527	9.0%	696	5.4%	821	3.8%

Usage fee

The expansion of our cellular subscriber base and the improvement in our network service capabilities have boosted cellular usage fees, which grew 81.9% to RMB14.94 billion, from RMB8.21 billion in 2000. The rapid growth of pre-paid service, which has a higher airtime charge base, and the discontinuation of connection fees in 2001 caused the revenue from usage fees to increase its share of Cellular Business service revenue (not including the sale of cellular-related telecommunications products) from 67.4% to 72.8%. The revenue from the pre-paid cellular service in 2001 amounted to RMB4.10 billion, which increased by 5.3 times from RMB0.65 billion in 2000, accounting for 20.5% of the Cellular Business service revenue.



Service Revenue Composition for Cellular Business

- Usage Fee
- Monthly Fee
- Connection Fee
- Interconnection Revenue
- Other Service Revenue

Monthly fee

The monthly fee from Cellular Business rose 47.8% to RMB3.66 billion in 2001 from RMB2.48 billion in 2000. The relatively slow growth was mainly due to the preference of the new subscribers for pre-paid service. Subscribers of pre-paid service accounted for 58.7% of the additional subscribers in 2001 compared to 24.3% in 2000. As a result, the share of the monthly fees in the Cellular Business service revenue dropped to 17.9% from 20.3% in 2000.

Connection fee

Connection fee from Cellular Business reduced to RMB0.2 billion in 2001 from RMB0.52 billion in 2000 resulting accordingly in a diminished share in the Cellular Business service revenue from 4.2% to 1.0%. The drop was caused by the discontinuation of connection fees for new subscribers, effective from July 1, 2001, in accordance with relevant regulations by the Ministry of Information Industry and the Ministry of Finance.

Interconnection revenue

Interconnection revenue from the Cellular Business rose sharply from RMB0.75 billion in 2000 to RMB1.26 billion in 2001, an increase of 67.5%. The increase was mainly due to growing cellular coverage and subscriber base and rising incoming traffic from other networks.

Value-added services and other revenue

In order to continue to meet the diverse needs of our customers, we emphasized the rapid development and application of value-added services and improved the quality of our service. In 2001, we initiated our wireless data business under the uniform brand of "UNI-INFO", while further developing value-added services based on the SMS platform and WAP and GRPS technologies. The revenue from cellular value-added services and other revenue amounted to RMB0.44 billion. Maintaining our position in value-added services will have a positive influence on our revenue growth and help to sustain our competitiveness.

Sales of cellular-related telecommunications products

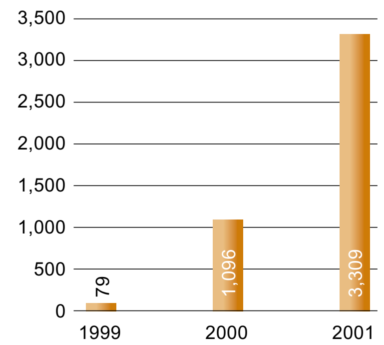
In 2001, sales of cellular-related telecommunications products were RMB0.82 billion, up 17.9% compared to RMB0.70 billion in 2000. The growth was principally due to increased SIM card sales caused by the sharp rise of cellular subscribers, although this was partially offset by the lowering of the unit price of SIM cards.

Strong growth in revenue from long distance, data and internet business

The coverage and capacity of our Long Distance, Data and Internet networks expanded significantly in 2001. Our network and subscriber resources were leveraged to further the integration of our business and realize consistent expansion in the competitive market environment through delivery of quality and comprehensive service and attractive product mix. Long Distance, Data and Internet business have been developing into important revenue generation sources. Total service revenue from these business amounted to RMB3.31 billion, an increase of 2.0 times from 2000. In addition, our Long Distance, Data and Internet business also provided transmission capacity for our Cellular Business and thus our inter-segment revenue reached RMB1.17 billion. The fast and strong revenue growth from the Long Distance, Data and Internet Business not only contributed to our overall revenue growth, but also demonstrated our positive long-term development outlook as an integrated telecommunications operator.

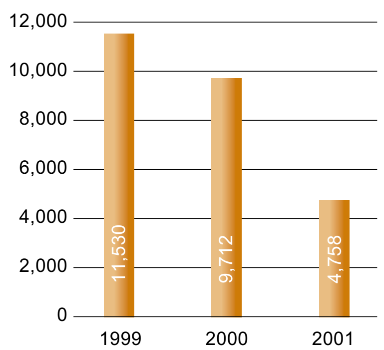
PSTN long distance revenue

As our nationwide long distance coverage expanded and interconnection improved, PSTN long distance revenue increased rapidly to RMB1.49 billion in 2001. We not only continued to satisfy domestic long distance demand, but also actively cooperated with overseas international telecommunications operators to effectively allocate resources to service incoming international, Hong Kong, Macau and Taiwan calls. We expect the international long distance call business to continue to enjoy positive growth, as the length of international incoming calls connected reached 1.16 billion minutes in 2001.



Revenue of Long Distance, Data and Internet Business

RMB million



Revenue of Paging Business

RMB million

Revenue from data and IP telephony

We fully leveraged our competitive advantage as an integrated telecommunications operator and focused on the development of high value-added data services, such as FR, ATM, VPN, with our uniform and advanced integrated data communication platform. At the same time, we further improved the network coverage and communication quality of IP telephony and effectively expanded the usage of our IP telephony services (both domestic and international) through Direct Dial, PBX Preselection, Long Distance Registration and strengthening retail sales of telephone cards. The revenue from Data and IP Telephony business reached RMB1.55 billion in 2001.

Revenue from Internet business

In 2001, our Internet services expanded to mobile SMS download, IDC, VPN/VPDN, bank card, VISP, etc. The open platform was actively used to reinforce the cooperation with the ISP, ICP and SP businesses. The annual Internet revenue reached RMB0.27 billion.

Sharp decline in paging business revenue

The total paging revenue in 2001 was RMB4.76 billion. Paging service revenue (i.e., excluding sales of paging-related telecommunications products) was RMB4.34 billion, representing a decline of 48.8% from RMB8.48 billion in 2000. The principal factor for the decline was the replacement of paging services by cellular and other telecommunications services, which led to negative growth in the paging business and decreasing tariffs from intensifying competition. Therefore, we used considerable efforts to stabilize the incumbent traditional paging market and accelerate the development of bundled services and deployment of new technology. At the same time, we also sought to provide our former paging subscribers with our cellular and other telecommunications services.

As we have been reducing our share of pager sales, our revenue from the sales of paging-related telecommunications products dropped from RMB1.23 billion in 2000 to RMB0.42 billion in 2001, corresponding in a drop in its proportion in Paging Business revenue from 12.7% to 8.8%.

II. OPERATING EXPENSES

Total operating expenses

In 2001, in addition to boosting revenue, we also focused on tightening cost control through increasing operational efficiency from economies of scale and sharing of network, business, subscriber and sales resources. Nonetheless, total operating expenses increased to RMB24.13 billion in 2001 as compared to RMB18.47 billion in 2000, an increase of 30.6%, due to increases in fixed costs, such as depreciation and amortization, rising selling and marketing expenses in an increasingly competitive environment, and a provision for impairment of paging assets. Compared to the 24.1% increase in total revenue, the increase in expenses exceeded the increase in total revenue by 6.5%. We will continue to focus on cost control and optimization of our expense structure in order to ensure the continued growth in earnings.

The following table illustrates the major expenditure items from 1999 to 2001 and their respective share in the total revenue as a percentage.

	1999		2000		2001	
	RMB in million	% of Total Revenue	RMB in million	% of Total Revenue	RMB in million	% of Total Revenue
Total Revenue	17,450	100%	23,692	100%	**29,393**	**100%**
Total Operating Expenses	14,634	83.9%	18,470	78.0%	**24,129**	**82.1%**
Leased Lines	1,099	6.3%	1,158	4.9%	**853**	**2.9%**
Interconnection Charges	693	4.0%	1,380	5.8%	**2,073**	**7.1%**
Depreciation and Amortization	3,691	21.2%	5,734	24.2%	**8,262**	**28.1%**
Personnel	1,713	9.8%	1,770	7.5%	**2,487**	**8.5%**
Selling and Marketing	1,557	8.9%	2,492	10.5%	**3,613**	**12.2%**
General, Administrative and Other Expenses	2,586	14.8%	3,743	15.8%	**5,499**	**18.7%**
Cost of Telecommunications Products sold	3,294	18.9%	2,193	9.3%	**1,342**	**4.6%**

Leased lines

Reduced leased line tariffs contributed to the further reduction of our leased line expenses. At the same time, we effectively reduced our leased line expenses by extending and optimizing our nationwide optical fiber network, utilizing our own transmission network and improving the allocation and coordination of network resources.

Even though our network capacity and subscriber base has expanded substantially, in 2001, our leased line expenses decreased by 26.3% from RMB1.16 billion in 2000 to RMB0.85 billion in 2001. Leased line expenses accounted for 2.9% of total revenue, a decrease from 4.9% in 2000.

Interconnection charges

Due to the expansion of our network, increases in our subscriber base and interconnection traffic and adjustments to interconnection settlement methods and standards, interconnection charges grew from RMB1.38 billion in 2000 to RMB2.07 billion in 2001, representing a 50.2% increase. Interconnection charges in our Cellular Business, Long Distance Business, Data and Internet business increased by 73.1%, 10.7 times and 3.6 times, respectively. Interconnection charges as a percentage of our total revenue grew from 5.8% to 7.1%. Furthermore, in accordance with certain regulations issued in 2001 by the Ministry of Information Industry regarding settlement of interconnection charges between networks, our IP telephone business began interconnection settlements with other domestic operators from March 2001, resulting in an additional expense of RMB0.12 billion.

Depreciation and amortization

Depreciation and amortization expenses grew by 44.1% from RMB5.73 billion in 2000 to RMB8.26 billion in 2001. The increase of RMB2.53 billion accounted for 44.7% of the total increase in our operating expenses of RMB5.66 billion, making this the biggest factor in the increase in operating expenses. Rising depreciation and amortization expenses were the result of increased capital expenditures in the further expansion of our networks. The share of depreciation and amortization in total revenue increased to 28.1% in 2001 from 24.2% in 2000.

Personnel

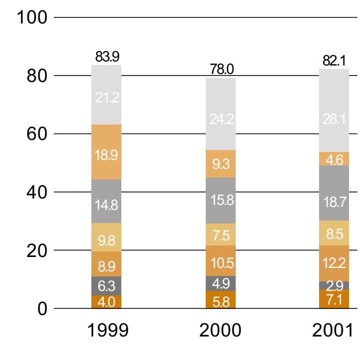
Despite the consistent and rapid growth of our various businesses, we emphasized reasonable allocation of human resources and were able to maintain strict control over personnel growth, thereby steadily raising our productivity.

As of the end of 2001, we employed 29,973 employees, 15.4% less than the 35,432 in 2000. In order to adapt to the changing competitive human resource market, to promote competition for positions at our company and to incentivize employees, we reformed our compensation structure in 2001. As a result, our personnel expenses rose from RMB1.77 billion in 2000 to RMB2.49 billion in 2001, accounting for 8.5% of total revenue as compared to 7.5% in 2000. Meanwhile, our compensation structure was tied to individual performance and company performance, resulting in reasonable personnel expenses. An attractive remuneration scheme is helpful in enhancing the long-term competitiveness of our company by retaining and attracting talented employees.

Selling and marketing

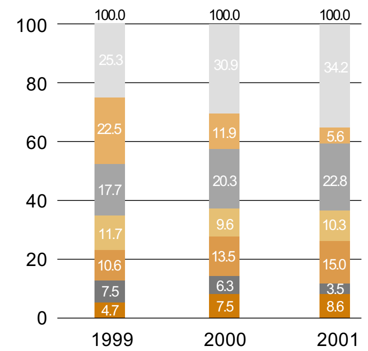
Our major selling and marketing expenses include commissions and promotion and advertising expenses. The rapid expansion of our various businesses and the substantial growth in new subscribers have resulted in an increase in commissions paid to agents. Increasing investment in market development and promotion of new products also resulted in increased promotion and advertising expenses. Our annual selling and marketing expenses were RMB3.61 billion in 2001, up 45.0% from RMB2.49 billion in 2000. Of this amount, RMB2.82 billion was commissions (an increase of 59.2% from 2000) and RMB0.79 billion was promotion and advertising expenses (an increase of 9.9% from 2000). Accordingly, the proportion of selling and marketing expenses in total revenue increased to 12.2% in 2001 from 10.5% in 2000. In order to exercise tighter control of our selling and marketing expenses, we implemented a variety of strategies including bundled sales and commission payments pegged to the usage fees of the new subscribers. We also increased efficiency in the allocation of selling and marketing expenses through a strategic partnership with China Post, which further enhanced the depth and breadth of our marketing initiatives.

Analysis of Operating Expenses



Percentage of expenses to total revenue (%)

- Depreciation and Amortization
- Costs of Telecommunications Products Sold
- General, Administrative and Other Expenses
- Personnel
- Selling and Marketing
- Leased Lines
- Interconnection Charges



Composition of operating expenses (%)

- Depreciation and Amortization
- Costs of Telecommunications Products Sold
- General, Administrative and Other Expenses
- Personnel
- Selling and Marketing
- Leased Lines
- Interconnection Charges

General, administrative and other expenses

Our general, administrative and other expenses rose by 46.9% to RMB5.50 billion in 2001, as compared to RMB3.74 billion in 2000. The main reasons for the increase in these expenses include: a provision in the amount of RMB0.63 billion for impairment of paging assets due to operating loss in the Paging Business in certain provinces and increases in telephone card manufacturing expenses, consumables, administrative and management expenses.

The provision for doubtful debts for 2001 was RMB0.54 billion. Despite a rise of 21.6% from 2000, by improving our user credit management and enhancing our billing and payment systems, the proportion of provision for doubtful debts in total service revenue has already improved from 2.0% in 2000 to 1.9% in 2001, out of which the proportion of provision for doubtful debts in service revenue from the Cellular Business dropped from 2.9% in 2000 to 2.5% in 2001.

Cost of telecommunications products sold

The cost of telecommunications products sold declined from RMB2.19 billion in 2000 to RMB1.34 billion in 2001, a drop of 38.8%. The main reason for the cost reduction is our withdrawal from the sale of pagers. The cost of the pagers sold plummeted from RMB1.81 billion in 2000 to RMB0.55 billion in 2001.

III. NET INCOME

Operating income

We have been effectively implementing our strategy of focusing on large customers while actively developing the increasingly important mass market. By increasing our total revenue through timely launching of differentiated products and services and by controlling the growth of our operating expenses, we maintained a reasonable profit level. Total revenue and total service revenue in 2001 increased 24.1% and 29.3%, respectively, from 2000. In the same period, our operating expenses increased by 30.6%. Operating income increased from RMB5.22 billion in 2000 to RMB5.26 billion in 2001, an increase of 0.8%. Operating margin was 17.9% in 2001, as compared to 22.0% in 2000.

Interest income and expenses

Our total interest income in 2001 rose to RMB2.1 billion from RMB1.75 billion in 2000 mainly due to the interest income from the short-term bank deposits of our initial public offering proceeds in 2001.

Our interest expenses in 2001 were RMB1.91 billion, 40.9% higher than the RMB1.35 billion in 2000. The major reason for the rise was the interest on the bank loans obtained for our expanding network buildout. Our interest-bearing debts increased from RMB35.65 billion in 2000 to RMB44.27 billion in 2001.

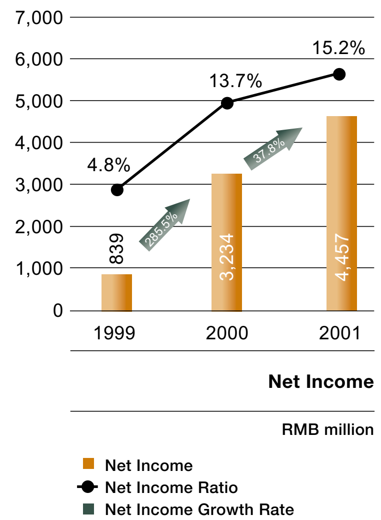
Our net interest income was RMB0.19 billion in 2001, RMB0.21 billion less than the RMB0.40 billion in 2000.

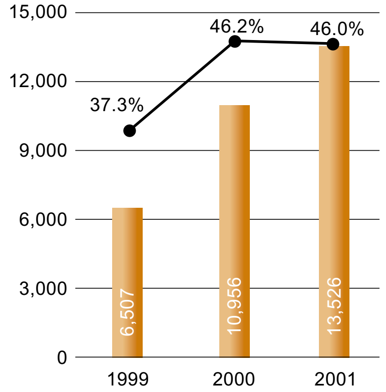
Income tax

Our income tax decreased from RMB1.10 billion in 2000 to RMB1.04 billion in 2001. Our effective tax rates in 2000 and 2001 were 24.7% and 19.1%, respectively. Our statutory tax rate under PRC enterprise income tax laws was 33%. The lower effective tax rate was due to the fact that the interest on the deposits of our initial public offering proceeds in Hong Kong was not subject to Hong Kong income tax.

Net income

Our net income grew from RMB3.23 billion in 2000 to RMB4.46 billion in 2001, an increase of 37.8%. Net income per share was RMB0.36 in 2001, 24.1% higher than RMB0.29 in 2000. Our net income margin also increased from 13.7% in 2000 to 15.2% in 2001. The improvement of our profit level reflected our operational improvements from economies of scale. The loss from the terminations of China-China-Foreign Arrangements in 2000 was also a major factor in the increase of our net income in 2001.



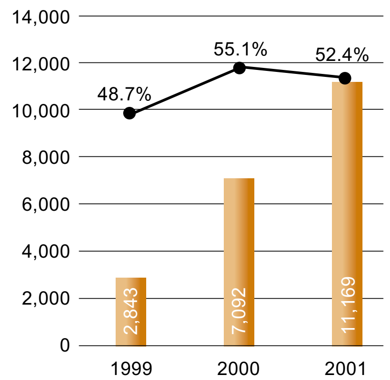


EBITDA and EBITDA Margin

RMB million

EBITDA
EBITDA Margin

EBITDA and EBITDA Margin for each Business Segment



Cellular

RMB million

EBITDA
EBITDA Margin

IV. EBITDA

EBITDA in 2001 was RMB13.53 billion, a 23.4% increase from 2000. EBITDA margin (EBITDA as percentage of total revenue) maintained a relatively high level of 46.0% in 2001. This not only highlighted the sound growth of our overall revenue and the further enhancement of our revenue structure, but also reflected the result of our improved internal management and control of operating expenses.

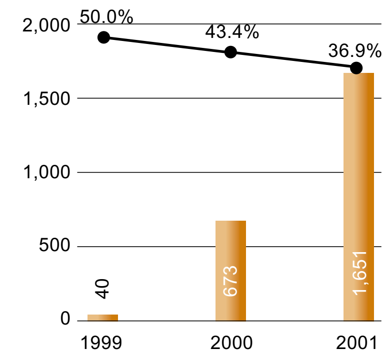
EBITDA of the Cellular Business in 2001 was RMB11.17 billion, an increase of 57.5% from 2000. EBITDA margin for the Cellular Business decreased from 55.1% in 2000 to 52.4% in 2001. The rise in EBITDA of the Cellular Business was mainly due to improvements in network optimization and service quality, as well as our efforts in developing new growth areas through our active promotion of value-added cellular services. The decline in the EBITDA margin of the Cellular Business was mainly due to intensifying market competition and the growth of operating expenses before depreciation and amortization as a percentage of Cellular Business revenue.

EBITDA of the Long Distance, Data and Internet Business grew 145.2% to reach RMB1.65 billion in 2001. The EBITDA margin for these business declined from 43.4% in 2000 to 36.9% in 2001, due principally to rising interconnection charges, personnel expenses and general administrative expenses in these business as a percentage of its revenue.

EBITDA of the Paging Business was RMB0.79 billion in 2001, a decrease of 75.4% from RMB3.21 billion in 2000. The EBITDA margin for this business also decreased to 16.3% in 2001 from 32.4% in 2000. The decline was the result of negative growth in the Paging Business, sharp decline in revenue and profit, and a provision of RMB0.63 billion for impairment of paging assets. We will continue to impose tighter control over operating expenses and capital expenditures in the Paging Business, while working to cut losses in pager sales, so as to stabilize the EBITDA level in this business in the near future.

Even though the EBITDA margins of various business segments recorded different levels of decline, the increase in the share of Cellular Business revenue in our total revenue and the higher EBITDA margin of our Cellular Business as compared with our average EBITDA margin resulted in our ability to maintain a relatively stable overall EBITDA margin.

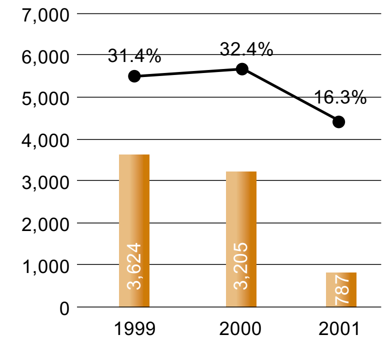
EBITDA and EBITDA Margin for each Business Segments



Long Distance, Data and Internet

RMB million

EBITDA
EBITDA Margin



Paging

RMB million

EBITDA
EBITDA Margin

V. DEBT-EQUITY STRUCTURE

Sound debt-equity structure

The following table sets forth our debt-equity structure as of the end of each of 1999, 2000 and 2001 (RMB in million).

	31 December 1999	31 December 2000	31 December 2001
Cash	6,211	52,556	43,335
Total assets	45,366	112,829	127,905
Short-term interest-bearing debts	7,894	8,501	7,933
Long-term interest-bearing debts	12,234	27,151	36,337
Minority interests	2,530	883	829
Shareholders' equity	8,538	57,224	61,681
Debt-to-assets ratio(1)	72.6%	39.0%	42.2%
Debt-to-equity ratio(2)	265.4%	63.9%	73.1%

Notes:

(1) Debt-to-assets = (Long-term interest-bearing debts + Short-term interest-bearing debts + Minority interests)/(Long-term interest-bearing debts + Short-term interest-bearing debts + Minority interests + Shareholders' equity)

(2) Debt-to-equity = (Long-term interest-bearing debts + Short-term interest-bearing debts + Minority interests)/Shareholders' equity

We have always emphasized the optimization of our capital structure and enhanced risk management. In order to ensure appropriate levels of financial flexibility and healthy financial conditions, we optimized our debt-equity ratio and our debt structure through the flexible utilization of domestic and international financing channels. Our efforts also provided a reliable basis for our network expansion and business development.

Using our debt management capabilities, we increased our leverage in 2001. Outstanding short-term and long-term bank loans, all of which are RMB-denominated, fixed-interest rate loans, rose from RMB35.65 billion at the end of 2000 to RMB44.27 billion at the end of 2001. The debt to assets ratio and the debt to equity ratio were 42.2% and 73.1%, respectively, at the end of 2001, compared with 39.0% and 63.9%, respectively, at the end of 2000.

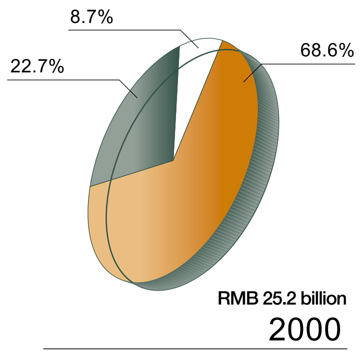
As of the end of 2001, we had RMB18.41 billion in cash and cash equivalents and RMB24.92 billion in short-term bank deposits. Our net liabilities, after cash and cash equivalents and short-term bank deposits, amounted to RMB1.76 billion.

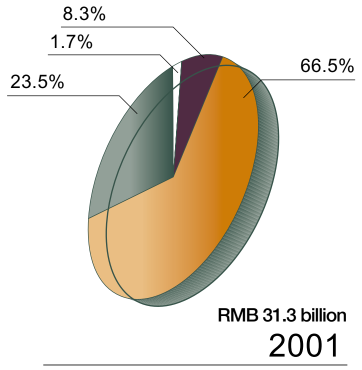
Our working capital was RMB21.04 billion at the end of 2001, RMB9.25 billion less than the RMB30.29 billion at the end of 2000. The main factor for the decrease in working capital is the increase in capital expenditures for network expansion.

