

REPORT OF THE DIRECTORS

The board of directors (the "Board") of China Communications Services Corporation Limited (the "Company") is pleased to present the Report of the Directors of the Company, together with the audited financial statements of the Company and its subsidiaries (the "Group") prepared in accordance with International Financial Reporting Standards for the year ended 31 December 2017.

PRINCIPAL BUSINESSES

The Group is a leading service provider in the PRC that provides integrated comprehensive solutions in the field of informatization. We offer telecommunications infrastructure services, including design, construction and project supervision and management; business process outsourcing services, including management of infrastructure for information technology ("network maintenance"), general facilities management ("facilities management"), supply chain and products distribution; and applications, content and other services, including system integration, software development and system support, and value-added services. The major customers of the Group include domestic telecommunications operator customers, domestic non-telecom operator customers such as government agencies, industrial customers and small and medium enterprises, and overseas customers.

RESULTS

Results of the Group for the year ended 31 December 2017 and the financial position of the Group as at that date are set out in the audited financial statements on page 99 to page 180 in this annual report.

BUSINESS REVIEW

A fair review of the business, business outlook and the key financial performance indicators of the Group are provided in the "Chairman's Statement", "President's Statement", "Business Overview" and "Management Discussion and Analysis of Financial Conditions and Results of Operations" of this annual report. Description of the principal risks and uncertainties faced by the Group is disclosed in this section. Particulars of important events affecting the Group that have occurred since the end of the financial year of 2017, if applicable, can also be found in the aforesaid sections.

In addition, more details regarding the Group's performance in relation to environmental and social-related policies, an account of the Group's relationships with its key stakeholders, as well as compliance with relevant laws and regulations which have a significant impact on the Group, are provided in the "Environmental, Social and Governance Report" of this annual report.

The above discussion forms part of this "Report of the Directors".

DIVIDENDS

The Board proposes a final dividend of RMB0.1176 per share and a special dividend of RMB0.0235 per share, and the total dividend is RMB0.1411 per share (pre-tax) for the year ended 31 December 2017. The dividend proposal will be submitted for consideration at the annual general meeting to be held on 29 June 2018 (the "AGM").

Dividends will be denominated and declared in Renminbi. Dividends will be paid in Renminbi for holders of domestic shares and holders of H shares (including enterprises and individuals) who invest in the H shares of the Company listed on the Hong Kong Stock Exchange through the Shanghai Stock Exchange or Shenzhen Stock Exchange ("the Southbound Trading") (the "Southbound Shareholders"), and dividends for H share shareholders other than the Southbound Shareholders will be paid in Hong Kong dollars. The relevant exchange rate will be the average of the mid-point rates of Renminbi to Hong Kong dollars as announced by the People's Bank of China for the week prior to the date of approval of declaration of dividends by the AGM. The record date for entitlement to the shareholders' rights and the relevant arrangements of dividend distribution for Southbound Shareholders are the same as those for the Company's H share shareholders. The proposed dividends are expected to be paid on or about Friday, 17 August 2018 upon approval at the AGM.

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Further details in respect of the dividends and distribution by the Company are set out in note 14 of the audited financial statements on page 135 of this annual report.

For the overseas resident individual shareholders of the Company, pursuant to relevant laws and regulations including the Law of the People's Republic of China on Individual Income Tax, the Regulations for the Implementation of the Law of the People's Republic of China on Individual Income Tax, and the letter dated 28 June 2011 from the State Administration of Taxation to the Inland Revenue Department of Hong Kong, for individual H share shareholders receiving dividends who are Hong Kong or Macau residents or whose country of domicile is a country which has entered into a tax treaty with the PRC stipulating a dividend tax rate of 10%, the Company, as a withholding agent, is required to withhold and pay individual income tax at the rate of 10%. For individual H share shareholders receiving dividends whose country of domicile is a country which has entered in to a tax treaty with the PRC stipulating a dividend tax rate lower than 10%, the Company will withhold the individual income tax at a tax rate of 10%. The Company can process applications on behalf of those shareholders to seek entitlement of the relevant agreed preferential treatments pursuant to relevant regulations, and upon approval by the tax authorities, the extra amount of tax withheld will be refunded. For individual H share shareholders receiving dividends whose country of domicile is a country which has entered into a tax treaty with the PRC stipulating a dividend tax rate higher than 10% but lower than 20%, the Company will withhold the individual income tax at the agreed-upon effective tax rate when distributing dividends and no application procedures will be necessary. For individual H share shareholders receiving dividends whose country of domicile is a country which has not entered into any tax treaty with the PRC or are under other situations, the Company will withhold the individual income tax at a tax rate of 20% when distributing dividends.