VI. CAPITAL EXPENDITURE

The following table sets forth the capital expenditure in each business segment for 1999, 2000 and 2001 and the anticipated capital expenditure for 2002.

	1999 RMB in billion	2000 RMB in billion	2001 RMB in billion	2002 RMB in billion
Cellular Business	8.29	17.28	20.78	7.88
Paging Business	3.02	2.19	0.55	0.45
Long Distance, Data and Internet Business	1.39	5.71	7.33	8.5
Others	—	—	2.59	4.89
TOTAL	12.70	25.18	31.25	21.72





Capital Expenditure

- Cellular
- Long Distance, Data and Internet
- Paging
- Others

Working from a system of shared network infrastructure in 2001, we tightened our comprehensive management and control of projected capital expenditures and projects with an increased emphasis on accountability for capital expenditures in order to lower unit construction cost. At the same time, we also effectively reduced capital expenditures by actively enhancing our spectrum utilization rates, for example through network optimization and traffic adjustment. Decreases in the telecommunications equipment prices have also provided additional room for cost saving in project investments.

The annual capital expenditure for our various businesses totaled RMB31.25 billion, of which the portion attributed to the Cellular Business amounted to RMB20.78 billion. Our cellular expenditure was used mainly for the build-out of a more rational structure with higher coverage GSM network. Capital expenditure for the Long Distance, Data and Internet Business totaled RMB7.33 billion, which was mainly for the establishment of long distance switch center in the provincial capitals and the coverage of 300 local networks. In the Data Business, our expenditures concentrated on the construction of the broadband, high speed and integrated carrier data backbone and local transmission and access facilities. As for the Internet Business, the construction of Internet access points, data centers and portals was the main focus. Capital expenditure for the Paging Business was RMB0.55 billion, which was mainly used to upgrade existing networks and develop new technology and services. RMB2.59 billion was used for other projects, such as billing, customer service and information systems, operation maintenance and research and development.

Projected capital expenditure for 2002 is RMB21.72 billion. We will further improve our investment structure. Focus will be placed on enhancing our existing network coverage, strengthening work on optimization and depth. At the same time, a certain level of investment will be maintained for network infrastructure improvements, such as trunk line transmission, local transmission and access network. Investment will also be made in the development and implementation of supporting systems, such as billing, customer service and information systems, and appropriate technology unique to us to better enable us to exploit our competitive advantages. We principally rely on cash generated by operations, capital market financings and appropriate bank loans for our capital expenditure needs.

Virtually all of our revenue and expenses are denominated in Renminbi; however, a small portion of our telecommunications equipment purchases is denominated in foreign exchange. In the future, if the Renminbi exchange rate fluctuates, our equipment purchase expenditures may also change, thus affecting our operating expenses and profitability.

VII. PRINCIPAL ACCOUNTING ESTIMATE AND ACCOUNTING POLICIES

Impairment of assets for paging business

As of each year end, we conduct a full review of our property, plant and equipment and intangible assets, and provide a reasonable and prudent estimate on the amount of impairment loss of each asset whenever events or circumstances indicate that the carrying amount of assets may not be recoverable. To the extent that the estimated recoverable amount of an asset is lower than its carrying amount, an impairment loss is recognized.

In 2001, our Paging Business in certain provinces experienced a decline in revenue, loss of customers and incurred an operating loss. As a result, the carrying amounts of assets (including telecommunications equipment and goodwill related to the business) of these Paging Business exceeded their values in use, and provision for impairment loss of these assets has been made accordingly to properly reflect their recoverable values. Value in use is determined by us based on the expected discounted future net cash flows generated from the continuing use of these paging assets, and recognize an impairment loss for the amount not recoverable. In estimating the discounted future net cash flows, we have made key assumptions and estimations on the appropriate discount rate adopted and the period covered by the cash flow forecast, the gradual slow-down in the future loss of customers, the expected stability in average revenue per subscriber, the effects of incremental cash flows arising from new paging businesses and the adoption of cost reduction plans. These assumptions and estimation are made after considering the historical trends, the current market changes and the physical condition of the related assets, reasonably reflecting the risks involved. Based on the above, we recorded impairment losses of assets for the year ended 31 December 2001 amounting to approximately RMB0.63 billion.

Since our estimates are made based on certain assumptions described above, the actual positions may differ from these assumptions. If these assumptions and estimates change significantly in the future, we may need to make additional impairment provisions accordingly.

Provision for doubtful debts

Accounts receivables are stated at cost less provision for doubtful debts. Provision for doubtful debts is initially estimated through ascertaining specific accounts where there are indications that the receivable may be doubtful or cannot be collectible and after an estimate of the corresponding probability of non-recovery, a specific provision would be recorded. For the remaining receivable balances as of balance sheet date, we make a general provision based on the aging pattern and by applying reasonable percentages to the outstanding receivables. We determine such estimates based on experience, subscriber creditability and collection trends. Since the Paging Business mainly collect fees in advance and only limited revenue is collected from sales agents, 100% provision is made for receivables from sales agents aged over one month. For other telecommunications services, 100% provision is made for receivables aged over 3 months.

We make such estimates based on historical experience, subscriber creditability and collection trends. If circumstances change (e.g., business development or external market environment) in the future, we will continuously review the policy for provision for doubtful debts, and make reasonable estimates.

Accounting for income taxes

Income tax is provided based on the income before tax for statutory financial reporting purposes, adjusted for income and expense items, which are not assessable or deductible for tax purposes and taking into consideration all the tax preferential treatment.

Deferred taxation is provided under the liability method, at the current tax rate, in respect of temporary differences between income as computed for taxation purposes and income as stated in the income statement, except where it is considered probable that no liability will arise or no asset will crystallize in the foreseeable future. A deferred tax asset is not recognized unless the related benefits are expected to crystallize in the foreseeable future.

In the preparation of our financial statements, we are required to estimate our income taxes in accordance with the prevailing tax rules and regulations in each locations or jurisdictions in which the Company and its subsidiaries operate. This process involves an estimation made by us about our current tax exposure together with the assessment of temporary differences resulting from different treatment of items for tax and accounting purposes in order to determine the amount of tax provisions for the period. Major deferred tax components include interest on loans from CCF joint ventures, income tax on advances from subscribers and prepaid telephone cards, impairment provisions for plant, property and equipment and other long-lived assets, provision for doubtful debts and write-down for inventory to net realizable value, additional depreciation deductible for tax purpose. Owing to the effects of these temporary differences on income tax, we have recorded deferred tax assets amounting to RMB1.58 billion, RMB1.01 billion and RMB0.5 billion as of 31 December 2001, 2000 and 1999, respectively. Deferred tax assets are recognized based on management estimates, to the extent that they will be recovered from future taxable income from continuing operations in the foreseeable future.

We believe that the Group has recorded adequate current and deferred taxes based on prevailing tax rules and regulations and represents the best estimates for the present circumstance. In the event that future tax rules and regulations or circumstances change, additional adjustments on the current and deferred taxes may be necessary.

The directors (the "Directors") of China Unicom Limited (the "Company") are pleased to present their report together with the audited financial statements of the Company and the subsidiaries (the "Group") for the year ended 31 December 2001.

PRINCIPAL ACTIVITIES

The principal activities of the Company is investment holding and its subsidiaries are principally engaged in the provision of Cellular, Long Distance, Data, Internet and Paging services in China.

RESULTS AND APPROPRIATION

The results of the Group for the year ended 31 December 2001 are set out in pages 67 and 68 of the financial statements.

The Board of Directors considers that, with the current rapid growth in the business of the Group, a large amount of funds will be required for network expansion and other capital investments. As such, the Board of Directors does not recommend the payment of a final dividend for the year ended 31 December 2001.

SUMMARY OF FINANCIAL INFORMATION

Please refer to the Financial Summary on pages 141 and 142 for a summary of the operating results, assets and liabilities of the Group for the five years ended 31 December 2001.

LOANS

Please refer to Notes 27 and 28 to the financial statements for details of the bank loans of the Group as of 31 December 2001.

CAPITALISED INTEREST

Please refer to Note 6 to the financial statements for details of the Group's capitalized interest for the year ended 31 December 2001.

FIXED ASSETS

Please refer to Note 20 to the financial statements for changes in the fixed assets of the Group and the Company for the year ended 31 December 2001.

DESIGNATED DEPOSITS AND OVERDUE FIXED DEPOSITS

As of 31 December 2001, the Company did not have any designated deposit or any overdue fixed deposit in financial institutions or any other units.

RESERVES

Please refer to page 75 of the financial statements for the movements in the reserves of the Group for the year ended 31 December 2001.

DONATIONS

For the year ended 31 December 2001, the Group made charitable and other donations totalling RMB9,200,348.

SUBSIDIARIES AND ASSOCIATED COMPANIES

Please refer to Note 24 and 25 to the financial statements for the details of the Company's subsidiaries and the Group's associated companies as of 31 December 2001.

CHANGES IN SHAREHOLDERS' EQUITY

Please refer to page 75 of the financial statements on the Statement of Changes in Shareholders' Equity.

HOUSING BENEFITS

Please refer to Note 13 to the financial statements for the details of the housing benefits of the Group.

RETIREMENT BENEFITS

Please refer to Note 12 to the financial statements for the details of the retirement benefits of the Group.

PRE-EMPTIVE RIGHTS

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

MAJOR SUPPLIERS AND CUSTOMERS

The Group's sales to the five largest customers did not exceed 30% of the Group's total turnover for the year ended 31 December 2001.

Purchases from the largest supplier for the year ended 31 December 2001 represented approximately 17% of the Group's total purchase. The total purchases attributable to the five largest suppliers of the Group for the year ended 31 December 2001 accounted for approximately 49% of the total purchases of the Group for year 2001.

None of the Directors or their respective associates (as defined in the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules")) or any shareholder of the Company (which to the knowledge of the Directors owns more than 5% of the Company's share capital) had any interests in the five largest suppliers of the Group for the year ended 31 December 2001.

CONNECTED TRANSACTIONS

The independent non-executive Directors confirmed that all connected transactions in year 2001 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 its business;

2. had been entered into either (a) on normal commercial terms, or (b) if there are not sufficient comparable transactions to judge whether they are on normal commercial terms, on terms that are no less favourable than terms available to or from (as appropriate) independent third parties; and

3. had been entered into in accordance with the relevant agreements governing such transactions on terms that are fair and reasonable and in the interests of our shareholders as a whole.

The independent non-executive Directors further confirm that:

1. the aggregate annual value of the lease of the Group's head office in Beijing from Unicom Xingye Science and Technology Trade Co. Ltd (the "Beijing Lease") has not exceeded the cap of RMB15.2 million ("Cap A"); and

2. the aggregate annual value of the rental charges for premises, equipment and facilities between the Group and China United Telecommunications Corporation, excluding the Beijing Lease (the "Mutual Provision of Premises"), had not exceeded the cap of RMB650 million ("Cap B").

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

(a) the transactions have received the approval of the Directors;

(b) the transactions were entered into in accordance with the pricing policies of the Company as stipulated in the relevant agreements governing such transactions;

(c) the transactions were entered into in accordance with the terms of the relevant agreements governing such transactions; and

(d) the Beijing Lease and the Mutual Provision of Premises have not exceeded Cap A and Cap B, respectively.

Please refer to Note 33 to the financial statements for a summary of the connected transactions for the year ended 31 December 2001.

SHARE CAPITAL AND SHARE OPTION SCHEME

Please refer to Note 30 to the financial statements for the details of the increase in the share capital of the Company for the year ended 31 December 2001.

On 1 June 2000, the Company adopted a share option scheme (the "Share Option Scheme") for the purpose of providing incentives and rewards to employees who have made contributions to the development of the Company. Under the terms of the Share Option Scheme, the Directors 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 up to a maximum aggregate number of shares (including those that could be subscribed for under the pre-global offering share option scheme, the particulars of which are described later in this section) equal to 10% of the total issued share capital of the Company. The Share Option Scheme became effective on 22 June 2000, and unless otherwise cancelled or amended, will remain in force for 10 years from that date. No option shall be granted to any employee such that the total number of shares issued and to be issued upon exercise of options granted to such employee exceeds 25% of the aggregate number of shares issued and issuable under the Share Option Scheme. According to the Share Option Scheme, the consideration payable by a participant for the grant of options will be HK$1.00. The price of a share payable by a participant upon the exercise of an option will be determined by the Directors at their discretion at the date of grant, except 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 prices of shares on The Stock Exchange of Hong Kong Limited (the "Stock Exchange") on the five trading days immediately preceding the date of grant of the option on which there were dealings in the shares on the Stock Exchange.

The period during which an option may be exercised will be determined by the directors at their discretion, except that no option may be exercised later than 10 year from 22 June 2000. On 30 June 2001, the Company granted 6,724,000 share options under the Share Option Scheme to its employees which represent, on their full exercise, 6,724,000 shares of the Company with the following terms:

(i) the price of a share payable by a participant upon the exercise of an option shall be HK$15.42 (excluding the brokerage fee and Stock Exchange transaction levy); and

(ii) the period during which an option may be exercised commences from the date of grant of the options and will end by 22 June 2010.

The closing price of the Shares on the Stock Exchange was HK$13.6 on 29 June 2001.

As of 31 December 2001, the Company had granted 6,724,000 share options under the Share Option Scheme.

The terms stated above reflect the terms of the Share Option Scheme as adopted by the shareholders on 1 June 2000. The amendments to the relevant provisions of the Listing Rules regarding the requirements of share option schemes of a Hong Kong listed company came into effect on 1 September 2001. The Company must comply with the new provisions of the Listing Rules if it wishes to grant any options after 1 September 2001.

On 1 June 2000, the Company also adopted a pre-global offering share option scheme (the "Pre-Global Offering Share Option Scheme"), the principal terms of which are the same as the Share Option Scheme in all material respects except that:

(i) on 22 June 2000, 27,116,600 options have been granted under the scheme of which 2,107,000 options have been granted to the directors. Please refer to the section headed "Directors" Interest in and right to acquire shares". Such options, on their full exercise, represent 27,116,600 shares of the Company;

(ii) the price of a share payable by a participant upon the exercise of an option shall be HK$15.42 (excluding the brokerage fee and Stock Exchange transaction levy); and

(iii) the period during which an option may be exercised commences two years from the date of grant of the options and will end no later than 10 year from 22 June 2000.

The maximum number of Shares in respect of which options can be granted under the Pre-Global Offering Share Option Scheme shall not exceed 27,116,600. No further options can be granted under this scheme.

The financial impact of share options granted is not recorded in the Company's or the Group's balance sheet until such time as the options are exercised, and no charge is recorded in the income statement account or balance sheet for their cost. Upon the exercise of the share options, the resulting shares issued are recorded by the Company as additional share capital at the nominal value of the shares, and the excess of the exercise price per share over the nominal value of the shares is recorded by the Company in the share premium account. Options which are cancelled prior to their exercise date are deleted from the register of outstanding options.

In respect of disclosure of value of options granted, please refer to Additional Financial Information for North American Shareholders as set out on page 140.

The Company has proposed to amend its Share Option Scheme to comply with the new Listing Rules Requirements and to create a more favourable scheme to attract and retain key personnel. In order to synchronise the administration of the options granted under the Share Option Scheme and Pre-Global Offering Share Option Scheme, the Company also proposes to amend the Pre-Global Offering Share Option Scheme to reflect some of the changes proposed to be made to the Share Option Scheme.

The details of the share options granted to the Directors are set out in "Directors' interest in and right to acquire shares".

Please also refer to Note 31 to the financial statements for the description of the respective share option schemes.

WARRANTS

The Company has issued 26 warrants certificates representing 312,966,836 underlying shares of the Company for the year ended 31 December 2000, which would constitute approximately 2.5% of the issued share capital of the Company, to a total of 24 holders. The warrants may be exercised at any time commencing at 9:00 a.m. on 23 December 2000 and ending at 5:00 p.m. on 22 June 2001. The number of shares that the warrant holder may subscribe is determined by dividing the warrants' aggregate exercise price by HK$15.58.

Up to the expiry date on 22 June 2001 at 5:00 afternoon, all outstanding 26 warrants certificates representing 312,966,836 underlying shares of the Company issued by the Company had not been exercised. As at 31 December 2001, there were no warrants outstanding.

Please refer to Note 32 to the financial statements for further details on the warrants.

PURCHASE, SALE OR REDEMPTION OF SHARES

For the year ended 31 December 2001, neither the Company nor its subsidiaries has purchased, sold or redeemed any of the Company's listed shares.

SUBSTANTIAL INTERESTS IN THE SHARE CAPITAL OF THE COMPANY

The Company has been notified of the following interests in the Company's issued shares as of 31 December 2001 amounting to 10% or more of the ordinary shares in issue:

	Ordinary shares held directly	Ordinary shares held Indirectly	Percentage of Total issued Shares
(i) China United Telecommunications Corporation ("Unicom Group")	—	9,725,000,020	77.47%
(ii) China Unicom (BVI) Limited ("China Unicom (BVI)")	9,725,000,020	—	77.47%

Note: Because of the fact that Unicom Group directly control one-third or more of the voting rights in the shareholders' meetings of China Unicom (BVI), in accordance with the Securities (Disclosure of Interests) Ordinance, the interests of China Unicom (BVI) are deemed to be, and have therefore been included in, the interests of Unicom Group.

Apart from the foregoing, no person or corporation had any interest in the share capital of the Company as recorded in the register required to be kept under section 16(1) of the Securities (Disclosure of Interests) Ordinance as having an interest in 10% or more of the issued share capital of the Company.

Please also refer to Note 30 to the financial statements for the shareholding position of the Company's shares as of 31 December 2001.

DIRECTORS AND SENIOR MANAGEMENT OF THE COMPANY

The following table sets forth certain information concerning the Directors and senior management of the Company.

Name	Age	Position in the Company	Original Appointment Date	Re-appointment Date
Yang Xian Zu	62	Executive Director Chairman, Chief Executive Officer	20 April 2000 28 May 2000	
Wang Jianzhou	53	Executive Director President	20 April 2000 28 May 2000	
Shi Cuiming	62	Executive Director Executive Vice President	20 April 2000 28 May 2000	21 June 2001
Li Zhengmao	39	Executive Director Vice President	20 April 2000 28 May 2000	21 June 2001
Tan Xinghui	40	Executive Director and Vice President	7 September 2000	21 June 2001
Ge Lei	61	Non-Executive Director	20 April 2000	21 June 2001
Craig O. McCaw	52	Non-Executive Director	24 May 2000	
Lee Hon Chiu	73	Independent Non-Executive Director	20 April 2000	
Wu Jing Lian	72	Independent Non-Executive Director	20 April 2000	
C. James Judson	57	Alternate Director to Craig O. McCaw	14 March 2001	
Liu Yunjie	59	Vice President	28 May 2000	

In accordance with Article 97 of the Articles of Association, Messrs. Wang Jianzhou, Lee Hon Chiu and Wu Jinglian will retire by rotation at the forthcoming annual general meeting of the Company and being eligible, offer themselves for re-election.

In accordance with Article 101 of the Articles of Association, Mr Tan Xinghui will retire at the forthcoming annual general meeting of the Company and being eligible, offer himself for re-election.

DIRECTORS' INTEREST IN AND RIGHT TO ACQUIRE SHARES

As of 31 December 2001, the interests of the directors and the chief executive of the Company in the equity securities of the Company or any of its associated corporations as defined in the Securities (Disclosure of Interests) Ordinance (the "Ordinance") as recorded in the register required to be kept under Section 29 of the Ordinance were as follows:

Name of Directors	Personal Interest
Shi Cuiming	30,000 Ordinary Shares
Li Zhengmao	20,000 Ordinary Shares
Tan Xinghui	20,000 Ordinary Shares
C. James Judson (an alternate director to Craig O. McCaw)	1,000 American Depositary Shares[1]

[1] One American Depositary Shares represents 10 ordinary shares of HK$0.1 each of the Company.

As of 31 December 2001, the Directors and the chief executive of the Company had share options granted pursuant to the Pre-Global Offering Share Option Scheme to the Directors and chief executive to subscribe for shares of the Company. Further details of the above are set out as follow:

Name of directors	No. of options granted[2]	No. of options exercised during the year	No. of options outstanding at year end
Yang Xian Zu	525,000	—	525,000
Wang Jianzhou	396,200	—	396,200
Shi Cuiming	396,200	—	396,200
Li Zhengmao	292,600	—	292,600
Ge Lei	292,600	—	292,600
Tan Xinghui	204,400	—	204,400

[2] Each option gives the holder the right to subscribe for one share.

Apart from the foregoing, at no time during year 2001 was the Company, or any of its holding companies or subsidiaries or subsidiaries of the Company's holding companies, a party to any arrangement to enable the Directors or any of their spouses of children under eighteen years of age to acquire benefits by means of the acquisition of shares in or debentures of the Company or any other body corporate.

Furthermore, apart from the foregoing, as at 31 December 2001, none of the Directors had any personal, family, corporate or other interests in the securities of the Company or any of its associated corporations as defined in the Ordinance.

DIRECTORS' INTEREST IN CONTRACTS AND SERVICE CONTRACTS

Each of the existing executive Directors entered into a service contract with the Company for a term of three years.

Save as the service contracts mentioned above, for the year ended 31 December 2001, the Directors did not have any material interests, whether directly or indirectly, in any contracts of significance entered into by the Company, any of its holding companies or subsidiaries or subsidiaries of the Company's holding companies.

None of those Directors proposed for re-election at the forthcoming annual general meeting has an unexpired service contract which is not terminable by the Company within one year without payment compensation (other than statutory compensation).

EMOLUMENTS OF THE DIRECTORS AND SENIOR MANAGEMENT

Please refer to Note 9 of the financial statements for the details of the emoluments of the Directors and senior management of the Company.

MAJOR EVENTS AND CONTRACTS OF SIGNIFICANCE

On 22 November 2001, the Company's wholly subsidiary, China Unicom Corporation Limited entered into a lease with the wholly owned subsidiary of China United Telecommunications Corporations, Unicom New Horizon Mobile Telecommunications Company Limited in respect of leasing CDMA network capacity in the 9 provinces and 3 municipalities of Guangdong, Jiangsu, Zhejiang, Fujian, Liaoning, Shandong, Anhui, Hebei, Hubei, Beijing, Shanghai and Tianjin. Other than the above, there is no major event or contract of significance entered into by the Group for the year ended 31 December 2001.

Please refer to Note 33(d) of the financial statements for the details of the CDMA network capacity leasing.

COMPLIANCE WITH CODE OF BEST PRACTICE

The Company has complied throughout the year of 2001 with the Code of Best Practice as set out by the Stock Exchange in Appendix 14 to the Listing Rules except that the non-executive Directors were not appointed for a specific term but are subject to retirement by rotation and re-election at the Company's annual general meeting in accordance with the Articles of Association.

USE OF PROCEEDS

For the year ended 31 December 2001, the Group has used approximately RMB 14.6 billion of its net listing proceeds for repayment of loans which were borrowed to finance the network expansion and upgrade in 2001. The remaining net listing proceeds is deposited into interest bearing accounts.

MATERIAL LEGAL PROCEEDINGS

As of 31 December 2001, the Company was not involved in any material litigation or arbitration and no material litigation or claims was pending or threatened or made against the Company as far as the Company is aware of.

AUDITORS

Arthur Andersen & Co. was appointed as the auditors of the Company for the year ended 31 December 2001 and has audited the accompanying financial statements. The Directors will, at the forthcoming annual general meeting of the Company, to recommend to its shareholders to appoint one of the biggest five international accounting firms other than Arthur Andersen & Co. as the Company's auditors for the year ending 31 December 2002. The Directors will notify its shareholders of the name of a proposed international accounting firm by way of a public announcement in due course, which will be submitted to its shareholders at the meeting for voting under the resolution for appointment of the auditors of the Company for the ensuing year.

By Order of the Board
Yang Xian Zu
Chairman

Hong Kong, 27 March 2002

Notice of Annual General Meeting

Notice is hereby given that the Annual General Meeting of China Unicom Limited will be held on 13 May 2002 at 10:30 a.m. in Island Shangri-la Hotel, Ballroom C, 5/F, Pacific Place, Supreme Court Road, Hong Kong for the following purposes:

As Ordinary Business:

1. To receive and consider the financial statements and the Reports of the Directors and of the Auditors for the period ended 31 December 2001.

2. To re-elect the Directors and fix their fees.

3. To appoint Auditors, and to authorise the Directors to fix their remuneration for the year ending 31 December 2002.

And as Special Business, to consider and, if thought fit, to pass the following as ordinary resolutions:

ORDINARY RESOLUTIONS

4. **"THAT:**

(a) subject to paragraphs (b) and (c) below, the exercise by the Directors during the Relevant Period (as hereinafter defined) of all the powers of the Company to purchase shares of HK$0.10 each in the capital of the Company including any form of depositary receipts representing the right to receive such shares ("Shares") on The Stock Exchange of Hong Kong Limited (the "Stock Exchange") or any other stock exchange recognised for this purpose by the Securities and Futures Commission of Hong Kong and the Stock Exchange in accordance with all applicable laws including the Hong Kong Code on Share Repurchases and the Rules Governing the Listing of Securities on the Stock Exchange as amended from time to time be and is hereby generally and unconditionally approved;

(b) the aggregate nominal amount of Shares which may be purchased or agreed conditionally or unconditionally to be purchased by the Directors pursuant to the approval in paragraph (a) above shall not exceed 10 per cent. of the aggregate nominal amount of the share capital of the Company in issue at the date of passing this Resolution, and the said approval shall be limited accordingly;

(c) for the purpose of this Resolution:

"Relevant Period" means the period from the passing of this Resolution until the earlier of:

(i) the conclusion of the next annual general meeting of the Company;

(ii) the expiry of the period within which the next annual general meeting of the Company is required by the Company's articles of association (the "Articles of Association") or the Companies Ordinance to be held; and

(iii) the revocation or variation of the authority given to the Directors under this Resolution by ordinary resolution of the Company's shareholders in general meeting."

5. **"THAT:**

(a) subject to paragraph (c) below, the exercise by the Directors during the Relevant Period (as hereinafter defined) of all the powers of the Company to allot, issue and deal with additional Shares and to make or grant offers, agreements and options which might require the exercise of such powers be and are hereby generally and unconditionally approved;

(b) the approval in paragraph (a) shall authorize the Directors during the Relevant Period to make or grant offers, agreements and options which might require the exercise of such powers after the end of the Relevant Period;

(c) the aggregate nominal amount of share capital allotted, issued and dealt with or agreed conditionally or unconditionally to be allotted, issued and dealt with (whether pursuant to an option or otherwise) by the Directors pursuant to the approval in paragraph (a), otherwise than pursuant to (i) a Rights Issue (as hereinafter defined), (ii) the exercise of options granted under any share option scheme adopted by the Company or (iii) any scrip dividend or similar arrangement providing for the allotment of Shares in lieu of the whole or part of a dividend on Shares in accordance with the Articles of Association, shall not exceed the aggregate of (aa) 20 per cent. of the aggregate nominal amount of the share capital of the Company in issue at the date of passing this Resolution, plus (bb) (if the Directors are so authorised by a separate ordinary resolution of the shareholders of the Company) the aggregate nominal amount of share capital of the Company repurchased by the Company subsequent to the passing of this Resolution (up to maximum equivalent to 10 per cent. of the aggregate nominal amount of the share capital of the Company in issue at the date of passing this Resolution), and the said approval shall be limited accordingly; and

(d) for the purpose of this Resolution:

"Relevant Period" means the period from the passing of this Resolution until the earlier of:

(i) the conclusion of the next annual general meeting of the Company;

(ii) the expiry of the period within which the next annual general meeting of the Company is required by the Articles of Association or the Companies Ordinance to be held; and

(iii) the revocation or variation of the authority given to the Directors under this Resolution by ordinary resolution of the Company's shareholders in general meeting; and

"Right Issue" means on offer of shares open for a period fixed by the Directors to holders of Shares on the register of members on a fixed record date in proportion to their then holdings of such Shares (subject to such exclusion or other arrangements as the Directors may deem necessary or expedient in relation to fractional entitlements or having regard to any legal or practical restrictions or obligations under the laws of, or the requirements of, any recognised regulatory body or any stock exchange in any territory applicable to the Company) and an offer, allotment or issue of shares by way of rights shall be construed accordingly."

6. "**THAT** the Directors be and are hereby authorised to exercise the powers of the Company referred to in paragraph (a) of Resolution 5 in respect of the share capital of the Company referred to in sub-paragraph (bb) of paragraph (c) of such resolution."

By order of the Board
Ngai Wai Fung
Company Secretary

Hong Kong, 27 March 2002

Notes:

1. Any member entitled to attend and vote at the above meeting is entitled to appoint one or more proxies to attend and, on a poll, vote in his stead. A proxy need not be a member of the Company.

2. In order to be valid, a form of proxy together with the power of attorney or other authority (if any) under which it is signed, or a notarially certified copy thereof, must be deposited at the Company's registered office at 75/F., The Center, 99 Queen's Road Central, Hong Kong at least 48 hours before the time for holding the above Meeting. Completion and return of a form of proxy will not preclude a member from attending and voting in person if he is subsequently able to be present.

3. In relation to the appointment of the Auditors, please refer to the Report of the Directors contained in the annual report of the Company to be despatched to the shareholders of the Company.

4. In relation to the Ordinary Resolution set out in item 4 of the Notice, the Directors wish to state that they will exercise the powers conferred thereby to repurchase Shares in circumstances which they deem appropriate or for the benefit of the shareholders. The Explanatory Statement containing the information necessary to enable the shareholders to make an informed decision on whether to vote for or against the resolution to approve the repurchase by the Company of its own Shares, as required by the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules"), will be set out in a separate letter from the Company to be enclosed with the 2001 annual report.

Financial Section

ANDERSEN

Arthur Andersen & Co
21st Floor Edinburgh Tower
The Landmark
15 Queen's Road Central
Hong Kong

TO THE SHAREHOLDERS OF CHINA UNICOM LIMITED

(Incorporated in Hong Kong with limited liability)

We have audited the financial statements of China Unicom Limited (the "Company") and its subsidiaries (the "Group") on pages 67 to 131 which have been prepared in accordance with accounting principles generally accepted in Hong Kong.

Respective responsibilities of directors and auditors

The Companies Ordinance requires the directors to prepare financial statements which give a true and fair view. In preparing financial statements which give a true and fair view it is fundamental that appropriate accounting policies are selected and applied consistently.

It is our responsibility to form an independent opinion, based on our audit, on those statements and to report our opinion to you.

Basis of opinion

We conducted our audit in accordance with Statements of Auditing Standards issued by the Hong Kong Society of Accountants. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgments made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Company's and the Group's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance as to whether the financial statements are free from material misstatement. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements. We believe that our audit provides a reasonable basis for our opinion.

Opinion

In our opinion the financial statements give a true and fair view of the state of affairs of the Company and of the Group as of 31 December 2001 and of the Group's profit and cash flows for the year then ended and have been properly prepared in accordance with the Companies Ordinance.

Arthur Andersen & Co
Certified Public Accountants

Hong Kong, 27 March 2002

Consolidated Income Statement

For the Year Ended 31 December 2001

(Expressed in thousands of Renminbi ("RMB"), except per share data and number of shares)

	Note	Year ended 31 December 2001	2000
Revenue:			
Cellular Business		20,505,058	12,187,804
Paging Business		4,341,824	8,483,490
Long Distance, Data and Internet Business		3,308,944	1,096,394
Total service revenue		28,155,826	21,767,688
Sales of telecommunications products		1,237,060	1,924,770
Total revenue	4	29,392,886	23,692,458
Operating expenses:			
Leased lines		(853,306)	(1,158,123)
Interconnection charges		(2,072,584)	(1,379,465)
Depreciation and amortisation		(8,262,296)	(5,734,315)
Personnel		(2,487,218)	(1,769,840)
Selling and marketing		(3,612,890)	(2,492,433)
General, administrative and other expenses	7 (iv)	(5,498,997)	(3,743,063)
Cost of telecommunications products sold		(1,342,244)	(2,192,938)
Total operating expenses	7	(24,129,535)	(18,470,177)
Operating income		5,263,351	5,222,281
Financial income	5	2,096,972	1,748,805
Financial expense	6	(1,917,566)	(1,353,746)
Loss arising from terminations of CCF Arrangements	11	—	(1,193,838)
Other income, net	8	19,831	59,229
Income before taxation and minority interests	6	5,462,588	4,482,731
Taxation	10	(1,041,137)	(1,104,969)
Income before minority interests		4,421,451	3,377,762
Minority interests		35,310	(143,711)
Net income		4,456,761	3,234,051

Consolidated Income Statement

For the Year Ended 31 December 2001

(Expressed in thousands of Renminbi ("RMB"), except per share data and number of shares)

	Note	Year ended 31 December 2001	2000
Basic net income per share (RMB)	15	**0.36**	0.29
Diluted net income per share (RMB)	15	**0.36**	0.29
Number of shares outstanding for basic net income (in thousand)	15	**12,552,996**	11,208,224
Number of shares outstanding for diluted net income (in thousand)	15	**12,552,996**	11,219,679
Basic net income per ADS (RMB)	15	**3.55**	2.89
Diluted net income per ADS (RMB)	15	**3.55**	2.88
Number of ADS outstanding for basic net income (in thousand)	15	**1,255,300**	1,120,822
Number of ADS outstanding for diluted net income (in thousand)	15	**1,255,300**	1,121,968

Consolidated Statement of Recognised Gains and Losses

For the Year Ended 31 December 2001

(Expressed in thousands of RMB)

	Note	Year ended 31 December 2001	2000
Surplus on revaluation of land use rights and buildings	20	**—**	176,853
Net gains not recognised in the income statement		**—**	176,853
Net income for the year		**4,456,761**	3,234,051
Total recognised gains		**4,456,761**	3,410,904

Consolidated Balance Sheet

As of 31 December 2001

(Expressed in thousands of RMB)

	Note	As of 31 December 2001	As of 31 December 2000
ASSETS			
Current assets:			
Cash and cash equivalents		**18,413,010**	44,716,685
Short-term bank deposits		**24,921,943**	7,838,935
Trading securities	16	**203,832**	373,405
Accounts receivable, net	17	**2,498,063**	1,545,051
Inventories	18	**751,991**	679,689
Prepayments and other current assets	19	**969,561**	1,665,661
Amounts due from China Telecom	34(b)	**199,460**	376,246
Amounts due from related parties	33(c)	**1,430,818**	539,321
Current portion of deferred tax assets	10	**569,192**	19,642
Total current assets		**49,957,870**	57,754,635
Non-current assets:			
Property, plant and equipment, net	20	**75,748,435**	52,863,637
Goodwill	21	**43,287**	295,962
Deferred expenditures	22	**1,015,438**	805,869
Deferred tax assets	10	**1,012,216**	994,078
Investment securities	23	**123,500**	88,945
Investment in associated companies	25	**4,146**	25,700
Total assets		**127,904,892**	112,828,826
LIABILITIES AND EQUITY			
Current liabilities:			
Payables and accrued liabilities	26	**15,329,436**	12,521,167
Short-term bank loans	27	**7,089,000**	7,733,817
Advances from customers		**2,765,541**	2,615,676
Taxes payable		**1,025,269**	1,618,863
Current portion of long-term bank loans	28	**843,603**	766,875
Current portion of obligations under finance leases	29, 34(b)	**8,151**	—
Amounts due to Unicom Group	33(e)	**947,934**	821,797
Amounts due to China Telecom	34(b)	**742,366**	1,276,965
Amounts due to related parties	33(c)	**135,724**	53,153
Dividends payable		**29,847**	59,224
Total current liabilities		**28,916,871**	27,467,537

	Note	As of 31 December 2001	As of 31 December 2000
Long-term liabilities:			
Long-term bank loans	28	**36,336,768**	27,151,349
Obligations under finance leases	29, 34(b)	**100,757**	—
Other long-term liabilities		**39,928**	102,286
Total liabilities		**65,394,324**	54,721,172
Minority interests		**829,405**	883,252
Capital and reserves:			
Share capital	30	**1,331,371**	1,331,371
Share premium		**52,482,127**	52,482,127
Reserves		**826,286**	601,658
Retained profits		**7,041,379**	2,809,246
Shareholders' equity		**61,681,163**	57,224,402
Total liabilities and equity		**127,904,892**	112,828,826

Approved by the Board of Directors on 27 March 2002 and signed on behalf of the Board by:

Yang Xian Zu
Director

Shi Cuiming
Director

Balance Sheet

As of 31 December 2001

(Expressed in thousands of RMB)

	Note	As of 31 December 2001	2000
ASSETS			
Current assets:			
Cash and cash equivalents		9,334,171	38,449,637
Short-term bank deposits		24,707,719	7,793,935
Prepayments and other current assets	19	170,172	669,453
Amounts due from related parties	33(c)	—	14
Total current assets		34,212,062	46,913,039
Non-current assets:			
Investment in subsidiaries	24	23,190,368	8,542,833
Property, plant and equipment, net	20	8,848	10,291
Total assets		57,411,278	55,466,163
LIABILITIES AND EQUITY			
Current liabilities:			
Payables and accrued liabilities	26	31,089	7,848
Amounts due to subsidiaries		—	59,969
Total liabilities		31,089	67,817
Capital and reserves:			
Share capital	30	1,331,371	1,331,371
Share premium		52,482,127	52,482,127
Retained profits		3,566,691	1,584,848
Shareholders' equity		57,380,189	55,398,346
Total liabilities and equity		57,411,278	55,466,163

Approved by the Board of Directors on 27 March 2002 and signed on behalf of the Board by:

Yang Xian Zu
Director

Shi Cuiming
Director

Consolidated Statement of Cash Flows

For the Year Ended 31 December 2001

(Expressed in thousands of RMB)

	Note	Year ended 31 December 2001	2000
Net cash inflows from operating activities	(a)	13,249,360	10,228,880
Returns on investments and servicing of finance			
Interest received		2,605,507	1,083,148
Interest paid		(2,576,822)	(1,331,326)
Dividends received		22,864	258
Dividends paid to minority owners of subsidiaries		(29,377)	(153,316)
Net cash inflows (outflows) from return on investments and servicing of finance		22,172	(401,236)
Taxation			
PRC income tax paid		(2,193,657)	(483,777)
Investing activities			
Purchase of property, plant and equipment		(28,547,009)	(21,352,609)
Proceeds from disposal of property, plant and equipment		131,692	—
Acquisition of minority interests		(18,537)	(1,525,536)
Purchase of investment in associated companies		—	(10,696)
Proceeds from disposal of associated companies		—	6,446
Increase in short-term bank deposits		(17,083,008)	(7,630,435)
Purchase of trading securities		—	(570,905)
Proceeds from disposal of trading securities		144,976	689,463
Purchase of investment securities		(21,426)	(10,903)
Proceeds from disposal of investment securities		5,139	—
Addition of deferred expenditures		(736,844)	(145,771)
Net cash outflows from investing activities		(46,125,017)	(30,550,946)
Net cash outflows before financing activities		(35,047,142)	(21,207,079)
Financing activities			
Proceeds from issue of ordinary shares, net of expenses		—	45,275,152
Repayment of loans from CCF joint ventures		—	(7,393,940)
Increase in amounts due to Unicom Group		126,137	316,430
Proceeds from short-term and long-term bank loans		21,243,410	23,360,879
Repayment of short-term and long-term bank loans		(12,626,080)	(1,637,118)
Net cash inflows from financing activities		8,743,467	59,921,403
(Decrease) increase in cash and cash equivalents		(26,303,675)	38,714,324
Cash and cash equivalents, beginning of year		44,716,685	6,002,361
Cash and cash equivalents, end of year		18,413,010	44,716,685

Consolidated Statement of Cash Flows

For the Year Ended 31 December 2001

(Expressed in thousands of RMB)

(a) The reconciliation of income before taxation and minority interests to net cash inflows from operating activities is as follows:

	Year ended 31 December 2001	2000
Income before taxation and minority interests	**5,462,588**	4,482,731
Adjustments for:		
Depreciation and amortisation	**8,262,296**	5,734,315
Interest income	**(2,096,972)**	(1,748,805)
Interest expense	**1,907,148**	1,353,746
Loss on disposal of property, plant and equipment	**54,475**	319,659
Provisions for impairment in value of property, plant and equipment and goodwill	**632,511**	—
Provision for doubtful debts	**540,954**	444,831
Share of losses (profits) from associated companies	**24,773**	(258)
Dividends from investment securities	**(22,864)**	(9,321)
Realised gains on trading securities	**(31,979)**	(64,956)
Unrealised losses (gains) on trading securities	**56,576**	(31,855)
Realised gains on investment securities	**(944)**	—
(Write-back) provision for impairment in value of associated companies	**(3,219)**	7,501
(Write-back) provision for impairment in value of investment securities	**(12,490)**	6,812
Loss arising from terminations of CCF Arrangements	**—**	1,193,838
Increase in accounts receivable	**(1,493,966)**	(993,069)
(Increase) decrease in inventories	**(72,302)**	54,717
Decrease (increase) in prepayments and other current assets	**187,565**	(424,133)
Decrease in amounts due from China Telecom	**176,786**	798,537
Increase in amounts due from related parties	**(891,497)**	(433,506)
Increase (decrease) in payables and accrued liabilities	**872,084**	(164,854)
Increase (decrease) in advances from customers	**149,865**	(31,970)
Decrease in amounts due to China Telecom	**(534,599)**	(276,355)
Increase in amounts due to related parties	**82,571**	11,275
Net cash inflows from operating activities	**13,249,360**	10,228,880

(b) Significant non-cash transactions:

Payables to equipment suppliers for construction-in-progress during the year ended 31 December 2001 increased by approximately RMB2,706 million (2000: RMB3,828 million).

During 2000, long-term bank loans of approximately RMB10,502 million previously borrowed by Unicom Group were restructured into long-term bank loans borrowed directly by China Unicom (See Note 33(b)).

Statement of Changes in Shareholders' Equity

For the Year Ended 31 December 2001

(Expressed in thousands of RMB)

	Head office account	Share capital	Share premium	Revaluation reserve	Statutory reserve	Retained profits	Total
Consolidated							
Balance at 1 January 2000	8,538,346	—	—	—	—	—	8,538,346
Effect of restructuring	(8,538,346)	1,030,850	7,507,496	—	—	—	—
Shareholders' equity after restructuring	—	1,030,850	7,507,496	—	—	—	8,538,346
Revaluation surplus	—	—	—	176,853	—	—	176,853
Issue of shares, net of direct listing expenses	—	300,521	44,974,631	—	—	—	45,275,152
Net income for the year	—	—	—	—	—	3,234,051	3,234,051
Appropriation to statutory reserve (Note 14)	—	—	—	—	424,805	(424,805)	—
Balance at 31 December 2000	—	1,331,371	52,482,127	176,853	424,805	2,809,246	57,224,402
Net income for the year	—	—	—	—	—	4,456,761	4,456,761
Appropriation to statutory reserve (Note 14)	—	—	—	—	224,628	(224,628)	—
Balance at 31 December 2001	—	1,331,371	52,482,127	176,853	649,433	7,041,379	61,681,163

	Share capital	Share premium	Retained profits	Total
The Company				
Effect of incorporation	1,030,850	7,507,496	—	8,538,346
Issue of shares, net of direct listing expenses	300,521	44,974,631	—	45,275,152
Net income for the year	—	—	1,584,848	1,584,848
Balance at 31 December 2000	1,331,371	52,482,127	1,584,848	55,398,346
Net income for the year	—	—	1,981,843	1,981,843
Balance at 31 December 2001	1,331,371	52,482,127	3,566,691	57,380,189

1. ORGANISATION AND PRINCIPAL ACTIVITIES

China Unicom Limited (the "Company") was incorporated in the Hong Kong Special Administrative Region ("Hong Kong"), the People's Republic of China (the "PRC") on 8 February 2000 to engage in investment holding, the provision of cellular, paging, long distance, data and Internet services in the PRC. Prior to the incorporation of the Company, the paging business was carried out by Guoxin Paging Corporation Ltd. and its subsidiaries ("Guoxin") whereas the cellular and other telecommunications businesses were carried out by the head office and various branches of China United Telecommunications Corporation ("Unicom Group"). These businesses are hereinafter collectively referred to as the "Predecessor Entities". All such businesses were transferred to the Company pursuant to a restructuring (the "Restructuring"), as described below, in preparation for a global offering of the Company's shares (the "Global Offering").

Prior to and following the Restructuring, Unicom Group and Guoxin were and are under the supervision and regulation of the Ministry of Information Industry (the "MII"). The MII is a body established in 1998 under the direct supervision of the State Council of the PRC to take over the regulatory responsibility for the telecommunications industry in the PRC from its predecessor, the Ministry of Posts and Telecommunications (the "MPT").

Unicom Group was established as a state-owned enterprise in the PRC in 1994 under the approval of the State Council to build and operate cellular networks, fixed line local networks and fixed line domestic long distance networks in the PRC.

Guoxin was a subsidiary of China Telecom and was established as a limited liability company in September 1998. China Telecom originally comprised the Directorate General of Telecommunications, Provincial Post and Telecommunications Administrations (the "PTA") and the municipal and county Post and Telecommunications Bureaus (the "PTB"). All these entities were state-owned entities established under the ownership of the government. As ministries of the government, the MPT exercised actual control over the operations of China Telecom.

Guoxin operated a nationwide paging business through its 31 subsidiaries in 27 provinces and 4 municipalities in the PRC (originally undertaken by the PTAs, hereinafter referred to as the "Paging Business"). After the establishment of Guoxin, the Paging Business continued to operate under the ultimate control of the MII, until June 1999 when, pursuant to a State Council decision, the 99.67% ownership interest in Guoxin held by China Telecom was transferred to Unicom Group at no consideration.

Under the Restructuring, Unicom Group injected its entire equity interests in Guoxin, together with the following businesses, into a limited liability company established in the PRC on 21 April 2000 under the name of China Unicom Corporation Limited ("China Unicom"):

(i) the cellular businesses in 9 provinces in the PRC, namely, Guangdong, Fujian, Anhui, Jiangsu, Zhejiang, Shandong, Liaoning, Hebei and Hubei; and 3 municipalities, namely, Beijing, Shanghai and Tianjin (originally undertaken by various branches of Unicom Group and hereinafter collectively referred to as the "Cellular Business");

1. ORGANISATION AND PRINCIPAL ACTIVITIES (Cont'd)

(ii) the nationwide domestic and international long distance telephony businesses including Internet protocol-based telephony businesses and the nationwide data and Internet business in major cities of the PRC (originally undertaken by various branches of Unicom Group, hereinafter referred to as the "Long Distance, Data and Internet Business").

By 31 December 2001, Guoxin has already acquired all of the minority interests of 28 subsidiaries and part of the minority interests of Heilongjiang Guoxin Paging Co. Ltd. ("Heilongjiang Guoxin") and Liaoning Guoxin Paging Co. Ltd. ("Liaoning Guoxin"). These 28 Paging Businesses then became the wholly-owned subsidiaries of Guoxin. In addition, Guoxin deregistered the legal entity status of 22 wholly-owned subsidiaries in 21 provinces and 1 municipality in the PRC. Minority interests only existed in Heilongjiang Guoxin, Liaoning Guoxin and Unicom Guomai Communications Co. Ltd. ("Unicom Guomai").

The Company and its subsidiaries are hereinafter referred to as the "Group".

The immediate holding company of the Company is China Unicom (BVI) Limited ("Unicom BVI"). The directors of the Company consider Unicom Group to be the ultimate parent company.