For the overseas non-resident enterprise shareholders of the Company (including HKSCC Nominees Limited, corporate nominees or trustees, or other organizations or entities that are considered non-resident enterprise shareholders), pursuant to the Law of the People's Republic of China on Enterprise Income Tax, the Regulations for the Implementation of the Law of the People's Republic of China on Enterprise Income Tax and relevant rules and regulations, as a withholding agent, the Company is required to withhold and pay the enterprise income tax at the tax rate of 10% on behalf of the overseas non-resident enterprise shareholders.

For the Southbound Shareholders of the Company, the Shanghai branch of China Securities Depository and Clearing Corporation Limited and the Shenzhen branch of China Securities Depository and Clearing Corporation Limited, as the nominees of the shareholders of the Southbound Trading, will receive all dividends distributed by the Company and will distribute the dividends to the relevant shareholders under the Southbound Trading through its depository and clearing system. According to the relevant provisions under the "Notice on Tax Policies for Shanghai-Hong Kong Stock Connect Pilot Programme (Cai Shui [2014] No. 81)" and "Notice on Tax Policies for Shenzhen-Hong Kong Stock Connect Pilot Programme (Cai Shui [2016] No. 127)", the Company shall withhold individual income tax at the rate of 20% with respect to dividends received by the Mainland individual investors for investing in the H shares of the Company listed on the Hong Kong Stock Exchange through the Southbound Trading. In respect of the dividends for the investment of Mainland securities investment funds in the H shares of the Company listed on Hong Kong Stock Exchange through the Southbound Trading, the tax levied on dividends derived from such investment shall be ascertained by reference to the rules applicable to the treatment of individual income tax. The Company is not required to withhold income tax on dividends derived by the Mainland enterprise investors under the Southbound Trading, and such enterprises shall report the income and make tax payment by themselves.

Should the shareholders of the H shares of the Company have any doubt in relation to the aforesaid arrangements, they are recommended to consult their tax advisors for relevant tax impact in mainland China, Hong Kong and other countries (regions) on the possession and disposal of the H shares of the Company.

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DIRECTORS AND SENIOR MANAGEMENT OF THE COMPANY

The following table sets out information concerning the directors and senior management of the Company as at the date of this report:

Name	Position in the Company	Date of the first appointment
Wang Xiaochu	Honorary Chairman ¹	8 April 2008
Zhang Zhiyong	Chairman Executive Director	16 March 2018 16 March 2018 ²
Si Furong	Executive Director President	21 February 2014 19 December 2013
Hou Rui	Executive Director Chief Financial Officer Executive Vice President	23 February 2011 30 December 2010 27 October 2010
Li Zhengmao	Non-executive Director	27 November 2012
Shao Guanglu	Non-executive Director	23 June 2017
Zhao Chunjun	Independent Non-executive Director	26 September 2006
Siu Wai Keung, Francis	Independent Non-executive Director	28 June 2012
Lv Tingjie	Independent Non-executive Director	26 June 2015
Wu Taishi	Independent Non-executive Director	26 June 2015
Liu Linfei	Independent Non-executive Director	24 June 2016
Cheng Hongyan	Executive Vice President	21 July 2014
Xu Chuguo	Executive Vice President	21 July 2014
Liang Shiping	Executive Vice President	3 March 2010
Yan Dong	Executive Vice President Chief Risk Officer	18 June 2013
Chung Wai Cheung, Terence	Company Secretary Deputy Chief Financial Officer	16 October 2006

On 10 March 2017, Mr. Zhang Junan resigned as a non-executive director of the Company. On 23 June 2017, Mr. Shao Guanglu was appointed as a non-executive director of the Company. On 16 March 2018, Mr. Sun Kangmin resigned as the Chairman and an executive director of the Company, on the same day, Mr. Zhang Zhiyong was appointed as an executive director and the Chairman of the Company.