2. BASIS OF PRESENTATION

The reorganisation of Guoxin and the subsequent transfer of its ownership to Unicom Group were completed pursuant to restructuring plans for the telecommunications industry of the PRC approved by the State Council and implemented through the MII. Prior to and following the Restructuring, both Unicom Group and Guoxin continued to be governed by the strategic-planning and policy-making mechanism of the State Council and the MII. Accordingly, the reorganisation of Guoxin and the combination of Unicom Group and Guoxin are considered to be a reorganisation of businesses under the common control of the State Council. In addition, upon the transfer of the ownership interest in Guoxin from China Telecom to Unicom Group, Unicom Group controlled all the Predecessor Entities prior to the Restructuring and continued to control the Company after the Restructuring. Accordingly, the series of combination of the various telecommunications businesses and the transfer of these businesses from Unicom Group to the Company as described in Note 1 above have been accounted for as a reorganisation of entities under common control by using merger accounting as if the Group had been operating continuously throughout the periods presented.

(Amounts expressed in RMB unless otherwise stated)

2. BASIS OF PRESENTATION (Cont'd)

On the basis described above, the financial statements for the year ended 31 December 2000 were prepared to present the combined results of operations and cash flows of the Predecessor Entities, now comprising the Group, and the financial position of the Group as of 31 December 2000 as if the state-owned interests in the Group had been held continuously by the Group since 1 January 2000 and the business activities had been conducted by the Group throughout the year ended 31 December 2000. Consequently, the assets, liabilities, revenues and expenses that were clearly identifiable with the businesses and operations transferred to the Group were included at their recorded amounts. Other amounts for which the specific identification method was not practical were not material and were allocated on the following basis:

Items allocated	Allocation basis
Salaries	Number of employees
Accounting and legal services	Number of employees
Training	Number of employees
Retirement benefits	Number of employees
Rent and depreciation	Floor area
Other selling, general and administrative expenses	Number of employees/revenue

Management believed that the above was a reasonable basis of estimating what the Group's expenses would have been on a stand-alone basis.

The financial statements are prepared under the historical cost convention, as modified by the revaluation of land use rights and buildings, and in accordance with Statements of Standard Accounting Practice ("HK SSAP") issued by the Hong Kong Society of Accountants and accounting principles generally accepted in Hong Kong ("HK GAAP"). This basis of accounting differs from that used in the preparation of the financial statements for PRC statutory reporting purposes, which were based on the accounting principles and financial regulations applicable to enterprises established in the PRC ("PRC GAAP").

The principal adjustments made to conform to HK GAAP include the following:

- Reversal of revaluation surplus and related depreciation and amortisation charges arising from the revaluation of assets performed by independent valuers registered in the PRC;
- Additional accrual for retirement benefits;
- Additional provision for housing benefits;
- Additional capitalisation of interest expenses;
- Provision for deferred taxation; and
- Recognised loss arising from the terminations of CCF Arrangements as one-time losses.

3. PRINCIPAL ACCOUNTING POLICIES

The principal accounting policies adopted by the Group in the preparation of the financial statements for the year ended 31 December 2001, which conform to HK GAAP, are as follows:

(a) Adoption of Statements of Standard Accounting Practice

For the year ended 31 December 2001, the Group adopted, for the first time, the following HK SSAP issued by the Hong Kong Society of Accountants:

SSAP9 (revised)	Events after the balance sheet date
SSAP14 (revised)	Leases
SSAP26	Segment reporting
SSAP28	Provisions, contingent liabilities and contingent assets
SSAP29	Intangible assets
SSAP30	Business combinations
SSAP31	Impairment of assets
SSAP32	Consolidated financial statements and accounting for investments in subsidiaries

The impact of the adoption of the new standards on the Group's consolidated operating results and financial position is not significant and, accordingly, no prior period adjustment has been made.

(b) Basis of consolidation

The consolidated financial statements of the Group include the accounts of the Company and the enterprises that it controls. This control is normally evidenced when the Company has the power to govern the financial and operating policies of an enterprise so as to benefit from its activities. In addition, the Company holds, either directly or indirectly, more than 50% of the issued share capital or controls more than half of the voting power or the composition of the Board of Directors of the subsidiaries. The results of subsidiaries acquired or disposed of during the year are consolidated from or to their effective dates of acquisition or disposal. The equity and net income attributable to minority owners' interests are shown separately in the balance sheet and income statement, respectively.

All significant intercompany transactions and balances, and any unrealised gains arising from intercompany transactions, have been eliminated on consolidation.

(c) Use of estimates

The preparation of financial statements in conformity with HK GAAP requires management to make estimates and assumptions that affect the reported amount and disclosures. Accordingly, actual results may differ from those estimates and assumptions.

3. PRINCIPAL ACCOUNTING POLICIES (Cont'd)

(d) Property, plant and equipment

Property, plant and equipment, other than land use rights and buildings, are stated at cost less accumulated depreciation and accumulated impairment losses. The cost of an asset comprises its purchase price and any directly attributable costs of bringing the asset to its working condition and location for its intended use. Expenditures incurred after the property, plant and equipment have been put into operation, such as repairs and maintenance and overhaul costs, are normally charged to expense in the year in which they are incurred. In situations where it can be clearly demonstrated that the expenditure has resulted in an increase in the future economic benefits expected to be obtained from the use of the asset beyond its originally assessed standard of performance, the expenditure is capitalised as an additional cost of the assets.

Land use rights and buildings are stated at valuation. Independent valuations are performed periodically with the last valuation performed on 31 March 2000. In the intervening years, the directors review the carrying value of land use rights and buildings and adjustment is made where in the directors' opinion there has been a material change in value.

Any increase in land use rights and buildings valuation is credited to the revaluation reserve; any decrease is first offset against an increase on earlier valuation in respect of the same property and is thereafter charged to the income statement.

Upon the disposal of revalued land use rights and buildings, the realised portion of the revaluation reserve is transferred from the revaluation reserve to retained profits.

Depreciation is provided using the straight-line method over the estimated useful lives of the assets, after taking into consideration their estimated residual value. The estimated useful lives of property, plant and equipment are as follows:

	Depreciable life	Residual value
Land use rights	Over the period of grant	—
Buildings	8 - 40 years	3%
Leasehold improvements	Over the lease term	—
Telecommunications equipment	4 - 11 years	3%
Office, furniture and fixtures and other	4 - 14 years	3%

The carrying amount of property, plant and equipment stated at depreciated cost is reviewed periodically in order to assess whether the recoverable amount has declined below the carrying amount. When such a decline has occurred, the carrying amount is reduced to the recoverable amount. The amount of the reduction is recognised as an expense unless it reverses a previous revaluation increase, in which case, it is charged against any related revaluation reserve to the extent that the reduction does not exceed the amount held in the revaluation reserve in respect of the same item. In determining the recoverable amount, expected future cash flows generated by the property, plant and equipment are discounted to their present values.

A subsequent increase in the recoverable amount is written back to the income statement when the circumstances and events that led to the write-down or write-off cease to exist. The amount written back is reduced by the amount that would have been recognised as depreciation had the write-down or write-off not occurred.

3. PRINCIPAL ACCOUNTING POLICIES (Cont'd)

(d) Property, plant and equipment (Cont'd)

When assets are sold or retired, their costs and accumulated depreciation and accumulated impairment losses are eliminated, any gain or loss resulting from their disposals is included in the income statement.

(e) Construction-in-progress

Construction-in-progress represents buildings under construction and plant and equipment pending installation, and is stated at cost less accumulated impairment losses. Costs include construction and acquisition costs, and interest charges arising from borrowings used to finance the assets during the construction period.

No provision for depreciation is made on construction-in-progress until such time as the assets are completed and ready for use.

(f) Goodwill

Goodwill represents the excess of purchase consideration over the Group's interests in the fair values of the net identifiable assets and liabilities acquired as at the date of acquisition. Goodwill is carried at cost less accumulated amortisation and accumulated impairment losses. Goodwill is amortised on a straight-line method over the economic lives of the acquired businesses, estimated to be 5 to 7 years. When later events and circumstances occur which indicate the remaining balance of goodwill may not be recoverable, the unamortised balance is written down to its estimated recoverable amount. Estimated recoverable amount is determined based on estimated discounted future net cash flows of the related business over its remaining life.

(g) Deferred expenditures and amortisation

Deferred expenditures mainly represent (i) expenditures on facilities for interconnection with other operators, for which the Group has a permanent use right, and (ii) housing benefits arising from selling staff quarters to employees at preferential prices lower than cost. Expenditures on interconnection facilities are amortised using the straight-line method over the expected period of benefit of 5 years. Housing benefits are amortised using the straight-line method over the estimated service lives of the employees.

3. PRINCIPAL ACCOUNTING POLICIES (Cont'd)

(h) Investments in securities

Investment securities

Equity securities intended to be held on a continuing basis are classified as investment securities and recorded at cost less any provision for impairment in value.

The carrying amounts of investment securities are reviewed at the end of each year to assess whether the fair values have declined below the carrying amounts. If such a decline has occurred, the carrying amounts are reduced and the reduction is recognised as an expense unless there is evidence that the decline is temporary.

Provisions against the carrying value of investment securities are reversed when the circumstances and events leading to the write-downs or write-offs cease to exist and there is persuasive evidence that the new circumstances and events will persist for the foreseeable future.

Upon disposal of investment securities, profit or loss thereon is accounted for in the income statement.

Trading securities

Trading securities represent government bonds and marketable securities held for dealing purposes and are included in the balance sheet at their fair values. Any changes in fair values of trading securities are recognised in the income statement when they arise.

Upon disposal of investment securities, any profit and loss is accounted for in the income statement.

(i) Subsidiaries

A subsidiary is an enterprise in which the Company holds, directly or indirectly, more than 50% of the equity interest as a long-term investment or otherwise has the power to control the financial and operating policies of the enterprise.

In the Company's standalone, unconsolidated balance sheet, investment in subsidiaries is stated at cost less any provision for impairment in value where considered necessary by the directors. The results of the subsidiaries are included in the income statement to the extent of dividends declared.

(j) Associated companies

An associated company is an enterprise in which the Company has significant influence, but not control or joint control, and thereby has the ability to participate in its financial and operating policy decisions.

In the consolidated financial statements, investment in associated companies is accounted for under the equity method, whereby the investment is initially recorded at cost and the carrying amount is adjusted thereafter to recognise the Group's share of the post-acquisition profits or losses of the associated company, distributions received from the associated company and other adjustments arising from changes in the equity of the associated company that have not been included in the income statement.

Where, in the opinion of the directors, there is an impairment in value of an associated company, permanently reduced below its carrying value, or the market value has fallen below the carrying value over a sustained period, a provision is made for such impairment in value.

3. PRINCIPAL ACCOUNTING POLICIES (Cont'd)

(k) Cash and cash equivalents

Cash represents cash on hand and deposits with banks which are repayable on demand.

Cash equivalents represent short-term, highly liquid investments which are readily convertible into known amounts of cash with original maturities of three months or less and that are subject to an insignificant risk of change in value.

(l) Short-term bank deposits

Short-term bank deposits are cash invested in fixed-term deposits with original maturities ranging from more than three months to one year.

(m) Accounts and other receivables

Accounts and other receivables are stated at their cost, after provision for doubtful debts.

(n) Inventories

Inventories, which principally comprise handsets, SIM cards, pagers and accessories, are stated at the lower of cost and net realisable value. Cost is based on the weighted average method and comprises all costs of purchase and other costs incurred in bringing the inventories to their present location and condition. Net realisable value is the estimated selling price in the ordinary course of business and the estimated costs necessary to make the sale.

When inventories are sold, their carrying amount is charged to expense in the year in which the revenue is recognised. Write-downs to net realisable value and losses of inventories are recognised as an expense in the year the write-down or loss occurs.

(o) Advances from customers

Advances from customers are monthly fees paid by subscribers in advance or amounts paid by customers for GSM prepaid cards, Internet protocol ("IP") telephone cards and other calling cards which cover future telecommunications services (over a period of 3 to 12 months). Customer advances are stated at the amount of proceeds received less the amount already recognised as revenues upon the rendering of services.

(p) Finance leases

A finance lease is a lease that transfers substantially all the risks and rewards incident to ownership of an asset to the lessee. Title may or may not eventually be transferred. The Group recognises finance leases as assets and liabilities in the balance sheet at amounts equal at the inception of the lease to the fair value of the leased property or, if lower, at the present value of the minimum lease payments. In calculating the present value of the minimum lease payments, the discount factor used is the interest rate implicit in the lease, when it can be determined. Otherwise, the Group's incremental borrowing rate is used. Initial direct costs incurred are included as part of the asset. Lease payments are apportioned between the finance charge and the reduction of the outstanding liability. The finance charge is allocated to periods during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability for each period.

A finance lease gives rise to depreciation expense for the asset as well as a finance cost for each accounting period. The depreciation policy for leased assets is the same as that for depreciable assets that are owned.

3. PRINCIPAL ACCOUNTING POLICIES (Cont'd)

(q) Operating leases

An operating lease is a lease other than a finance lease.

Leases of assets under which substantially all the risks and rewards of ownership are retained by the lessor are classified as operating leases. Lease payments or lease rental received under an operating lease are recognised as an expense or income on a straight-line basis over the lease term.

(r) Borrowing costs

Borrowing costs include interest charges and other costs incurred in connection with the borrowing of funds. Interest charges are expensed as incurred, except for interest directly attributable to a construction project, that necessarily takes a substantial period of time to prepare for its intended use, in which case they are capitalised as part of the cost of the project. Capitalisation of borrowing costs commences when expenditures for the asset and borrowing costs are being incurred and the activities to prepare the asset for its intended use are in progress. Interest is capitalised up to the date when the project is completed and ready for its intended use.

To the extent that funds are borrowed specifically for the purpose of obtaining a qualifying asset, the amount of borrowing costs eligible for capitalisation on that asset is determined as the actual borrowing costs incurred on that borrowing during the period less any investment income on the temporary investment of those borrowings.

To the extent that funds are borrowed generally and used for the purpose of obtaining a qualifying asset, the amount of borrowing costs eligible for capitalisation is determined by applying a capitalisation rate to the expenditures on that asset. The capitalisation rate is the weighted average of the borrowing costs applicable to the borrowings of the enterprise that are outstanding during the period, other than borrowings made specifically for the purpose of obtaining a qualifying asset. The amount of borrowing costs capitalised incurred during a period should not exceed the amount of borrowing cost incurred during that period.

The capitalised interest rate represents the cost of capital for raising the related borrowings externally and varies from 5.46% to 7.65% for the year ended 31 December 2001 (2000: 4.95% to 6.66%).

(s) Provisions

A provision is recognised when an enterprise has a present obligation (legal or constructive) as a result of a past event and it is probable (i.e. more likely than not) that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation. Provisions are reviewed at each balance sheet date and adjusted to reflect the current best estimate. Where the effect of the time value of money is material, the amount of a provision is the present value of the expenditures expected to be required to settle the obligation.

3. PRINCIPAL ACCOUNTING POLICIES (Cont'd)

(t) Revenue recognition

(1) Revenue is recognised when it is probable that the economic benefits associated with a transaction will flow to the Group and when the revenue and cost can be measured reliably, on the following bases:

- Usage fees are recognised when the service is rendered;
- Monthly fees are recognised as revenue in the month during which the services are rendered;
- Connection fees are recognised as revenue upon activation of service for subscribers;
- Revenue from IP card and other calling card sales, which represents prepaid service fees received from customers for telephony services, is recognised when the related service is rendered upon actual usage of the telephone cards by customers;
- Leased line rental income is recognised on the straight-line basis over the lease term;
- Sales of telecommunications products, such as handsets, SIM cards and pagers, are recognised when title has passed to the buyers.

(2) Interest income

Interest income from deposits in banks or other financial institutions is recognised on the accrual basis.

(u) Foreign currency translation

The Group maintains its books and records in Renminbi ("RMB"), which is not freely convertible into foreign currencies. Transactions denominated in currencies other than RMB are translated into RMB at the exchange rates prevailing at the dates of the transactions. Monetary assets and liabilities denominated in other currencies are translated into RMB at exchange rates prevailing at the balance sheet date. Exchange gains or losses arising from changes in exchange rates subsequent to the transaction dates are included in the income statement.

(v) Retirement benefits

The cost of providing retirement benefits under defined benefit schemes is charged to expense over the expected service lives of the employees. The fixed contributions for retirement benefits made under defined contribution schemes are charged to expense as incurred.

(w) Taxation

Income tax is provided on the basis of income for statutory financial reporting purposes, adjusted for income and expense items which are not assessable or deductible for tax purposes.

Deferred taxation is provided under the liability method, at the current tax rate, in respect of timing differences between income as computed for taxation purposes and income as stated in the income statement. A deferred tax asset is not recognised unless the related benefits are expected to crystallise in the foreseeable future.

3. PRINCIPAL ACCOUNTING POLICIES (Cont'd)

(x) **Impairment of assets**

Property, plant and equipment, goodwill, investment in associated companies and securities are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Whenever the carrying amount of an asset exceeds its recoverable amount, an impairment loss is recognised in the income statement for assets carried at cost or treated as a revaluation decrease for land use rights and buildings that are carried at revalued amounts to the extent that the impairment loss does not exceed the amount held in the revaluation surplus for that same assets. The recoverable amount is the higher of an asset's net selling price and value in use. The net selling price is the amount obtainable from the sale of the asset in an arm's length transaction while value in use is the present value of estimated future net cash flows expected to arise from the continuing use of the asset and from its disposal at the end of its useful life. Recoverable amounts are estimated for individual assets or, if it is not possible, for the cash-generating unit.

Provision for impairment loss is classified under "general, administrative and other expenses" as a component of operating expenses. Reversal of impairment losses recognised in prior years is recorded when the impairment losses recognised for the asset no longer exist or have decreased. The reversal is recorded in the income statement or as a revaluation increase.

(y) **Related parties**

Entities are considered to be related if one has the ability to control the other, directly or indirectly, or has the ability to exercise significant influence over the financial and operating decisions of the other. Entities are also considered to be related if they are subject to common control or common significant influence.

(z) **Contingencies**

Contingent liabilities are not recognised in the financial statements. They are disclosed unless the possibility of an outflow of resources embodying economic benefits is remote. A contingent asset is not recognised in the financial statements but disclosed when an inflow of economic benefits is probable.

(aa) **Events after the balance sheet date**

Events after the balance sheet date that provide additional information about a company's position at the balance sheet date or those that indicate the going concern assumption is not appropriate, (adjusting events), are reflected in the financial statements. Events after the balance sheet date that are not adjusting events are disclosed in the notes when material.

(ab) **Net income per share and per American Depository Share ("ADS")**

Basic net income per shares has been computed by dividing the net income by the number of weighted average number of ordinary shares outstanding during the year.

Diluted net income per share has been computed by dividing the net income by the weighted average number of ordinary shares, after adjusting for the effects of the dilutive potential ordinary shares.

Basic and diluted net income per ADS have been computed by multiplying the net income per share by 10, which is the number of shares represented by each ADS.

4. REVENUE

Revenue is primarily comprised of usage fees, monthly fees, connection fees and interconnection revenue earned by the Group by providing cellular, paging, long distance, data and Internet services. Tariffs for these services are subject to regulations by various government authorities, including the State Development Planning Commission, the MII and the provincial regulatory authorities.

Revenue is net of business tax, government surcharges and central irrigation construction levy, where applicable.

The major components of the revenue are as follows:

		Year ended 31 December	
	Note	2001	2000
		RMB'000	RMB'000
Cellular Business			
Usage fee	(i) (a)	14,937,448	8,212,332
Monthly fee	(ii)	3,660,473	2,476,104
Connection fee	(iii)	204,986	517,642
Interconnection revenue	(iv)	1,262,267	753,591
Other revenue	(vi)	439,884	228,135
Total Cellular Business revenue		20,505,058	12,187,804
Paging Business			
Monthly fee	(ii)	4,141,232	7,992,999
Connection fee	(iii)	1,595	68,233
Other revenue	(vi)	198,997	422,258
Total Paging Business revenue		4,341,824	8,483,490
Long Distance, Data and Internet Business			
Usage fee	(i) (b)	2,120,997	470,526
Monthly fee	(ii)	—	7,076
Interconnection revenue	(iv)	724,624	293,745
Leased lines rental	(v)	427,195	321,255
Other revenue	(vi)	36,128	3,792
Total Long Distance, Data and Internet Business revenue		3,308,944	1,096,394
Total service revenue		28,155,826	21,767,688
Sales of telecommunications products		1,237,060	1,924,770
Total revenue		29,392,886	23,692,458

4. REVENUE (Cont'd)

Notes:

(i) Usage fees comprise:

(a) charges for incoming and outgoing calls made by cellular subscribers including charges for local calls, domestic direct dial ("DDD") and international direct dial ("IDD") as well as roaming fees for calls made by cellular subscribers outside their local service areas.

(b) charges for IP telephone calls, fixed line long distance calls, and data and Internet services.

(ii) Monthly fees represent fixed amounts charged to cellular, paging, and data and Internet subscribers on a monthly basis for maintaining their access to the related services.

(iii) Connection fees are charged to cellular and paging subscribers for the one-time activation service rendered to connect the cellular subscribers to the Group's cellular network or to reconfigure the receiving frequency of the subscribers' pagers to the Group's paging network.

(iv) Interconnection revenue represents amounts received from other operators, including Unicom Group, for calls from their networks to the Group's networks. It also includes roaming-in fees received from other operators, including Unicom Group, for calls made by their subscribers using the Group's cellular networks.

(v) Leased line rental income represents rentals received for leasing of transmission lines to Unicom Group, business customers and other carriers in the PRC.

(vi) Other revenue mainly represents revenue from the provision of value-added services to subscribers and commission revenue for providing agency services to sell telecommunications products for Unicom Group.

5. FINANCIAL INCOME

Financial income for the year ended 31 December 2001 mainly represents interest income arising from the proceeds of the Global Offering amounting to RMB2,096,972,000 (2000 : RMB1,748,805,000).

6. INCOME BEFORE TAXATION AND MINORITY INTERESTS

Income before taxation and minority interests is arrived at after crediting and charging the following:

	Note	Year ended 31 December 2001 RMB'000	2000 RMB'000
After crediting/(charging):			
Interest income	5	2,096,972	1,748,805
Gains (losses) from exchange difference	8	14,476	(30,881)
Share of (losses) profits from associated companies	8	(24,773)	258
Dividends from investment securities		22,864	9,321
Realised gains on investment securities		944	—
Realised gains on trading securities	8	31,979	64,956
Unrealised (losses) gains on trading securities	8	(56,576)	31,855
After charging/(crediting):			
Financial expense:			
Interest on bank loans repayable within five years		2,593,402	1,558,090
Interest on loans from Unicom Group repayable within five years		—	48,313
Less: amounts capitalised in construction-in-progress		(686,254)	(252,657)
Total interest expense		1,907,148	1,353,746
Bank charges		10,418	—
Total financial expense		1,917,566	1,353,746
Depreciation and amortisation			
- Assets held under finance leases		9,327	—
- Other assets		8,252,969	5,734,315
Total depreciation and amortisation		8,262,296	5,734,315
Operating lease expenses	7(iv)	569,954	546,165
Loss on disposal of property, plant and equipment	7(iv), 20	54,475	277,973
Auditors' remuneration		52,972	47,030
Provision (write-back) for doubtful debts			
- Cellular Business		517,663	355,082
- Paging Business		(14,510)	85,430
- Long Distance, Data and Internet Business		37,801	4,319
Total provision for doubtful debts	7(iv)	540,954	444,831

6. INCOME BEFORE TAXATION AND MINORITY INTERESTS (Cont'd)

	Note	Year ended 31 December 2001 RMB'000	2000 RMB'000
After crediting (charging)			
Personnel:			
- Salaries and wages		2,156,911	1,573,147
- Contributions to defined contribution pension schemes	12	163,500	148,322
- Special monetary housing benefits	13	88,911	—
- Contributions to housing fund	13	69,963	44,333
- Other housing benefits	13	7,933	4,038
Total personnel	7(iii)	2,487,218	1,769,840
Provision for impairment in value of:			
- Property, plant, and equipment	20	468,611	—
- Goodwill	21	163,900	—
Total provisions for impairment	7(iv)	632,511	—
(Write-back) provision for impairment in value of investments in:			
- Associated companies		(3,219)	7,501
- Investment securities		(12,490)	6,812
Total provisions for impairment in value of investments		(15,709)	14,313

7. OPERATING EXPENSES

The nature of the major components of operating expenses is as follows:

(i) Leased line charges are incurred in association with leasing of transmission capacity from other operators.

(ii) Interconnection charges represent amounts paid to other operators, including Unicom Group, for calls from the Group's networks to the networks of other operators.

(iii) Personnel costs comprise staff salaries, bonuses and medical benefits, contributions to employee retirement schemes and housing benefits.

7. OPERATING EXPENSES (Cont'd)

(iv) General, administrative and other expenses are analysed as follows:

	Year ended 31 December 2001 RMB'000	2000 RMB'000
Operating lease expenses	569,954	546,165
Repair and maintenance expenses	424,614	635,197
Provision for doubtful debts	540,954	444,831
Loss on disposal of property, plant and equipment	54,475	277,973
Provisions for impairment in value of property, plant and equipment and goodwill	632,511	—
Travelling, entertainment and meeting expenses	612,592	389,335
Power and water charges	473,774	229,308
Office expenses	587,727	385,980
Other	1,602,396	834,274
	5,498,997	3,743,063

8. OTHER INCOME, NET

	Year ended 31 December 2001 RMB'000	2000 RMB'000
Realised gains on trading securities	31,979	64,956
Unrealised (losses) gains on trading securities	(56,576)	31,855
Share of (losses) profits from associated companies	(24,773)	258
Gains (losses) from exchange difference	14,476	(30,881)
Other	54,725	(6,959)
	19,831	59,229

9. DIRECTORS', SENIOR EXECUTIVES' AND SUPERVISORS' EMOLUMENTS

(a) Details of directors' emoluments pursuant to Section 161 of the Companies Ordinance are set out below:

	Year ended 31 December 2001 RMB'000	2000 RMB'000
Non-executive directors:		
Fees	1,273	—
Executive directors:		
Fees	—	—
Other emoluments		
- Salaries, allowance and other allowances	9,083	2,825
- Pension benefits/pension scheme contributions	124	52
- Bonuses paid and payable	11,162	222
	20,369	3,099
	21,642	3,099

The emoluments of the directors analysed by the number of directors and emolument ranges were as follows:

(All amounts expressed in Hong Kong dollars)	Year ended 31 December 2001	2000
Up to $1,000,000	4	5
$2,500,001 - $3,000,000	2	—
$3,500,001 - $4,000,000	1	—
$4,000,001 - $4,500,000	1	—
$4,500,001 - $5,500,000	1	—
	9	5

No directors waived the right to receive emoluments during the year.

(b) Details of five highest paid individuals:

	Year ended 31 December 2001 RMB'000	2000 RMB'000
Salaries, allowance and other allowances	9,083	2,825
Pension benefits/pension scheme contributions	124	52
Bonuses paid and payable	11,162	222
	20,369	3,099

Of the five highest paid individuals of the Group, all (2000: all) are directors of the Company whose emoluments are included above.

No emolument was paid to the five highest paid individuals as an inducement to join or upon joining the Company or as compensation for loss of office.

10. TAXATION

Provision for taxation represents:

	Year ended 31 December 2001 RMB'000	2000 RMB'000
PRC enterprise income tax	1,608,825	1,619,169
Deferred taxation	(567,688)	(514,200)
	1,041,137	1,104,969

There is no Hong Kong profits tax liabilities as the Group does not have any assessable income sourced from Hong Kong for the years ended 31 December 2001 and 2000.

For 2000, the provincial branches and the head office of China Unicom was assessed for income tax liability on a consolidated basis as a single entity and were subject to the statutory tax rate of 33%. On the other hand, most of Guoxin's subsidiaries were individually subject to enterprise income tax at the rate of 33% and certain subsidiaries were granted by tax authorities a reduced income tax rate of 15%.

For 2001, China Unicom has obtained new tax approval and the income tax liability was assessed as follows:

(a) China Unicom was approved as foreign investment enterprise ("FIE") and the tax liability for the year of 2001 was assessed in accordance with FIE taxation requirement.

(b) China Unicom was assessed for income tax liability on a consolidated basis as a single entity and settled income tax liabilities centrally with the Beijing tax authority.

(c) Starting from 1 January 2001, Guoxin and its subsidiaries (except for Unicom Guomai) were subject to the FIE taxation requirement as stated in note (a) above and assessed for income tax liability on a consolidated basis with China Unicom as a single entity.

10. TAXATION (Cont'd)

The reconciliation of PRC enterprise income tax at the statutory tax rate of 33% applied to income before taxation, to the effective tax rate actually recorded in the income statement, is as follows:

	Year ended 31 December 2001	2000
PRC		
Statutory tax rate of 33%	33.0%	33.0%
Non-deductible expenses:		
- Housing benefits	2.2	—
- Personnel expenses	0.7	2.0
- Selling and marketing expenses	—	2.9
- Other	1.2	0.5
Non-taxable income:		
- Connection fees	—	(2.6)
Effect of tax holiday	(2.7)	(1.3)
Non-recognition of deferred taxes:		
- Provision for doubtful debts of Cellular Business	4.6	3.8
Additional depreciation deductible for tax purpose from 2001	(9.8)	—
Other	—	(0.2)
Effective PRC income tax rate	29.2%	38.1%
Hong Kong		
Statutory tax rate of 16%	16.0%	16.0%
Non-taxable income:		
- Interest income	(16.0)	(16.0)
Effective HK income tax rate	—	—
Total overall effective income tax rate	19.1%	24.7%

Tax effect of tax holiday is as follows:

	Year ended 31 December 2001	2000
Aggregate amount (RMB in millions)	83.6	37.9
Per share effect (RMB)	0.007	0.003

10. TAXATION (Cont'd)

Deferred taxation represents the taxation effect of the following timing differences:

	Consolidated As of 31 December 2001 RMB'000	2000 RMB'000
Deferred tax assets:		
Interest on loans from CCF joint ventures	317,447	439,479
Loss arising from terminations of CCF Arrangements	348,082	298,331
Income tax on advances from customers for telephone cards	529,049	189,915
Operating loss of the Cellular Business	—	14,709
Difference in goodwill amortisation period	23,590	18,284
Provision for impairment in value for property, plant and equipment	154,642	—
Provision for impairment in value for goodwill	54,087	—
Provision for doubtful debts of Paging Business and Long Distance, Data and Internet Business	53,223	46,450
Write-off of deferred expenditures	24,368	136,848
Write-down of inventory to net realisable value	35,819	21,856
Amortisation of retirement benefits	39,852	41,241
Additional depreciation deductible for tax purpose from 2001	232,291	—
Other	20,590	86,120
	1,833,040	1,293,233
Deferred tax liabilities:		
Accelerated depreciation for tax purpose	(129,526)	(239,143)
Other	(122,106)	(40,370)
	(251,632)	(279,513)
Net deferred tax assets	1,581,408	1,013,720
Less: Current portion of deferred tax assets	(569,192)	(19,642)
	1,012,216	994,078

Deferred tax assets not recognised consist of the following:

	Consolidated As of 31 December 2001 RMB'000	2000 RMB'000
Tax effect of provision for doubtful debts of Cellular Business	373,159	228,061
Tax effect of operating loss of a subsidiary	107,299	107,299

11. CHINA-CHINA-FOREIGN ARRANGEMENTS AND THEIR TERMINATIONS

In the process of developing its cellular network, the Cellular Business entered into cooperation agreements with certain contractual joint venture companies (the "CJVs") established in the PRC. Each CJV was established by one or more Chinese enterprises and one or more foreign parties. The cooperation arrangements between the Cellular Business and the CJVs are hereinafter referred to as the China-China-Foreign Arrangements (the "CCF Arrangements").

Pursuant to the CCF Arrangements, the CJVs extended funding to the Cellular Business for the construction of telecommunications systems and network equipment in the PRC. Upon completion of construction, the Cellular Business was responsible for operating the systems. In return for funding the construction of the cellular networks, the CJVs were entitled to receive (usually on an annual or semi-annual basis) from the Cellular Business a fixed proportion of the cash flows generated from the operations of the cellular networks. It was anticipated at the inception of the CCF Arrangements that such periodic distributions of cash would be sufficient for the CJVs to recover their principal together with a reasonable return. The cooperation periods under these CCF Arrangements generally ranged from twelve to fifteen years. As security, the fixed assets during the cooperation periods were held by the CJVs in a manner similar to a pledging arrangement under a mortgage loan. Accordingly, the CCF Arrangements were accounted for as secured financing arrangements. At the end of the cooperation periods, the CJVs' rights to share the cash flows from the cellular networks and the security rights in the underlying fixed assets were to be relinquished.

The estimated costs of the funding provided by the CJVs were accrued over the cooperation periods and accounted for as interest costs. The accrual was made using the then-prevailing market interest rates applicable to long-term bank loans which ranged from 6.21% to 8.01%. As all CCF Arrangements were terminated in early 2000, no further interest was accrued during that year.

The periodic cash distribution to the CJVs in excess of the accrued interest payable was accounted for as repayment of principal. Since the amount and the timing of the periodic cash distributions to the CJVs were not fixed and depended on the actual cash flows generated by the operations of the cellular networks, the CCF Arrangements were treated as long-term borrowings with no fixed repayment schedules. The entire outstanding amounts of approximately RMB6,200 million in relation to those CCF Arrangements were terminated in 2000 (as further discussed below).

Certain CCF Arrangements were terminated in 1999 and all the remaining CCF Arrangements were terminated in 2000. Pursuant to the termination agreements signed between the CJVs and Unicom Group, compensation in the form of cash and share warrants was paid to the CJVs. The aggregate losses arising from the extinguishment of these CCF debts amounted to approximately RMB1,194 million for 2000. The losses were calculated based on the difference between the net carrying amounts of the outstanding CCF debts being terminated, which amounted to approximately RMB6,263 million for 2000, and the total cash compensation amounts of approximately RMB7,457 million for 2000 made to the CJVs.

Substantially all of the total cash compensation of approximately RMB7,457 million (1999: RMB2,001 million) was financed by long-term bank loans originally borrowed by Unicom Group, which were restructured into long-term loans borrowed directly by China Unicom in 2000 (see Note 33(b)).

11. CHINA-CHINA-FOREIGN ARRANGEMENTS AND THEIR TERMINATIONS (Cont'd)

Apart from the cash compensation, share warrants were granted to the CJVs or their designees as part of the compensation for the termination of the CCF Arrangements in 2000. These share warrants allowed the holders to subscribe for new shares of the Company at the initial public offering price. The total exercise value of the share warrants granted to the CJVs or their designees was fixed, amounting to approximately RMB5,024 million in aggregate. The exercise period lasted for six months following the date that was six months after the Global Offering, 22 June 2000. As of 31 December 2001, all share warrants expired and no share warrants were exercised by these CJVs or their designees.

12. RETIREMENT BENEFITS

All the full time employees of the Group are covered by a state-sponsored pension scheme under which the employees are entitled to an annual pension equal to their basic salaries at their retirement dates. The PRC government is responsible for the pension liability to these retired employees. The Group was required to make contributions to the state-sponsored pension scheme at the rate of 19% for 2001 (2000: 19.1%) of the employees' basic salaries. Under this scheme, the Group has no obligation for post-retirement benefits beyond the annual contributions.

In addition, effective from 11 August 1998, a supplementary defined contribution pension plan managed by an independent insurance company has been established. Under this plan, the Group makes a monthly contribution of 2% to 6% of the monthly salary of each employee. There were no vested benefits attributable to past services upon adoption of the plan.

Prior to 31 May 1998, the Paging Business also provided a defined benefit supplementary pension plan managed by China Telecom. The average annual supplementary pension payment was approximately RMB2,000 to RMB5,000 per retiree as of 31 May 1998. The estimated pension costs were amortised over the past service period of the retirees. Upon Guoxin's establishment, China Telecom agreed to take up the pension liabilities under this supplementary pension scheme for approximately 3,000 employees of China Telecom who had worked for the Paging Business before their retirement prior to 31 May 1998. In return, Guoxin agreed to pay China Telecom approximately RMB163 million which approximated the accrued pension liabilities for this group of retirees as of 31 May 1998. Thereafter, Guoxin ceased to provide this supplementary pension scheme to its employees. An actuarial valuation was carried out by Towers Perrin, Inc., which is registered in the Society of Actuaries in the United States of America, for this group of retirees as of 31 May 1998 to evaluate the funding adequacy of the accrued pension liabilities for the supplementary pension. In the opinion of the actuary, the aforementioned funding was sufficient to cover 100% of the accrued pension liabilities of this group of retirees as of 31 May 1998 on the basis provided by the Group. The key assumptions used by the actuary in the actuarial valuation were a discount rate of 2.5% per annum and the China Life Annuitant Mortality Table.

Retirement benefits charged to the income statement are as follows:

	Year ended 31 December	
	2001	2000
	RMB'000	RMB'000
Contributions to defined contribution pension schemes	163,500	148,322

13. HOUSING BENEFITS

Under housing reform schemes in accordance with government regulations at the provincial level, the Group provided benefits to certain qualified employees to enable them to purchase living quarters at a discount. In the case of Guoxin, the living quarters were provided by China Telecom prior to the establishment of Guoxin and the related benefits were not charged to the Group. In the case of the Cellular Business, certain of these living quarters were provided by Unicom Group and the related benefits were not charged to the Group. Housing benefits which were not charged to the Group amounted to approximately RMB18.5 million for 2001 (2000: RMB18.5 million).

Subsequent to the establishment of Guoxin, for living quarters purchased or built by the Group, the liability to provide the housing benefits was recognised by the Group upon finalisation of the allocation of the housing units to specific employees. The amount of the benefits was the difference between the cost of the quarters purchased by the employees and the amount actually charged to the employees. The benefits are recorded as expenses over the estimated remaining average service life of the participating employees.

In addition, all of the full time employees of the Group are entitled to participate in a state-sponsored housing fund. The fund can be used for the construction of living quarters or may be withdrawn upon the retirement of the employees. The Group is required to make annual contributions to the housing fund at a rate from 5% to 10% (2000: 5%) of the employees' basic salaries.

According to the central government policy on housing reform based on a State Council circular issued in 1998, monetary housing subsidies in the form of special cash payments are to be made by certain PRC enterprises to their employees in order to enable them to purchase living quarters. Under this general policy, enterprises are allowed to establish their own housing reform schemes taking into consideration the actual financial capability of the enterprises.

During the year, the Group finalised its monetary housing benefit scheme as a special employee incentive scheme for all qualified employees. According to the scheme, the total amount of monetary housing benefit for each employee is determined based on the working age of the employee and the property market price prevailing in the relevant location. The total monetary housing benefit is divided into three annual payments in the proportion of 40%, 30% and 30% respectively. In order to be included in the incentive scheme, employees are required to sign a service contract with a minimum service period of three years. The employees will be entitled to the first 40% payment only when the following criteria are met:

(i) the provincial branch in which the employees are working has achieved the annual performance budget set by head office management; and

(ii) the employees continue to be under the employment of the Group at the time of the payment.

Similarly, the employees will only be entitled to the second and then the third annual payments when and only when the above two conditions are also fulfilled in subsequent years.

The Group accrues for each annual payment upon the fulfillment of the above criteria by the employees, at which time the liability is considered to have arisen.

13. HOUSING BENEFITS (Cont'd)

For the year ended 31 December 2001, only certain provinces achieved the annual performance budget and were thus approved by management to distribute and pay out such monetary housing benefits. The provision for special monetary housing benefits for qualified employees of these provinces for the year ended 31 December 2001 amounted to approximately RMB88,911,000 representing their first 40% entitlements. The remaining provinces were not entitled to the special monetary housing benefits in 2001 since they did not achieve their annual performance budget in 2001 and accordingly, no provision for such benefits was made.

The expenses incurred by the Group in relation to the housing benefits described above were as follows (excluding those paid by Unicom Group and China Telecom and not charged to the Group):

	Year ended 31 December	
	2001	**2000**
	RMB'000	**RMB'000**
Special monetary housing benefits	**88,911**	—
Contributions to housing fund	**69,963**	44,333
Other housing benefits	**7,933**	4,038
	166,807	48,371

14. DISTRIBUTION OF INCOME

Prior to the Restructuring, the Cellular Business received funding from Unicom Group. Similarly, the Paging Business prior to the establishment of Guoxin received funding from China Telecom. Such funding was recorded as head office account. Prior to the Restructuring, retained earnings or accumulated deficits were recorded as changes in head office account. Periodically, the Cellular Business and the Paging Business made cash distributions to Unicom Group or to China Telecom. These cash distributions were deducted from head office account.

On 21 April 2000, China Unicom was established as a foreign investment enterprise in the PRC. In accordance with the Articles of Association of China Unicom, China Unicom is required to provide for certain statutory reserves, namely, general reserve fund and staff bonus and welfare fund, which are appropriated from net income after taxation but before dividend distribution.

China Unicom is required to allocate at least 10% of its income after tax determined under PRC GAAP to the general reserve fund until the cumulative amounts reach 50% of the registered capital. The statutory reserve can only be used, upon approval by the relevant authority, to offset accumulated losses or increase capital.

Appropriation to the staff bonus and welfare fund is at the discretion of the directors. The staff bonus and welfare fund can only be used for special bonuses or the collective welfare of the employees and are not distributable as cash dividends. Under HK GAAP, the appropriation to the staff bonus and welfare fund will be charged to the income statement as expenses incurred since any assets acquired through this fund belong to the employees. For the years ended 31 December 2000 and 2001, no appropriation to staff bonus and welfare fund was made.

14. DISTRIBUTION OF INCOME (Cont'd)

According to the Board of Directors'meeting dated on 17 March 2002, China Unicom appropriated approximately RMB224,628,000 to the statutory reserve (2000: RMB424,805,000).

For the year ended 31 December 2001, income attributable to shareholders included a profit of approximately RMB1,981,843,000 (2000: RMB1,584,848,000) which has been dealt with in the accounts of the Company. As of 31 December 2001, the amount of distributable reserves of the Company amounted to approximately RMB3,566,691,000 (2000: RMB1,584,848,000).

The Board of Directors of the Company does not recommend the payment of any dividends to the shareholders for the year ended 31 December 2001.

15. NET INCOME PER SHARE

Net income per share and per American Depository Share ("ADS")

Basic net income per share for the year ended 31 December 2000 was computed by dividing the net income by the weighted average number of ordinary shares in issue during the year, assuming the Company had been in existence since 1 January 2000.

Basic net income per share for the year ended 31 December 2001 was computed by dividing the net income by the weighted average number of ordinary shares in issue during the year.

Diluted net income per share for the year ended 31 December 2000 was computed by dividing the net income by the weighted average number of ordinary shares in issue during the year, after adjusting for the effects of the dilutive potential ordinary shares. All dilutive potential ordinary shares arose from share options granted to the directors or senior management under the Pre-Global Offering Share Option Scheme and share warrants as described in Note 11 and the over-allotment option granted to the underwriters, which if converted to ordinary shares would decrease profit attributable to the shareholders per share.

For the year ended 31 December 2001, all potential dilutive shares arose from share options granted under (i) the Pre-Global Offering Share Option Scheme in 2000 and (ii) the Share Option Scheme in 2001. There was no dilution of net income per share for the current year after taking into account the dilutive effect of the share options. In 2001, anti-dilutive shares arising from the share options of approximately 30,451,000 shares (2000: Nil) were not included in the calculation of diluted net income per share.

Basic and diluted net income per ADS have been computed by multiplying the net income per share by 10, which is the number of shares represented by each ADS.

15. NET INCOME PER SHARE (Cont'd)

Reconciliation of the numerators and denominators of the basic and diluted net income per share computations:

	Year ended 31 December					
	2001			2000		
	Net income RMB'000	Shares '000	Per share amount RMB	Net income RMB'000	Shares '000	Per share amount RMB
Basic net income	**4,456,761**	**12,552,996**	**0.36**	3,234,051	11,208,224	0.29
Effect of conversion of share options and share warrants	**—**	**—**	**—**	—	11,455	—
Diluted net income	**4,456,761**	**12,552,996**	**0.36**	3,234,051	11,219,679	0.29

16. TRADING SECURITIES

As of 31 December 2001, all trading securities represented listed equity securities in the PRC, which were stated at their market values. The realised gains on trading securities for the year ended 31 December 2001 amounted to approximately RMB31,979,000 (2000: RMB64,956,000) and the unrealised losses amounted to RMB56,576,000 (2000: unrealised gain of RMB31,855,000). There have been no significant changes in the market value of the listed securities after the balance sheet date.

17. ACCOUNTS RECEIVABLE, NET

	Consolidated As of 31 December 2001 RMB'000	Consolidated As of 31 December 2000 RMB'000
Accounts receivable for Cellular Business	2,787,993	1,890,338
Accounts receivable for Paging Business	130,172	109,813
Accounts receivable for Long Distance, Data and Internet Business	585,835	216,794
Sub-total	3,504,000	2,216,945
Less: Provision for doubtful debts for Cellular Business	(931,687)	(620,935)
Provision for doubtful debts for Paging Business	(32,131)	(46,641)
Provision for doubtful debts for Long Distance, Data and Internet Business	(42,119)	(4,318)
	2,498,063	1,545,051

The aging analysis of accounts receivable was as follows:

	Consolidated As of 31 December 2001 RMB'000	Consolidated As of 31 December 2000 RMB'000
Less than six months	2,939,485	1,970,206
Six months to one year	314,028	246,739
More than one year	250,487	—
	3,504,000	2,216,945

The normal credit period granted by the Group is on average 30 days from the date of invoice.

Provision for doubtful debts was analysed as follows:

	Consolidated As of 31 December 2001 RMB'000	Consolidated As of 31 December 2000 RMB'000
Balance, beginning of year	671,894	407,261
Provision for the year	540,954	444,831
Written-off for the year	(206,911)	(180,198)
Balance, end of year	1,005,937	671,894

18. INVENTORIES

	Consolidated As of 31 December 2001 RMB'000	Consolidated As of 31 December 2000 RMB'000
Handsets and telephone cards	559,553	219,201
Pagers	116,847	371,967
Other	75,591	88,521
	751,991	679,689

19. PREPAYMENTS AND OTHER CURRENT ASSETS

	Consolidated		The Company	
	As of 31 December		As of 31 December	
	2001	2000	2001	2000
	RMB'000	RMB'000	RMB'000	RMB'000
Deposits and prepayments	620,419	797,192	3,168	—
Interest receivable	167,004	665,657	167,004	665,657
Advances to employees	58,069	31,663	—	—
Other	124,069	171,149	—	3,796
	969,561	1,665,661	170,172	669,453

The aging analysis of prepayments and other current assets was as follows:

	Consolidated		The Company	
	As of 31 December		As of 31 December	
	2001	2000	2001	2000
	RMB'000	RMB'000	RMB'000	RMB'000
Within one year	906,225	1,665,661	170,172	669,453
Over one year	63,336	—	—	—
	969,561	1,665,661	170,172	669,453

20. PROPERTY, PLANT AND EQUIPMENT, NET

	Consolidated						
	2001						2000
	Land use rights and buildings RMB'000	Telecommunications equipment RMB'000	Office furniture, fixtures and others RMB'000	Leasehold improvements RMB'000	Construction-in- progress RMB'000	Total RMB'000	Total RMB'000
Cost or valuation:							
Beginning of year	4,043,384	45,335,956	1,994,544	619,957	13,136,373	65,130,214	40,320,423
Revaluations	—	—	—	—	—	—	148,853
Additions	163,013	203,395	118,954	58,920	30,719,850	31,264,132	25,331,490
Transfer from CIP	2,051,683	24,142,889	550,855	—	(26,745,427)	—	—
Disposals	(53,348)	(189,910)	(36,166)	(40,652)	—	(320,076)	(670,552)
End of year	6,204,732	69,492,330	2,628,187	638,225	17,110,796	96,074,270	65,130,214
Representing:							
At cost	3,501,652	69,492,330	2,628,187	638,225	17,110,796	93,371,190	62,427,134
At valuation	2,703,080	—	—	—	—	2,703,080	2,703,080
	6,204,732	69,492,330	2,628,187	638,225	17,110,796	96,074,270	65,130,214
Accumulated depreciation and impairment losses:							
Beginning of year	392,358	11,092,757	576,571	204,891	—	12,266,577	7,093,815
Revaluations	—	—	—	—	—	—	12,610
Charge for the year	224,876	6,995,931	410,164	93,585	—	7,724,556	5,511,045
Impairment losses	—	449,266	—	—	19,345	468,611	—
Disposals	(8,148)	(60,955)	(24,154)	(40,652)	—	(133,909)	(350,893)
End of year	609,086	18,476,999	962,581	257,824	19,345	20,325,835	12,266,577
Net book value:							
End of year	5,595,646	51,015,331	1,665,606	380,401	17,091,451	75,748,435	52,863,637
Beginning of year	3,651,026	34,243,199	1,417,973	415,066	13,136,373	52,863,637	33,226,608

20. PROPERTY, PLANT AND EQUIPMENT, NET (Cont'd)

	The Company			
	2001			2000
	Office furniture, fixtures and others RMB'000	Leasehold improvements RMB'000	Total RMB'000	Total RMB'000
Cost:				
Beginning of year	5,255	5,400	10,655	—
Additions	1,940	252	2,192	10,655
End of year	7,195	5,652	12,847	10,655
Accumulated depreciation:				
Beginning of year	190	174	364	—
Charge for the year	1,493	2,142	3,635	364
End of year	1,683	2,316	3,999	364
Net book value:				
End of year	5,512	3,336	8,848	10,291
Beginning of year	5,065	5,226	10,291	—

As of 31 December 2001, approximately RMB6,742 million (2000: RMB6,993 million) of property, plant and equipment at cost was pledged to banks as loan security.

As of 31 December 2001, prepayments for property, plant and equipment to be used in construction amounting to RMB2,272 million (2000: RMB1,376 million) have been included in construction-in-progress.

For the year ended 31 December 2001, interest of approximately RMB686 million (2000: RMB253 million) was capitalised to construction-in-progress.

As of 31 December 2001, the cost or valuation of land use rights (located in the PRC) and the related accumulated depreciation amounted to approximately RMB315 million and RMB60 million respectively (2000: RMB241 million and RMB34 million).

Land use rights and buildings of the Group as of 31 March 2000 were valued by Sallmanns (Far East) Ltd., registered property valuers in Hong Kong, using the replacement cost or open market value approach, as appropriate. The resulting revaluation surplus and deficit amounted to RMB177 million and RMB28 million, respectively. The additional depreciation attributable to the revaluation surplus amounted to RMB8.8 million for the year ended 31 December 2001 (2000: RMB12.6 million). The revaluation deficit was charged to the income statement for the year ended 31 December 2000.

As of 31 December 2001, the amount of land use rights and buildings which were revalued as of 31 March 2000 would have been included in the financial statements had the assets been carried at cost less accumulated depreciation was approximately RMB2,139 million (2000: RMB2,267 million).

As of 31 December 2001, net book value of telecommunications equipment held under finance leases amounted to approximately RMB178,622,000.

20. PROPERTY, PLANT AND EQUIPMENT, NET (Cont'd)

In 2001, the economic performance of Paging Business was worse than originally expected. Updated analyses and forecasts were prepared by the Group to determine if there had been an impairment of assets. The test for impairment was conducted for the paging telecommunciations business of each province, representing a cash-generating unit, after considering the significant decline in revenue and profitability in 2001. The impaired assets, including telecommunications equipment and the related goodwill of certain provinces were written down to their recoverable values determined based on their value in use. Value in use is determined based on the present value of estimated future net cash flows expected to arise from the continuing use of the paging assets. In estimating the future net cash flows, the Group has made key assumptions and estimates on the appropriate discount rate adopted (8% per annum) and the period covered by the cash flow forecast, the gradual slow-down in the future loss of customers, the expected stability in average revenue per subscriber, the effects of incremental cash flows arising from new paging businesses and the adoption of cost reduction plans. These assumptions and estimation are made after considering the historical trends, the current market trends and the physical condition of the related assets. Based on the above, the Group recorded impairment losses for property, plant and equipment amounting to approximately RMB468 million and for goodwill amounting to approximately RMB164 million for the year ended 31 December 2001.

In 2001, the Group also recognised loss on disposal of property, plant and equipment of approximately RMB54 million (2000: RMB278 million).

21. GOODWILL

	Consolidated As of 31 December	
	2001	2000
	RMB'000	RMB'000
Cost	505,485	519,999
Less: Accumulated amortisation	(298,298)	(224,037)
Less: Impairment losses	(163,900)	—
	43,287	295,962

Goodwill represents the excess of purchase consideration over the fair values of the separately identifiable assets acquired for (i) certain local Paging Businesses controlled by the PTA during the restructuring of Guoxin in 1998, amounting to RMB448 million and (ii) minority interests in the provincial subsidiaries of Guoxin after its establishment.

In 2000, Guoxin acquired the minority interests in 28 provincial and municipal subsidiaries. The total purchase consideration amounted to approximately RMB1,803 million. The minority owners' aggregate share of the fair value of net assets as of the effective dates of acquisition were approximately RMB1,779 million and goodwill arising from the acquisition of minority interests amounted to RMB24 million.

21. GOODWILL (Cont'd)

In 2001, Guoxin acquired the minority interests of 3.71% and 0.85% in Heilongjiang Guoxin and Sichuan Guoxin Telecommunications Co. Ltd. ("Sichuan Guoxin"), respectively. The total purchase consideration amounted to approximately RMB19.4 million. The minority owners' aggregate share of the fair value of net assets as of the effective dates of acquisition were approximately RMB18.9 million and goodwill arising from the acquisition of minority interests was immaterial.

The amortisation charge of goodwill for the year ended 31 December 2001 amounted to approximately RMB74,261,000 (2000: RMB100,781,000).

The impairment provision in 2001 represented the write-down of goodwill relating to the Paging Businesses in certain provinces (See note 20).

22. DEFERRED EXPENDITURES

	Consolidated As of 31 December	
	2001	2000
	RMB'000	RMB'000
Interconnection facilities	464,575	477,367
Long-term prepaid rental	599,424	374,566
Other	701,468	240,486
	1,765,467	1,092,419
Less: Accumulated amortisation	(750,029)	(286,550)
	1,015,438	805,869

Amortisation of deferred expenditures for the year ended 31 December 2001 amounted to approximately RMB463,479,000 (2000: RMB109,879,000).

23. INVESTMENT SECURITIES

	Consolidated As of 31 December 2001 RMB'000	2000 RMB'000
Unlisted equity securities in the PRC, at cost	131,212	109,147
Less: Provision for impairment in value	(7,712)	(20,202)
	123,500	88,945

24. INVESTMENTS IN SUBSIDIARIES

	The Company As of 31 December 2001 RMB'000	2000 RMB'000
Unlisted equity investments , at cost	23,190,368	8,542,833

The Company has direct or indirect interests in the following principal subsidiaries. All of these subsidiaries are privately-held limited companies except Unicom Guomai whose shares are listed on the Shanghai Stock Exchange.

24. INVESTMENTS IN SUBSIDIARIES (Cont'd)

As of 31 December 2001, the details of the Company's subsidiaries were as follows:

Name	Place and date of incorporation	Percentage of equity interest held Direct	Indirect	Issued and fully paid capital RMB'000	Principal activities
China Unicom Corporation Limited	The PRC, 21 April 2000	100.00%	—	6,502,490	Telecommunications operation
Guoxin Paging Corporation Ltd.	The PRC, 17 September 1998	—	100.00%	6,825,088	Investment holding
Anhui Guoxin Paging Co., Ltd.	The PRC, 28 October 1998	—	100.00%	263,150	Paging operation
Beijing Telecommunications Paging Co., Ltd.	The PRC, 10 April 1998	—	100.00%	133,661	Paging operation
Chongqing Guoxin Telecommunications Co., Ltd.	The PRC, 21 September 1998	—	100.00%	121,913	Paging operation
Guangdong Guoxin Telecommunications Co., Ltd.	The PRC, 30 September 1998	—	100.00%	1,473,802	Paging operation
Heilongjiang Guoxin Paging Co., Ltd. ("Heilongjiang Guoxin")	The PRC, 10 November 1998	—	95.10%	349,828	Paging operation
Liaoning Guoxin Paging Co., Ltd. ("Liaoning Guoxin")	The PRC, 11 November 1998	—	70.85%	372,000	Paging operation
Sichuan Guoxin Telecommunications Co., Ltd. ("Sichuan Guoxin")	The PRC, 30 September 1998	—	100.00%	386,628	Paging operation
Yunnan Guoxin Telecommunications Co., Ltd.	The PRC, 28 September 1998	—	100.00%	159,139	Paging operation
Unicom Guomai Communications Co., Ltd. ("Unicom Guomai")	The PRC, 24 November 1992	—	58.88%	364,883	Pagingoperation

24. INVESTMENTS IN SUBSIDIARIES (Cont'd)

As of 31 December 2001, Guoxin has already acquired all of the minority interests of 28 subsidiaries and part of the minority interests of Heilongjiang Guoxin and Liaoning Guoxin. Except for Heilongjiang Guoxin, Liaoning Guoxin and Unicom Guomai, the aforementioned 28 Paging Businesses have become wholly-owned subsidiaries of Guoxin. The legal status of 22 of these subsidiaries has been subsequently deregistered during 2001.

In 2001, the Company has contributed cash of RMB14,647,535,000 to China Unicom as additional investment.

25. INVESTMENT IN ASSOCIATED COMPANIES

	Consolidated As of 31 December 2001 RMB'000	Consolidated As of 31 December 2000 RMB'000
Cost	**51,145**	51,145
Share of net assets	**(23,940)**	833
	27,205	51,978
Less: Provision for impairment in value	**(23,059)**	(26,278)
	4,146	25,700

Full provision for impairment loss in respect of investments in certain associated companies was made in both 2000 and 2001 when the Group judged that the recoverable amount of these investments would be minimal based on the estimated discounted future net cash flows of the investment. In view of the persistent poor operating results of these associated companies, the Group concluded that the impairments were other than temporary.

25. INVESTMENT IN ASSOCIATED COMPANIES (Cont'd)

As of 31 December 2001, details of investment in associated companies were as follows:

Name	Place and date of incorporation	Percentage of equity interest held Direct	Percentage of equity interest held Indirect	Issued and fully paid capital RMB'000	Principal activities
Beijing Zhongjie Mobile Telecommunications Co., Ltd.	The PRC, 5 April 1999	—	33.00%	10,000	Telecommunications technology
Jiangxi Guoxin Technology Co., Ltd.	The PRC, 27 May 1999	—	23.80%	583	Telecommunications technology
Jiangxi Telecommunication Co., Ltd.	The PRC, 28 December 1993	—	24.00%	7,750	Telecommunications technology
Shanghai Bilder Telecommunications and Construction Co., Ltd.	The PRC, 17 April 1997	—	40.00%	20,000	Telecommunications technology
Shenzhen Jiaxun Co., Ltd.	The PRC, 12 January 2000	—	45.00%	10,000	Telecommunications technology
Shanghai Tianhua Communications Co., Ltd.	The PRC, 16 October 1997	—	40.00%	5,000	Telecommunications technology
Shanghai Guomai Communications and Technology Development Co., Ltd.	The PRC, 10 August 1998	—	49.00%	1,000	Telecommunications technology
Shanghai Beiyan Labor Service Co., Ltd.	The PRC, 12 January 1999	—	48.00%	500	Telecommunications technology
Suzhou Huihong Precision Metal Co., Ltd.	The PRC, 25 January 1994	—	22.50%	13,245	Telecommunications technology
Chengdu Tongfa Champin Communications Co., Ltd.	The PRC, 23 April 1993	—	40.00%	41,590	Telecommunications technology
Sichuan Sutong Expressway Communications Co., Ltd.	The PRC, 8 July 1997	—	30.00%	36,667	Telecommunications technology

26. PAYABLES AND ACCRUED LIABILITIES

	Note	Consolidated		The Company	
		As of 31 December			
		2001	2000	2001	2000
		RMB'000	RMB'000	RMB'000	RMB'000
Payables to contractors and equipment suppliers		13,141,029	10,539,987	—	—
Accrued expenses		717,827	745,043	31,089	7,848
Payables to telecommunications products suppliers		124,928	65,270	—	—
Other	(i)	1,345,652	1,170,867	—	—
		15,329,436	12,521,167	31,089	7,848

Note:

(i) Other includes customer deposits, miscellaneous accruals for housing fund and other government surcharges.

As of 31 December 2001, approximately RMB67 million (2000: RMB231 million) of payables to contractors and equipment suppliers was denominated in US dollars (i.e. US$8 million (2000: US$28 million)).

The aging analysis of payables and accrued liabilities was as follows:

	Consolidated		The Company	
	As of 31 December		As of 31 December	
	2001	2000	2001	2000
	RMB'000	RMB'000	RMB'000	RMB'000
Within one year	13,916,953	12,521,167	31,089	7,848
Over one year	1,412,483	—	—	—
	15,329,436	12,521,167	31,089	7,848

27. SHORT-TERM BANK LOANS

Interest rates on short-term bank loans ranged from 4.19% to 7.72% per annum for 2001 (2000: 4.52% to 7.72% per annum).

Supplemental information with respect to short-term bank loans was:

	Consolidated				
	Balance at year end RMB'000	Weighted average interest rate at year end per annum	Maximum amount outstanding during the year RMB'000	Average amount outstanding during the year* RMB'000	Weighted average interest rate during the year** per annum
31 December 2000					
- secured	377,000				
- unsecured	7,356,817				
	7,733,817	5.80%	7,733,817	4,711,191	5.62%
31 December 2001					
- secured	—				
- unsecured	7,089,000				
	7,089,000	5.80%	10,816,951	7,411,409	5.80%

* The average amount outstanding is computed by dividing the total of outstanding principal balance as of 1 January and 31 December, as applicable, by 2.

** The weighted average interest rate is computed by dividing the total of weighted average interest rates as of 1 January and 31 December, as applicable, by 2.

As of 31 December 2001, short-term bank loans of approximately RMB200 million (2000: Nil) were guaranteed by Unicom Group.

28. LONG-TERM BANK LOANS

	Interest rate and final maturity	Consolidated As of 31 December 2001 RMB'000	2000 RMB'000
Renminbi denominated bank loans	Fixed interest rate ranging from 5.46% to 7.65% per annum with maturity through 2007		
- secured		**17,247,009**	13,383,940
- unsecured		**19,933,362**	14,534,284
		37,180,371	27,918,224
Less: Current portion		**(843,603)**	(766,875)
		36,336,768	27,151,349

The repayment schedule of the long-term bank loans as of 31 December 2001 was as follows:

	RMB'000
Balances due:	
2002	843,603
2003	9,339,561
2004	4,600,135
2005	16,336,839
2006	4,276,763
Thereafter	1,783,470
	37,180,371
Less: Portion classified as current liabilities	(843,603)
	36,336,768

As of 31 December 2001, long-term bank loans were secured by the following:

(i) approximately RMB6,098 million (2000: RMB1,481 million) of long-term bank loans were secured by the future service fee revenue to be generated by the cellular operations of the relevant branches and RMB850 million of which was also guaranteed by Unicom Group;

(ii) approximately RMB1,149 million (2000: RMB1,903 million) of long-term bank loans were secured by the revenue streams and the related property, plant and equipment of the Liaoning GSM and Phases 4 and 5 of the Beijing GSM;

(iii) approximately RMB10,000 million (2000: RMB10,000 million) of long-term bank loans were secured by cash inflows generated from the operations.

(iv) approximately RMB3,403 million (2000 : Nil) of long-term bank loans were guaranteed by Unicom Group.

29. OBLIGATIONS UNDER FINANCE LEASES

Obligations under finance leases were analysed as follows:

	Consolidated As of 31 December 2001 RMB'000	2000 RMB'000
Total minimum lease payments under finance leases repayable:		
- not later than one year	8,642	—
- later than one year and not later than five years	34,569	—
- later than five years	163,127	—
	206,338	—
Less: future finance charges	(97,430)	—
Present value of minimum obligations	108,908	—
Representing obligations under finance leases:		
- current liabilities	8,151	—
- non-current liabilities	100,757	—

	Consolidated As of 31 December 2001 RMB'000	2000 RMB'000
The present value of obligations under finance leases:		
- not later than one year	8,151	—
- later than one year and not later than five years	28,224	—
- later than five years	72,533	—
	108,908	—
Less: Amount due within one year included in current liabilities	(8,151)	—
	100,757	—

Interest rate of obligations under finance leases is at 6% per annum.

30. SHARE CAPITAL

	As of 31 December 2001 RMB'000	As of 31 December 2000 RMB'000
Authorised:		
30,000,000,000 ordinary shares of HK$ 0.1 each	3,000,000	3,000,000

	As of 31 December 2001			As of 31 December 2000		
	Number of shares ('000)	HK$'000	RMB equivalent RMB'000	Number of shares ('000)	HK$'000	RMB equivalent RMB'000
Issued and fully paid:						
Unicom BVI	9,725,000	972,500	1,030,850	9,725,000	972,500	1,030,850
Public investors	2,827,996	282,799	300,521	2,827,996	282,799	300,521
	12,552,996	1,255,299	1,331,371	12,552,996	1,255,299	1,331,371

Pursuant to the resolution passed on 21 April 2000, 9,725,000,020 shares of HK$0.10 each were allotted and issued to Unicom BVI for the transfer of the entire interest in China Unicom to the Company.

Pursuant to the resolution passed on 20 June 2000, the Company completed its Global Offering as follows:

(i) issued an aggregate of 2,459,127,000 shares of HK$0.10 each including an offering of 122,956,000 shares at HK$15.42 per share on The Stock Exchange of Hong Kong Limited ("HKSE") (excluding the brokerage fee and HKSE transaction levy) and an offering of 233,617,100 ADSs (each ADS represents 10 shares) at US$19.99 (HK$15.58 each) on the New York Stock Exchange Inc., on 22 June 2000 and 21 June 2000 respectively; and

(ii) issued 368,869,050 shares of HK$0.10 each at HK$15.58 per share by way of a placing among professional and institutional investors on 3 July 2000 upon the full exercise of an over-allotment option.

The listing proceeds of the aforementioned Global Offering of shares, net of direct listing expenses, amounted to approximately RMB45,275,152,000. The resulting share premium amounted to approximately RMB44,974,631,000.

31. SHARE OPTION SCHEME

On 1 June 2000, the Company adopted a share option scheme (the "Share Option Scheme") pursuant to which 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 up to a maximum aggregate number of shares (including those that could be subscribed for under the pre-global offering share option scheme as described below) equal to 10% of the total issued share capital of the Company. According to the Share Option Scheme, the nominal consideration payable by a participant for the grant of options will be HK$1.00. The exercise price payable by a participant upon the exercise of an option will be determined by the Directors at their discretion at the date of grant, except 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 prices of shares on the HKSE on the five trading days immediately preceding the date of grant of the option on which there were dealings in the shares on the HKSE.

The period during which an option may be exercised will be determined by the directors at their discretion, except that no option may be exercised later than 10 years from 22 June 2000. According to a resolution of the Board of Directors in June 2001, the Company has granted 6,724,000 share options under the Share Option Scheme which represent, on their full exercise, 6,724,000 shares to certain employees of the Group in the following terms:

(i) the price of a share payable by a participant upon the exercise of an option shall be HK$15.42 (excluding the brokerage fee and HKSE transaction levy); and

(ii) the period during which an option may be exercised commences from the date of grant of the options and will end by 22 June 2010.

On 1 June 2000, the Company also adopted a fixed award pre-global offering share option scheme (''Pre-Global Offering Share Option Scheme''), the principal terms of which are the same as the Share Option Scheme in all material aspects except that:

(i) 27,116,600 options were granted on 22 June 2000 to the senior management, including directors, and certain other employees, which represent, on their full exercise, 27,116,600 shares;

(ii) the exercise price is equivalent to the share issue price of the Global Offering of HK$15.42 per share (excluding the brokerage fee and HKSE transaction levy); and

(iii) the options are exercisable after 2 years from grant date and expire 10 years from the date of grant.

No options have been exercised since the date of grant under the Share Option Scheme and Pre-Global Offering Share Option Scheme and up to the date when the Board of Directors approved the financial statements.

32. SHARE WARRANTS

On 22 June 2000, share warrants were granted by the Company to the CJVs or their designees as part of the compensation for termination of the CCF Arrangements (see Note 11). As of 31 December 2001, all share warrants were expired and no share warrants were exercised by these CJVs or their designees.

33. RELATED PARTY TRANSACTIONS

(a) **Transactions with Unicom Group**

The following is a summary of significant recurring transactions carried out with Unicom Group and its subsidiaries. In the directors' opinion, these transactions were carried out on normal commercial terms in the ordinary course of business.

	Note	Year ended 31 December 2001 RMB'000	2000 RMB'000
Transactions with Unicom Group:			
Interconnection and roaming revenues	(i), (iii)	**875,305**	339,536
Interconnection and roaming charges	(ii), (iii)	**298,828**	131,315
Rental charges for premises, equipment and facilities	(iv)	**21,257**	24,121
Revenue for leasing of transmission line capacity	(v)	**216,113**	168,556
Commission revenue for sales agency services	(vi)	**14,560**	259,981
Transactions with subsidiaries of Unicom Group:			
Leasing of satellite transmission capacity	(vii)	**61,778**	62,394
Purchase of telecom cards	(viii)	**1,255,533**	476,827
Commission expenses for sales agency services incurred for telecom cards	(ix)	**2,616**	5,033
Rental charges for leasing of transmission line	(x)	**16,882**	—
Agency fee incurred for procurement of telecommunications equipment	(xi)	**124,451**	54,421
Rental charge for the PRC corporate office	(xii)	**10,131**	10,131

Note:

(i) Interconnection revenues represent the amounts received or receivable from Unicom Group for calls from its networks to the Group's networks. Roaming revenues represent revenue for calls made using the Group's networks by Unicom Group's subscribers.

(ii) Interconnection charges are for calls made from the Group's networks to Unicom Group's networks. Roaming expenses represent expenses for calls made by the Group's subscribers using Unicom Group's networks.

33. RELATED PARTY TRANSACTIONS (Cont'd)

(a) **Transactions with Unicom Group (Cont'd)**

(iii) Interconnection settlement between Unicom Group's network and the Group's network is based on standards established from time to time by the MII. In the case of calls between cellular subscribers in different provinces, settlement is based on either the standards established by the MII or an internal settlement arrangement applied by Unicom Group based on their respective internal costs of providing this service. Also, charges for roaming services between the Group and Unicom Group are based on their respective internal costs of providing these services.

(iv) Prior to the establishment of China Unicom, the Group was provided with premises, equipment and facilities by Unicom Group. Rentals were paid based on the depreciation costs of the related premises, equipment and facilities. Upon the establishment of China Unicom in 2000, China Unicom signed a service agreement with Unicom Group to lease premises, equipment and facilities from Unicom Group. Rentals are based on the lower of depreciation costs and market rates.

(v) Following the Restructuring, Unicom Group leases transmission line capacity from the Group in accordance with the relevant provision of the service agreement. Revenue for leases of transmission line capacity are based on tariffs stipulated by MII from time to time less a discount of up to 10%.

(vi) For 2001 and 2000, Guoxin acted as the sales agent of Unicom Group to sell telecommunications products (such as SIM cards and prepaid cards). In return, Guoxin receives agency commission from Unicom Group at fixed rates based on commission rates stipulated by Unicom Group applicable to third party sales agents.

(vii) Satellite transmission capacity leasing fees represent the amounts paid or payable to China United Telecommunications Satellite Communication Company Limited ("Unisat"), a subsidiary of Unicom Group, for the use of satellite transmission capacity. The charges are based on the MII regulations then in effect less the applicable discount up to 10% as agreed with Unisat.

(viii) Prior to the establishment of China Unicom, the Group purchased subscriber identity module cards, Internet protocol phone cards and prepaid rechargeable calling cards at fixed prices from Unicom Xingye Science and Technology Trade Co. ("Unicom Xingye"), a subsidiary of Unicom Group. Upon the establishment of China Unicom in 2000, China Unicom signed a service agreement with Unicom Group to purchase telecom cards from Unicom Group (to be imported by Unicom Xingye) at cost plus a margin to be agreed from time to time, but not to exceed 20%, and subject to appropriate volume discounts.

(ix) For 2001 and 2000, Unicom International (HK) Limited a subsidiary of Unicom Group, provided sales agency services such as selling of telecommunications cards to the Group. The commission expenses are charged based on market rates.

(x) In 2001, the Group leased transmission line capacity from Unicom International (HK) Limited and China Unicom International Limited, both are subsidiaries of Unicom Group, in accordance with the relevant provision of the service agreement. Leased line expenses are charged based on market rates.

(xi) Prior to the establishment of China Unicom, the Group purchased certain foreign and domestic telecommunications equipment and materials through Unicom Import and Export Co., Ltd. ("Unicom I/E Co."), a subsidiary of Unicom Group, at an agency fee of 1% of the value of the equipment. Upon the establishment of China Unicom in 2000, China Unicom signed a service agreement with Unicom Group, in which Unicom Group agreed to provide equipment procurement services to China Unicom (through Unicom I/E Co.). Unicom I/E Co. charges the Group 0.7% of the value of imported equipment and 0.5% of the value of domestic equipment for such services.

33. RELATED PARTY TRANSACTIONS (Cont'd)

(a) Transactions with Unicom Group (Cont'd)

(xii) Upon the establishment of China Unicom, Unicom Group signed a rental agreement with Unicom Xingye, under which Unicom Xingye leases office premises to China Unicom at its PRC corporate office. Monthly rental is calculated on the basis of US$20 per square meter.

(xiii) Unicom Group is the registered proprietor of the "Unicom'' trademark in English and the trademark bearing the "Unicom" logo, which are registered at the PRC State Trademark Bureau. Pursuant to an exclusive PRC trademark license agreement entered into between Unicom Group and China Unicom, China Unicom and its affiliates are granted the right to use these trademarks on a royalty free basis for an initial period of five years, renewable at China Unicom's option.

(xiv) According to the Multiple Service Agreement signed between the Group and Unicom Paging Limited ("Unicom Paging, a subsidiary of Unicom Group") dated 1 August 2001, the Group and Unicom Paging agree to share the right to use the other party's logo and trademark in the paging business at no cost. In addition, the Agreement also specifies the basis of allocating common expenses incurred by each party for any shared resources and facilities. For the year ended 31 December 2001, management considered that the amount of common expenses involved was insignificant.

(b) Loans from Unicom Group

Loans of approximately RMB10,502 million as of 31 December 1999 were provided by Unicom Group to finance the operations and network construction of the Cellular Business and to finance the settlement payments for the terminations of the CCF Arrangements as described in Note 11. In order to provide these loans to the Cellular Business, Unicom Group borrowed from various banks at the interest rates ranging from 5.85% to 7.2% for 2000. Unicom Group allocated these bank loans to the Cellular Business based on the amount of funds actually utilised by the Cellular Business. The corresponding interest expenses were also charged to the Cellular Business based on the loan amounts allocated. For the year ended 31 December 2000, interest on loans from Unicom Group amounted to approximately RMB48,313,000. Upon the establishment of China Unicom in 2000, these loans were restructured into long-term loans borrowed directly by China Unicom.

(c) Amounts due from and to related parties

Amounts due from and to related parties are unsecured, non-interest bearing, repayable on demand and arise in the ordinary course of business in respect of transactions with subsidiaries of Unicom Group as described in (a) above.

(d) Leasing of CDMA network capacity

On 22 November 2001, China Unicom entered into a conditional lease agreement (the "Lease Agreement") with Unicom Group and Unicom New Horizon Mobile Telecommunications Company Limited ("Unicom New Horizon"), which is a subsidiary of Unicom Group. Pursuant to this Lease Agreement, Unicom Group and Unicom New Horizon agreed to lease the capacity of CDMA network being constructed by Unicom Group to China Unicom covering the 9 provinces of Guangdong, Jiangsu, Zhejiang, Fujian, Liaoning, Shandong, Anhui, Hebei, Hubei and the 3 municipalities of Beijing, Shanghai and Tianjin.

Commencement of the Lease Agreement is conditional upon, among others, the following conditions having been fulfilled:

- Satisfactory testing, initial acceptance and delivery of Phase 1 of the CDMA network in accordance with the Lease Agreement;
- Unicom Group providing or procuring that China Unicom is provided with all spectrum and number resources required by China Unicom for the operation of Phase 1 of the CDMA network;

33. RELATED PARTY TRANSACTIONS (Cont'd)

(d) Leasing of CDMA network capacity (Cont'd)

- Unicom Group and Unicom New Horizon having obtained all necessary government approvals to perform their respective obligations under the Lease Agreement;
- China Unicom having obtained approval from the MII to operate the CDMA network;
- The MII having approved the CDMA tariff plan;
- The passing of resolutions by the independent shareholders approving the Lease Agreement and the related connected transactions; and
- The Hong Kong Stock Exchange granting to the Company a waiver from strict compliance with the provisions of the Listing Rules relating to the Lease Agreement and the related connected transactions.

The term of the Lease Agreement is for an initial period of one year (the "Initial Lease Term"), commencing from the second business day following the fulfillment of the above conditions, among others, as set out in the Lease Agreement, or 1 January 2002, whichever is later.

Other major terms of the Lease Agreement include the following:

(i) China Unicom has the exclusive right to lease and operate the CDMA network capacity in the aforementioned provinces/municipals from Unicom New Horizon;

(ii) The lease period is renewable for further one year terms at the option of China Unicom ("Additional Lease Term");

(iii) The lease fee will be calculated so as to enable Unicom New Horizon to recover its investment in constructing the CDMA network within 7 years, together with an internal rate of return of 8%;

(iv) China Unicom may not reduce the amount of capacity leased or committed to be leased by it during the Initial Lease Term. However, subject to providing not less than 180 days' prior written notice to or with the prior written consent of Unicom New Horizon, China Unicom may reduce the amount of capacity leased for any Additional Lease Term, provided that China Unicom must lease all capacity which it has requested or otherwise committed to lease for at least one year following the date of delivery or renewal of the lease of such capacity;

(v) China Unicom has the option to purchase the CDMA network (the "Purchase Option"), which may be exercised at any time during the Initial Lease Term or any Additional Lease Term of the lease and within 1 year thereafter;

33. RELATED PARTY TRANSACTIONS (Cont'd)

(d) Leasing of CDMA network capacity (Cont'd)

(vi) The acquisition price under the Purchase Option shall be negotiated between Unicom New Horizon and China Unicom, based on the appraised value of the CDMA network determined in accordance with PRC laws and regulations and taking into account prevailing market conditions and other factors, provided that it will not exceed such price as would, added together with the lease fee payments made by China Unicom to Unicom New Horizon, enable Unicom New Horizon to recover its investment in the CDMA network, together with an internal rate of return on its investment of 8%;

(vii) China Unicom may terminate the lease by not less than 180 days' prior written notice, with effect from the end of any Additional Lease Term.

Upon the fulfillment of all the conditions precedent to the commencement of the Lease Agreement, the Initial Lease Term commenced in January 2002.

(e) Amounts due to Unicom Group

The following table summarises the activities between the Group and Unicom Group and the resulting balance due to Unicom Group:

	Consolidated Year ended 31 December 2001 RMB'000	2000 RMB'000
Due to Unicom Group, beginning of year	**821,797**	505,367
Interconnection and roaming revenues	**(875,305)**	(339,536)
Interconnection and roaming charges	**298,828**	131,315
Due to Unicom Group arising from network construction costs paid by Unicom Group for China Unicom	**702,614**	524,651
Due to Unicom Group, end of year	**947,934**	821,797

The outstanding amounts were unsecured, non-interest-bearing and payable within one year. The average outstanding balances during 2001 were approximately RMB884,866,000 (2000: RMB636,480,000).

34. TRANSACTIONS WITH CHINA TELECOM

The Group's telecommunications operations depend, in large part, on interconnection with China Telecom's public switched telephone network and on transmission lines leased from China Telecom.

(a) Transactions with China Telecom

The following is a summary of significant transactions with China Telecom:

	Note	Consolidated Year ended 31 December 2001 RMB'000	2000 RMB'000
Interconnection revenue	(i)	**461,133**	298,596
Interconnection charges	(i)	**1,375,852**	1,145,913
Leased line charges	(ii)	**668,386**	1,008,077
Operating lease charges	(iii)	**33,127**	135,075
Agency fee on collection of revenue	(iv)	**2,665**	108,943
Social service fees	(v)	**—**	15,907

Notes:

(i) The interconnection revenue and charges mainly represent the amounts due from or to China Telecom for cellular telephone calls made between the Group's cellular networks and the public switched telephone network of China Telecom. The interconnection settlements are calculated in accordance with interconnection agreements reached between the Cellular Business and China Telecom on a provincial basis. The terms of these agreements are set in accordance with the standard settlement arrangement stipulated by the MII.

(ii) Leased line charges are paid or payable to China Telecom by the Group for leasing China Telecom's transmission line. The charges are calculated at a fixed charge per line, depending on the number of lines being used.

(iii) Prior to the establishment of Guoxin, China Telecom charged the Paging Business for the use of certain land and buildings at cost. Upon its establishment, Guoxin signed operating lease agreements with the PTAs for the use of certain land and buildings. The rentals are based on the market rates in the locality of the land and building.

(iv) Prior to the establishment of Guoxin, China Telecom charged the Paging Business for sales agency services at cost. Upon its establishment, Guoxin signed agency agreements with the PTAs for sales agency services based on standard commission rates, being the prevailing market rates in the locality. Charges for collection services are calculated at a fixed percentage of fees collected from subscribers.

(v) Prior to the establishment of Guoxin, China Telecom charged the Paging Business for various social services, such as property management, meal and other social services, at cost. Upon its establishment, Guoxin signed social service agreements with China Telecom to provide such services at a fixed amount per employee annually. For 2001, such social service agreement was terminated and no more services have been rendered by China Telecom.

34. TRANSACTIONS WITH CHINA TELECOM (Cont'd)

(b) Amounts due from and to China Telecom

	Consolidated As of 31 December 2001 RMB'000	2000 RMB'000
Amounts due from China Telecom		
- revenue collected on behalf of Guoxin	258,317	485,434
- less: provision for doubtful debts	(58,857)	(109,188)
	199,460	376,246
Amounts due to China Telecom		
- payables for interconnection charges, leased lines, operating leases, social service fees, etc.	742,366	1,276,965
Long-term payable due to China Telecom		
- payables for obligations under finance leases:		
- current portion of obligations under finance leases	8,151	—
- obligations under finance leases	100,757	—
	108,908	—

All amounts due from and to China Telecom were unsecured, non-interest-bearing and repayable within one year.

Long-term payable for obligations under finance lease was related to the leasing of certain subsea transmission cables from China Telecom for a period of 25 years. (Note 29).

35. FINANCIAL INSTRUMENTS

The carrying amounts of the Group's cash and cash equivalents short-term bank deposits approximate their fair values because of the short maturity of those instruments. Cash and cash equivalents and short-term bank deposits denominated in foreign currencies summarised as below, have been translated to RMB at the applicable rates quoted by the People's Bank of China.

	Consolidated As of 31 December 2001 Original Currency ('000)	Exchange rate	RMB equivalent ('000)	2000 Original Currency ('000)	Exchange rate	RMB equivalent ('000)
Cash and cash equirvalent						
– denonrinated in HK$	1,777,224	1.06	1,886,523	8,264,893	1.06	8,765,746
– denonrinated in US dollars	899,868	8.28	7,448,635	3,588,218	8.27	29,683,891
Sub-total			9,335,158			38,449,637
Short-term bank deposits						
– denonrinated in HK$	5,941,644	1.06	6,307,055	1,647,445	1.06	1,747,280
– denonrinated in US dollars	2,222,981	8.28	18,400,664	730,926	8.27	6,046,655
Sub-total			24,707,19			7,793,935
Total			34,042,877			46,243,572

The Group did not have and does not believe it will have any difficulty in exchanging its foreign currency cash into RMB at the exchange rates quoted by the People's Bank of China. The carrying amounts of the bank loans approximate their fair values based on borrowing rates currently available for bank loans with similar terms and maturities.

36. CONTINGENCIES AND COMMITMENTS

(a) Capital commitments

As of 31 December 2001, the Group had capital commitments, mainly in relation to the construction of telecommunications networks, as follows:

	Land use rights and buildings RMB'000	Equipment RMB'000	Total RMB'000
Authorised and contracted for	574,205	9,382,730	9,956,935
Authorised but not contracted for	89	78,587	78,676
Total	574,294	9,461,317	10,035,611

As of 31 December 2001, approximately RMB662 million (2000: RMB1,387 million) of capital commitment outstanding was denominated in US dollars (i.e. US$80 million (2000: US$167 million)).

36. CONTINGENCIES AND COMMITMENTS (Cont'd)

(b) Operating lease commitments

As of 31 December 2001, the Group had the following commitments under operating leases:

	Land use rights and buildings RMB'000	Equipment RMB'000	Total RMB'000
Leases expiring in:			
2002	231,064	1,723,897	1,954,961
2003	176,080	83,786	259,866
2004	166,038	49,891	215,929
2005	133,164	43,312	176,476
2006	120,639	30,570	151,209
Thereafter	481,206	278,490	759,696
Total	1,308,191	2,209,946	3,518,137

As of 31 December 2001, the Company had the following commitments under operating leases:

	Land and buildings RMB'000	Equipment RMB'000	Total RMB'000
Leases expiring in:			
2002	1,550	—	1,550
2003	22,641	—	22,641
Total	24,191	—	24,191

As of 31 December 2001, the Group and the Company had no significant contingent liabilities.

(c) Commitment of CDMA network

In accordance with the Lease Agreement among China Unicom, Unicom Group and Unicom New Horizon, China Unicom has agreed to lease CDMA network capacity from Unicom New Horizon to the Group to provide CDMA cellular communication services in 9 provinces and 3 municipalities (See Note 33(d)). The term of the lease is for an initial period of one year, start from January 2002. Based on a forecast of CDMA subscriber growth and the anticipated capacity of the lease, China Unicom estimates that the total lease fee payable during the Initial Lease Term will be approximately RMB1.47 billion.

37. EVENTS AFTER BALANCE SHEET DATE

On 6 March 2002, Unicom Xingye Science and Technology Trade Co. settled the amount due to the Group of approximately RMB464,439,000 as of 31 December 2001.

38. COMPARATIVE FIGURES

Certain comparative figures have been reclassified in accordance with new disclosure requirement under new HK SSAP.

39. CONCENTRATION OF RISK

Business risks

The Group conducts its operations in the PRC and accordingly is subject to special considerations and significant risks not typically associated with investments in equity securities in the United States of America and Western European countries. These include risks associated with, among others, the political, economic and legal environments, influence of national authorities over tariff-setting and competition in the industry and spectrum availability.

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 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, will not have a material adverse impact on the Group's business, financial conditions and results of operations.

Competition

The Cellular Business of the Group currently faces intense competition from China Mobile Communication Corporation ("China Mobile"). In addition, the Paging Busiiners and Long Distance, Data and Internet Business of the Group also faces intense competition from China Telecom and other operators in the PRC. China Mobile and China Telecom have competitive advantage over the Group in terms of geographic coverage, financial resources, and brand recognition. Intensified competition from China Mobile and China Telecom may adversely affect the business operations and financial conditions of the Group.

Technological changes

The telecommunications industry is characterised by rapid and significant technological changes. The current telecommunications technologies of the Group may become obsolete or subject to competition from new technologies, which could increase subscriber churn rate, and adversely affect the results of operations and prospects of the Group.

Spectrum availability

The Group's telecommunications network is limited by the amount of spectrum allocated by the Chinese government. There is no assurance that the Group will be granted additional spectrum on acceptable terms. Any levels of system congestion could result in subscriber dissatisfaction, decreased system usage and increased churn rate, and any material increase in spectrum fees could adversely affect the results of operations of the Group.

Dependence on China Telecom's leased lines and interconnection arrangement

The Group's telecommunications businesses depend in large part upon access to China Telecom's public switched telephone network. Limitations on the public switched telephone network may lead to lower domestic, long-distance and international call completion rates for the Group's subscribers. There can be no assurance that the increasing usage of the Group's telecommunications services will not result in additional strain on the network switching capacity, or that the existing quality of the public switched telephone network will remain adequate.

In addition, the Group's operating revenues and costs are affected by the terms of its interconnection arrangement with China Telecom. Any material increase in costs associated with the interconnection could significantly and adversely affect the results of operations of the Group. There is no assurance that the terms of future interconnection arrangements will be commercially acceptable to the Group.

39. CONCENTRATION OF RISK (Cont'd)

Adequate financing for future expansion

Substantial financing will be required by the Group to broaden the existing range of telecommunications services and develop new services. There is no assurance that sufficient financing will be available to the Group on acceptable terms. If adequate capital is not available, the business prospects of the Group will be adversely affected.

Credit risks

As of 31 December 2001, cash and cash equivalents and short-term bank deposits were mainly maintained with state-owned banks in the PRC and commercial banks in Hong Kong.

Foreign currency risk

The Group has foreign currency risk as certain of its payables to equipment suppliers are denominated in foreign currencies, principally US dollars. Fluctuations in the exchange rates of RMB against foreign currencies could affect the Group's results of operations.

Interest rate risk

The interest rates and terms of repayment of bank loans and other loans of the Group are disclosed in Notes 27 and 28.

40. SEGMENT INFORMATION

Operating segments represent components of an enterprise regarding which separate financial information is available for regular evaluation by the chief operating decision maker, or decision making group, in deciding how to allocate resources and in assessing performance.

The Group organises its business segments based on the various types of telecommunications services provided to customers in different provinces in the PRC. The major business segments operated by the Group are classified as below:

- Cellular Business — the provision of cellular GSM telephone and related services;
- Paging Business — the provision of paging and related services;
- Long Distance, Data and Internet Business — the provision of domestic and international long distance telephony, data, Internet and other related services.

The operating segments are managed separately because each operating segment represents a strategic business unit that serves different markets. All the operating segments of the Group have been aggregated into the above reportable segments since they are expected to exhibit similar future economic characteristics to these reportable segments.

As the major telecommunications services of the Group operate autonomously under separate management teams at separate locations, most of the assets, liabilities, revenues and expenses are clearly identifiable to business segments. Allocation of centrally incurred costs amongst the different segments is not significant.

The Group's primary measure of segment income is based on segment income or loss before income tax.

40. SEGMENT INFORMATION (Cont'd)

(a) Business segments

Year ended 31 December

	2001						2000					
	Cellular Business RMB'000	Paging Business RMB'000	Long Distance, Data and Internet Business RMB'000	Unallocated amounts RMB'000	Elimination RMB'000	Total RMB'000	Cellular Business RMB'000	Paging Business RMB'000	Long Distance, Data and Internet Business RMB'000	Unallocated amounts RMB'000	Elimination RMB'000	Total RMB'000
Revenue:												
Usage fee	14,937,448	—	2,120,997	—	—	17,058,445	8,212,332	—	470,526	—	—	8,682,858
Monthly fee	3,660,473	4,141,232	—	—	—	7,801,705	2,476,104	7,992,999	7,076	—	—	10,476,179
Connection fee	204,986	1,595	—	—	—	206,581	517,642	68,233	—	—	—	585,875
Interconnection revenue	1,262,267	—	724,624	—	—	1,986,891	753,591	—	293,745	—	—	1,047,336
Leased lines rental	—	—	427,195	—	—	427,195	—	—	321,255	—	—	321,255
Other revenue	439,884	198,997	36,128	—	—	675,009	228,135	422,258	3,792	—	—	654,185
Total services revenue	20,505,058	4,341,824	3,308,944	—	—	28,155,826	12,187,804	8,483,490	1,096,394	—	—	21,767,688
Sales of telecommunications products	820,585	416,475	—	—	—	1,237,060	696,058	1,228,712	—	—	—	1,924,770
Total revenue from external customers	21,325,643	4,758,299	3,308,944	—	—	29,392,886	12,883,862	9,712,202	1,096,394	—	—	23,692,458
Intersegment revenue	651	66,734	1,169,929	—	(1,237,314)	—	—	180,701	455,722	—	(636,423)	—
Total revenues	21,326,294	4,825,033	4,478,873	—	—	29,392,886	12,883,862	9,892,903	1,552,116	—	—	23,692,458
Operating expenses:												
Leased lines	(533,455)	(307,348)	(430,532)	—	418,029	(853,306)	(580,596)	(759,025)	(274,224)	—	455,722	(1,158,123)
Interconnection charges	(2,195,396)	—	(634,345)	—	757,157	(2,072,584)	(1,268,574)	—	(110,891)	—	—	(1,379,465)
Depreciation and amortisation	(5,556,317)	(1,754,973)	(947,372)	(3,634)	—	(8,262,296)	(3,605,529)	(1,827,535)	(300,887)	(364)	—	(5,734,315)
Personnel	(1,106,962)	(937,198)	(410,112)	(32,946)	—	(2,487,218)	(361,914)	(1,354,964)	(52,962)	—	—	(1,769,840)
Selling and marketing	(2,486,867)	(478,478)	(708,854)	—	61,309	(3,612,890)	(1,426,829)	(952,210)	(294,095)	—	180,701	(2,492,433)
General, administrative and other expenses	(3,046,235)	(1,760,688)	(644,082)	(48,811)	819	(5,498,997)	(1,772,753)	(1,809,425)	(146,706)	(14,179)	—	(3,743,063)
Cost of telecommunications products sold	(788,218)	(554,026)	—	—	—	(1,342,244)	(380,849)	(1,812,089)	—	—	—	(2,192,938)
Total operating expenses	(15,713,450)	(5,792,711)	(3,775,297)	(85,391)	—	(24,129,535)	(9,397,044)	(8,515,248)	(1,179,765)	(14,543)	—	(18,470,177)

40. SEGMENT INFORMATION (Cont'd)

(a) Business segments (Cont'd)

	Year ended 31 December											
	2001						2000					
	Cellular Business RMB'000	Paging Business RMB'000	Long Distance, Data and Internet Business RMB'000	Unallocated amounts RMB'000	Elimination RMB'000	Total RMB'000	Cellular Business RMB'000	Paging Business RMB'000	Long Distance, Data and Internet Business RMB'000	Unallocated amounts RMB'000	Elimination RMB'000	Total RMB'000
Operating income (loss)	5,612,844	(967,678)	703,576	(85,391)	—	5,263,351	3,486,818	1,377,655	372,351	(14,543)	—	5,222,281
Financial income	31,544	23,493	3,078	2,038,857	—	2,096,972	100,944	52,320	636	1,594,905	—	1,748,805
Financial expense	(1,560,826)	(40,569)	(316,171)	—	—	(1,917,566)	(1,149,432)	—	(204,314)	—	—	(1,353,746)
Loss arising from terminations of CCF Arrangements	—	—	—	—	—	—	(1,184,534)	—	(9,304)	—	—	(1,193,838)
Other (expenses) income, net	(842)	(6,159)	(1,544)	28,376	—	19,831	9,493	49,736	—	—	—	59,229
Segment income (loss) before taxation and minority interests	4,082,720	(990,913)	388,939	1,981,842	—	5,462,588	1,263,289	1,479,711	159,369	1,580,362	—	4,482,731
Taxation					—	(1,041,137)					—	(1,104,969)
Income before minority interests					—	4,421,451					—	3,377,762
Minority interests					—	35,310					—	(143,711)
Net income					—	4,456,761					—	3,234,051
Total segment assets	65,320,115	11,306,153	17,057,714	34,220,910	—	127,904,892	42,393,650	14,748,230	8,763,617	46,923,329	—	112,828,826
Total segment liabilities	52,359,025	3,278,990	9,725,220	31,089	—	65,394,324	41,207,608	5,482,298	7,963,449	67,817	—	54,721,172
Other information:												
Provision or (write-back) for doubtful debts	517,663	(14,510)	37,801	—	—	540,954	355,082	85,430	4,319	—	—	444,831
Equity investment for segment assets	—	4,146	—	—	—	4,146	—	25,700	—	—	—	25,700
Impairment loss recognised in the income statement	—	632,511	—	—	—	632,511	—	—	—	—	—	—
Capital expenditures for segment assets (1)	20,777,990	549,338	7,332,060	2,594,071	—	31,253,459	17,277,859	2,178,287	5,713,435	10,655	—	25,180,236

(1) Capital expenditures classified under "unallocated amounts" represent capital expenditure on common facilities, which benefit all business segments.

40. SEGMENT INFORMATION (Cont'd)

(b) Geographical segments

The Group's services users are mainly in the PRC. There is no other geographical segment with segment revenue from external customers equal to or greater than 10% of total consolidated revenue from sales to all external customers.

Although the Group has its corporate headquarters in Hong Kong, a substantial portion of the Group's non-current assets (including property, plant and equipment, intangible assets and other assets) are situated in the PRC, as the Group's principal activities are conducted in the PRC. For the year ended 31 December 2001, substantially all capital expenditures were incurred to acquire assets located in the PRC. There is no other geographical segment with segment assets equal to or greater than 10% of the total assets of all geographical segments.

The accounting policies adopted by the Group to conform to HK GAAP differ in certain respects from the generally accepted accounting principles in the United States of America ("US GAAP"). The principal differences having a significant effect on the financial statements are set out below.

(a) **Revenue and costs recognition**

Under HK GAAP, upfront non-refundable revenue, such as connection fees, is recognised when received upon completion of activation services. Under US GAAP, in accordance with Staff Accounting Bulletin No. 101, "Revenue Recognition in Financial Statements'', upfront non-refundable revenue and the related direct incremental costs incurred are deferred and recognised over the estimated customer service periods. The expected customer service period for the Cellular Business is estimated based on the expected stabilised churn rates. On this basis, the weighted average customer service period based on current estimation considering the prevailing market environment is approximately 6 years (2000: 10 years). The effect of this change of estimate was to increase the net income by approximately RMB26 million for the year ended 31 December 2001.

(b) **Employee housing schemes**

Prior to the establishment of Guoxin and China Unicom, both China Telecom and Unicom Group, provided housing benefits to qualified employees of the Group to enable them to purchase living quarters. Under HK GAAP, housing benefits incurred and borne by China Telecom and Unicom Group for these employees were not recognised by the Group. Under US GAAP, the amount of such housing benefits was recorded as the Group's operating expenses over the estimated average service life of the participating employees. The corresponding amount was recorded as a capital contribution.

(c) **Deferred taxation**

Under HK GAAP, the Group provides for deferred tax liabilities only to the extent that there is a reasonable probability that such deferred taxes will become payable in the foreseeable future. Deferred tax assets are not recognised unless they are expected to crystallise in the foreseeable future. Under US GAAP, a provision is made for all deferred taxes. If it is more likely than not that deferred tax assets will not be realised, a valuation allowance is recorded.

(d) **Revaluation of fixed assets**

Under HK GAAP, revaluation surplus in relation to land and buildings is recorded by the Group. Thereafter, depreciation is provided based on the revalued amounts. Under US GAAP, all fixed assets are stated at historical cost.

(e) **Impairment of long-lived assets**

The carrying amount of fixed assets and goodwill 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 assets discounted to their present value. A subsequent increase in the recoverable amount is written back to the income statement when circumstances and events that led to the write-down or write-off cease to exist.

(e) **Impairment of long-lived assets (Cont'd)**

Under US GAAP Statements of Financial Accounting Standards No. 121 "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed of" ("SFAS 121"), long-lived assets including goodwill 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 evaluated 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 recognised is measured by the amount by which the carrying amounts of the assets exceed the fair value of the assets, which is determined based on the estimated future discounted net cash flows expected to be generated by the asset held for continuous use. Assets impaired or to be disposed of are reported at the lower of the carrying amounts or fair values less costs to sell, which result in a new cost basis for the impaired assets. This new cost basis is not adjusted for subsequent recoveries in value.

Impairment of goodwill is evaluated in connection with a business acquired. For the measurement of impairment of goodwill, the fair value is determined based on the estimated discounted future cash flows of the business acquired. When goodwill is identified with assets that are subject to impairment, the carrying amount of the identified goodwill is eliminated before any reduction of the carrying amounts of impaired long-lived assets.

As impairment of assets is evaluated using undiscounted net cash flow method under US GAAP, the impairment provisions for equipment and goodwill recognised under US GAAP were lower than those recognised under HK GAAP by RMB12,382,000 and RMB62,948,000, respectively for the year ended 31 December 2001. No such difference existed in prior years.

(f) **Losses on debt extinguishment and share warrants**

Under HK GAAP, the loss on CCF termination is accounted for as an operating loss which reduces the income from continuous operations of the Group. Under US GAAP, the amounts were classified as an extraordinary item in accordance with the requirement of SFAS Statement No. 4.

Under HK GAAP, the Company's share warrants granted to the CJVs or their designees as part of the compensation for terminations of CCF Arrangements did not result in an expense. The proceeds received from share warrants would be recognised as an increase to capital upon the exercise of the share warrants. Under US GAAP, an additional charge to income statement was recorded to account for the fair value of the share warrants granted at the completion of the Global Offering. The fair value of these share warrants as of the grant date, using the Black-Scholes option pricing method, was approximately RMB1,132 million. The major assumptions used include: no dividend yield, expected volatility of 50%, risk free interest rate of 6.54% and an expected life of one year.

(g) **Share option scheme**

Under HK GAAP, the proceeds received from the exercise of the share options granted under the fixed award Share Option Scheme and Pre-Global Offering Share Option Scheme are to be recognised as an increase to capital upon the exercise of the share options as stated in Note 31.

(g) **Share option scheme (Cont'd)**

Under US GAAP, the Company applies Accounting Principles Board Opinion No. 25 ("APB 25") to account for its fixed award stock options issued to employees. Under APB 25, compensation expense is recorded in the amount of the excess, if any, of the quoted market price of the shares on the date of grant over the exercise price of the options, which is amortised over the vesting period of the option. Since the exercise price of the options granted did not exceed the market price of the underlying stock on the date of grant, no compensation cost for options has been recognised in the reconciliation of net income to US GAAP. Required disclosures under Statement of Financial Accounting Standards No. 123 , "Accounting for Stock-Based Compensation"("SFAS 123") are provided below.

(h) **Investment in equity securities**

Under HK GAAP, negotiable equity securities including ownership interest in an enterprise, which are intended to be held on a continuing basis, are classified as investment securities and are stated at cost. The carrying amounts of investment securities are written down to reflect any diminution in value expected to be other than temporary. Provisions against the carrying value are reversed when the circumstances and events that led to the write-downs or write-offs cease to exist and if there is persuasive evidence that the new circumstances and events will persist for the foreseeable future.

Under US GAAP, equity securities which are not marketable and do not have readily determinable fair values are classified as other investments, which are stated at cost less impairment in value other than temporary. If an impairment in value is judged to be other than temporary, the cost of the investment is written down to its recoverable amount as a new cost basis and the amount of the write-down is included in the statement of income. The new cost basis is not changed for subsequent recoveries in value.

During the year ended 31 December 2001, the recovery in the value of investments in equity securities amounted to approximately RMB12,305,000 (2000: Nil).

(i) **Derivative instruments**

In June 1998, the Financial Accounting Standard Board ("FASB") issued Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities" ("SFAS 133"). SFAS 133 stipulates accounting and reporting standards for derivative instruments and for hedging activities. SFAS 133 requires an entity to recognise all derivatives as either assets or liabilities in the balance sheet and measure those instruments at their fair values. Changes in fair values for derivatives are recorded in either current income or other comprehensive income, depending on whether a derivative is designed as part of a hedge transaction and the type of the hedge transaction. SFAS 133, as revised by SFAS 137 and SFAS 138, is effective for fiscal years beginning after 15 June 2000. There were no material impacts of the adoption of these new standards on the Group's operating results and financial position.

(j) **Recently issued accounting standards**

During the year, FASB issued Statement of Financial Accounting Standards No. 141, "Business Combinations" ("SFAS 141"), Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" ("SFAS 142"), Statement of Financial Accounting Standards No. 143, Accounting for Asset Retirement Obligations ("SFAS 143") and Statement of Financial Accounting Standards No. 144 "Accounting for the Impairment or Disposal of Long-lived Assets" ("SFAS 144").

(a) SFAS 141 addresses financial accounting and reporting for business combinations and requires that the purchase method of accounting to be used for all business combinations after 30 June 2001. SFAS 141 is effective for fiscal years beginning after 15 December 2001 except for those goodwill and intangible assets acquired after 30 June 2001 or arising from combinations between mutual enterprises.

(b) Under SFAS142, goodwill and certain other intangible assets will no longer be systematically amortised, but instead will be reviewed for impairment annually and written down and charged to results of operations when their carrying amounts exceed their estimated fair values. SFAS 142 is effective for fiscal years beginning after 15 December 2001 except for those goodwill and intangible assets acquired after 30 June 2001 or arising from combinations between mutual enterprises.

(c) SFAS 143 addresses financial accounting and reporting for obligations associated with the retirement of tangible long-lived assets and the associated asset retirement costs. SFAS 143 is effective for fiscal years beginning after 15 June 2002.

(d) SFAS 144 addresses financial accounting and reporting for the impairment or disposal of long-lived assets. The changes in SFAS 144 improve financial reporting by requiring that one accounting model be used for long-lived assets to be disposed of by sale, whether previously held or used or newly acquired, and by broadening the presentation of discontinued operations to include more disposal transactions. SFAS 144 also resolves significant implementation issues related to impairment. SFAS 144 is effective for fiscal years beginning after 15 December 2001.

The Group has not completed its assessment of the effects of adopting SFAS 141, SFAS 142, SFAS 143 and SFAS 144.

Differences between HK GAAP and US GAAP which affect net income of the Group are summarised below:

	Year ended 31 December 2001 RMB'000	Year ended 31 December 2000 RMB'000
Net income under HK GAAP	4,456,761	3,234,051
Impact of US GAAP adjustments:		
- Deferral of upfront non-refundable revenue	(1,001,637)	(1,168,822)
- Amortisation of upfront non-refundable revenue	455,839	252,520
- Deferral of direct incremental cost	934,713	1,071,222
- Amortisation of direct incremental cost	(358,867)	(199,497)
- Employee housing benefits	(18,532)	(18,532)
- Reversal of depreciation for revalued fixed assets	7,485	12,610
- Reversal of revaluation deficit of fixed assets	—	28,000
- Differences in provision for impairment loss of equipment	12,382	—
- Differences in provision for impairment loss of goodwill	62,948	—
- Non-recognition of recovery of impairment provision of investment securities and associated companies	(17,948)	—
- Deferred tax impact arising from deferral and amortisation of upfront non-refundable revenue and incremental costs	63,126	11,370
- Deferred tax impact arising from differences in provision for impairment loss of equipment and goodwill and non-recognition of recovery of impairment provision of investment securities and associated companies	(18,936)	—
- Additional charge relating to the grant of share warrants for the terminations of CCF Arrangements	—	(1,131,806)
- Recognition of deferred tax assets in relation to the loss carryforward from a subsidiary	—	23,582
- Valuation allowance	—	(23,582)
- Recognition of other deferred tax assets	145,098	90,213
Net income as restated (US GAAP)	4,722,432	2,181,329
Add back: Extraordinary item (loss arising from terminations of CCF Arrangements)		
- cash compensation	—	1,193,838
- share warrants compensation	—	1,131,806
- less: related tax impact	—	(393,967)
	—	1,931,677
Income from continuing operations before extraordinary item (US GAAP)	4,722,432	4,113,006
Basic and diluted net income per share after extraordinary item (RMB)	0.38	0.19
Basic and diluted net income per ADS after extraordinary item (RMB)	3.77	1.94
Basic and diluted net income per share before extraordinary item (RMB)	0.38	0.37
Basic and diluted net income per ADS before extraordinary item (RMB)	3.77	3.67

Differences between HK GAAP and US GAAP which affect shareholders' equity of the Group are summarised below:

	Note	Consolidated As of 31 December 2001 RMB'000	Consolidated As of 31 December 2000 RMB'000
Shareholders'equity under HK GAAP		61,681,163	57,224,402
Impact of US GAAP adjustments:			
- Deferred upfront non-refundable revenue		(3,675,556)	(2,673,919)
- Accumulated amortisation of upfront non-refundable revenue		895,544	439,705
- Deferred direct incremental cost		2,843,514	1,908,801
- Accumulated amortisation of direct incremental cost		(581,497)	(222,630)
- Reversal of revaluation surplus of fixed assets:			
- Cost		(176,853)	(176,853)
- Accumulated depreciation		21,453	12,610
- Reversal of revaluation deficit of fixed assets:			
- Cost		28,000	28,000
- Accumulated depreciation		(1,358)	—
- Differences in provision for impairment loss of equipment		12,382	—
- Differences in provision for impairment loss of goodwill		62,948	—
- Non-recognition of recovery of impairment provision of investment securities and associated companies		(17,948)	—
- Deferred tax impact arising from deferred upfront non-refundable revenue, deferred direct incremental costs and the related accumulated amortisation		(194,275)	(257,401)
- Deferred tax impact arising from differences in provision for impairment loss of equipment and goodwill and non-recognition of recovery of impairment provision of investment securities and associated companies		(18,936)	—
- Recognition of deferred tax assets in relation to the loss carryforward from a subsidiary	(i)	107,299	107,299
- Valuation allowance	(i)	(107,299)	(107,299)
- Recognition of other deferred tax assets		373,159	228,061
Shareholders' equity as restated (US GAAP)		61,251,740	56,510,776

Note:

(i) A valuation allowance was recorded against the deferred tax assets in relation to the loss carryforward from a subsidiary prior to 2001 because it is highly uncertain as to whether sufficient future profit can be generated by the subsidiary to utilise the tax loss within the five-year carryforward period allowed under tax laws of the PRC at that time. The operating loss carryforward expire in various years through 2003, if not utilised. Starting from 2001, with the approval of the state tax bureau, loss incurred by this subsidiary can be set off against taxable profits of the Group.

The movement of significant provisions for the years ended 31 December 2001 and 2000 were summarised below:

(a) Provision for deferred taxation valuation allowance was analysed as follows:

	Consolidated As of 31 December 2001 RMB'000	2000 RMB'000
Balance, beginning of year	107,299	83,717
Provision for the year	—	23,582
Balance, end of year	107,299	107,299

(b) There was no other significant movement of provisions for the years ended 31 December 2001 and 2000 except for the provision for impairment loss of equipment amounted to approximately RMB457 million and provision for impairment loss of goodwill amounted to approximately RMB101 million under US GAAP in 2001. (see Note 20 and 21).

Reclassifications

The reconciliation of net income and shareholders' equity from HK GAAP to US GAAP as presented above includes those items which have a net effect on net income or shareholders' equity. Other than the principal differences between HK GAAP and US GAAP explained above, there are no other major GAAP differences which would affect the classification of assets and liabilities or income and expenses.

Statement of Comprehensive Income

According to SFAS No. 130 "Reporting of Comprehensive Income", certain items shown as components of common equity must be more prominently reported in a separate statement as components of comprehensive income. For the year ended 31 December 2001 and 2000, apart from the net income and revaluation surplus of land and buildings in 2000, there was no other comprehensive income which should be included in the statement of comprehensive income.

Statement of Cash Flows

The Group applies Hong Kong Statement of Standard Accounting Practice No. 15 "Cash Flow Statements" ("SSAP 15"). Its objectives and principles are similar to those set out in the United States Financial Accounting Standard Board Statement No. 95 "Statement of Cash Flows" ("FASB 95"). The principal differences between the standards relate to classification. Under SSAP 15, the Group presents its cash flows for (a) operating activities; (b) return on investments and servicing of finance; (c) taxation; (d) investing activities; and (e) financing activities. Cash flows from taxation and returns on investments and servicing of finance would be included as operating activities under FASB 95, with the exception of distributions, which under FASB 95 would be classified as financing activities. Summarised cash flow data by operating, investing and financing activities in accordance with FASB 95 are as follows:

	Year ended 31 December 2001 RMB'000	2000 RMB'000
Net cash inflows from:		
Operating activities	11,077,875	9,343,867
Investing activities	(46,125,017)	(30,550,946)
Financing activities	8,743,467	59,921,403
Changes in cash and cash equivalents	(26,303,675)	38,714,324
Cash and cash equivalents, beginning of year	44,716,685	6,002,361
Cash and cash equivalents, end of year	18,413,010	44,716,685

Share option scheme

As disclosed in Note 31, information relating to the share options outstanding under the Pre-Global Offering Share Option Scheme and Share Option Scheme as of 31 December 2000 and 2001 is as follows:

	Year ended 31 December			
	2001		2000	
	Options outstanding	Weighted average exercise price HK$	Options outstanding	Weighted average exercise price HK$
Outstanding, beginning of year	27,116,600	15.42	—	—
Granted during the year	6,724,000	15.42	27,116,600	15.42
Outstanding, end of year	33,840,600	15.42	27,116,600	15.42

As of 31 December 2001, 6,724,000 share options (2000: Nil) were exercisable and the weighted average exercise price was HK$15.42. Also, as of 31 December 2001, the weighted average remaining contractual life of the options outstanding were approximately 8.5 years (2000: 9.5 years).

The SFAS No. 123 method of accounting is based on several assumptions and should not be viewed as indicative of the operation of the Company in future periods. The estimated fair value of each option granted to the employees of the Group on the date of grant using the Black-Scholes option pricing method with the assumptions as follows:

	Year ended 31 December	
	2001	2000
Estimated fair value (in HK dollars)	4.90	8.14
Risk free interest rate	6%	6%
Expected life (in years)	8	5
Expected dividend yield	0%	0%
Volatility	52%	54%

Had the compensation costs for the plan been determined based on the estimated fair value at the grant dates for awards under the plan consistent with the method of SFAS 123, the Group's net income and net income per share on a pro forma basis for the years ended 31 December 2001 and 2000 would have been as follows:

	Year ended 31 December	
	2001	2000
Net income:		
As reported (RMB'000)	4,722,432	2,181,319
Pro forma (RMB'000)	4,568,479	2,121,670
Basic and net income per share:		
As reported (RMB)	0.38	0.19
Pro forma (RMB)	0.36	0.19
Basic and diluted net income per ADS		
As reported (RMB)	3.77	1.94
Pro forma (RMB)	3.64	1.89

Financial Summary

(Expressed in millions of RMB)

RESULTS

	Year ended 31 December				
	2001	2000	1999	1998	1997
Income Statement Data:					
Revenue:					
Cellular Business	20,505	12,188	5,314	2,126	810
Paging Business	4,342	8,483	9,047	8,423	7,273
Long Distance, Data and Internet Business	3,309	1,096	79	—	—
Total service revenue	28,156	21,767	14,440	10,549	8,083
Sales of telecommunications products	1,237	1,925	3,010	3,480	5,291
Total revenue	29,393	23,692	17,450	14,029	13,374
Operating expenses:					
Leased lines	(853)	(1,158)	(1,099)	(1,302)	(1,084)
Interconnection charges	(2,073)	(1,380)	(693)	(260)	(112)
Depreciation and amortisation	(8,262)	(5,734)	(3,691)	(2,260)	(1,300)
Personnel	(2,487)	(1,770)	(1,713)	(1,278)	(1,085)
Selling and marketing	(3,613)	(2,492)	(1,557)	(1,043)	(693)
General, administrative and other expenses	(5,499)	(3,743)	(2,587)	(2,356)	(1,709)
Cost of telecommunications products sold	(1,342)	(2,193)	(3,294)	(4,178)	(5,775)
Total operating expenses	(24,129)	(18,470)	(14,634)	(12,677)	(11,758)
Operating income	5,264	5,222	2,816	1,352	1,616
Net financial income (charges)	180	395	(704)	(413)	(267)
Loss arising from terminations of CCF Arrangements	—	(1,194)	(224)	—	—
Other income (expenses), net	19	59	(129)	(64)	(29)
Income before taxation and minority interests	5,463	4,482	1,759	875	1,320
Taxation	(1,041)	(1,104)	(556)	(311)	(469)
Income before minority interests	4,422	3,378	1,203	564	851
Minority interests	35	(144)	(364)	(192)	(252)
Net income	4,457	3,234	839	372	599
Net income per share (RMB)	0.36	0.29	0.09	0.04	0.06
Net income per ADS (RMB)	3.55	2.89	0.86	0.38	0.62

Financial Summary

(Expressed in millions of RMB)

SELECTIVE BALANCE SHEET DATA

	As of 31 December				
	2001	**2000**	**1999**	**1998**	**1997**
Current assets	**49,958**	57,755	10,497	8,945	4,951
Cash and cash equivalents	**18,413**	44,717	6,002	4,337	1,497
Accounts receivable, net	**2,498**	1,545	895	639	312
Property, plant and equipment, net	**75,748**	52,864	33,227	19,853	12,088
Total assets	**127,905**	112,829	45,366	30,156	17,470
Current liabilities	**28,917**	27,468	21,844	11,563	4,885
Short-term debts	**7,933**	8,501	7,894	2,276	380
Accounts payable	**15,329**	619	1,675	1,041	539
Long-term debts	**36,337**	27,151	12,234	9,372	5,944
Total liabilities	**65,394**	54,721	34,297	21,232	11,090
Shareholders' equity	**61,681**	57,224	8,538	6,408	5,176

Glossary

"ATM"	Asynchronous Transfer Mode, a high-bandwidth packet switching and multiplexing technique. Each cell in a stream is presented to the network on a "start-stop" basis (asynchronously), rather than having a circuit or a regular time slot reserved for the stream. This protocol is deployed both within core networks and as an access technology.
"base station"	Transmitter and receiver which serve as a bridge between all cellular users in a cell and connect cellular calls to the cellular switching centre.
"CDMA"	Code Division Multiple Access technology, which is a digital transmission technology that accommodates higher throughput by using various coding sequences to mix and separate voice and data signals for wireless communication.
"Circuit Switch"	A point-to-point network connection maintained only while the sender and recipient are communicating.
"DWDM"	Dense Wave Division Multiplexing technology, a means of increasing transmission capacity by transmitting signals through multiple wavelengths through a single fibre.
"FR"	Frame Relay, a high speed open protocol offering both access to a network and carriage of data across a network. This protocol is used by customers that have significant amounts of data traffic.
"Gbps"	One billion bits per second.
"GPRS"	General Packet Radio Service, the packet data service for the GSM Standard.
"GSM"	Global cellular system for cellular communications, a digital cellular telephone system operating in the 900 MHz frequency band based on digital transmission and cellular network architecture with roaming.
"IP"	Internet Protocol, the open protocol used for the Internet and on many LANs and WANs.
"IP telephony"	A general term for the technologies that use the Internet's packet to exchange data, voice, fax and other forms of information.
"ISDN"	Integrated Service Digital Network, a protocol which offers high capacity dial-in access to public networks; this protocol allows simultaneous handling of digitalised voice and data traffic on the same digital links via integrated switches across the public network.
"Kbps"	One thousand bits per second.
"Mbps"	One million bits per second.

"MHz"	Megahertz, a unit of measure of frequency; 1 MHz is equal to one million cycles per second.
"MPLS"	Multiple Protocal Label Switching.
"roaming"	A service offered by cellular communications network operators which allows a subscriber to use his or her handset while in different service areas of the same, carrier or in the service area of another carrier. International roaming requires an agreement between operators of different individual markets to permit customers of either operator to access the other's system.
"QoS"	Quality of Service.
"SDH"	Synchronous Digital Hierarchy architecture, a self-healing system that allows for instantaneous rerouting of signals in the event of a fibre cut.
"PSTN"	Public Switched Telephone Network.
"VISP"	Virtual Internet Service Provider.
"VPN"	Virtual Private Network.
"W-CDMA"	Wideband CDMA, one of the principal standards for third generation cellular technology. It supports both packet- and circuit-switched communications and has been designed for high speed data services.
"WAP"	Wireless Application Protocol, WAP technology will enable Internet access through cellular handsets.