¹ Honorary Chairman is not a member of the Board and does not have any power or right to vote on any matters considered by the Board.

² Mr. Zhang Zhiyong used to work at the Company from 2006 to 2010. During this period, he held various positions of the Company, including President of the Company, and an executive director from 12 December 2007 to 21 June 2010.

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SUPERVISORS OF THE COMPANY

The following table sets out information concerning the supervisors of the Company as at the date of this report:

Name	Position in the Company	Date of the first appointment
Han Fang	Chairperson of the Supervisory Committee	11 December 2015
Hai Liancheng	Independent Supervisor	3 August 2006
Si Jianfei	Employee Representative Supervisor	18 June 2013

Profiles of the directors, supervisors and senior management are set out in the “Profiles of Directors, Supervisors and Senior Management” section of this annual report.

The Company has received, from each of the independent non-executive directors, an annual confirmation of his independence pursuant to Rule 3.13 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the “Listing Rules”). The Company considers that all of the independent non-executive directors are independent.

SHARE CAPITAL

The Company was incorporated on 30 August 2006. In December 2006, by way of an initial public offering (the “IPO”), the Company issued 1,484,986,000 H shares with a nominal value of RMB1.00 each at a price of HK\$2.20 per share. At the same time, the promoters of the Company transferred 148,498,600 domestic state-owned shares with a nominal value of RMB1.00 each to the National Council for Social Security Fund of the PRC (the “NSSF”) and converted them into H shares on the basis of one domestic share to one H share. Immediately after the IPO, the registered capital of the Company amounted to RMB5,444,986,000, of which 1,633,484,600 H shares of the Company were listed and traded on The Stock Exchange of Hong Kong Limited (the “Stock Exchange”).

On 9 April 2008, the Company announced the completion of placing a total of 359,365,600 H shares, including an issue of 326,696,000 new H shares and a placement of 32,669,600 H shares on behalf of NSSF upon conversion of the same number of existing domestic shares of the Company allocated to NSSF by China Telecommunications Corporation (“China Telecom”). After the completion of placing, the total issued shares of the Company increased to 5,771,682,000 shares, of which 1,992,850,200 shares were H shares.

As disclosed in the prospectus of the Company dated 27 November 2006, China Telecom entered into equity transfer arrangements with China Mobile Communications Corporation (now known as China Mobile Communications Group Co., Ltd. (“China Mobile”)) and China United Telecommunications Corporation (now known as China United Network Communications Group Company Limited (“China Unicom”)), respectively. Pursuant to the arrangements, China Telecom agreed to transfer 506,880,000 and 236,300,000 domestic shares to China Mobile and China Unicom, respectively. On 24 March 2009, the equity transfers were formally completed and became effective. On the same date, Guangdong Telecom Industry Group Corporation and Zhejiang Telecom Industry Corporation completed the transfers of 236,313,086 and 87,664,532 domestic shares, respectively, to China Telecom.

According to the equity transfer agreement between China Telecom and China National Postal and Telecommunications Appliances Corporation (now known as China National Postal and Telecommunications Appliances Co., Ltd.) on 28 May 2010, China Telecom agreed to transfer 108,899,720 domestic shares of the Company to China National Postal and Telecommunications Appliances Corporation. On 21 June 2011, the equity transfer was formally completed.

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Pursuant to the resolutions passed at the extraordinary general meeting, H shareholders class meeting and the domestic shareholders class meeting of the Company held on 28 June 2011 and as approved by domestic and overseas regulatory authorities, the Company announced the launch of H share and domestic share rights issue plan of an aggregate of 1,154,336,400 new shares, including 398,570,040 H rights shares and 755,766,360 domestic rights shares on the basis of 2 rights shares for every 10 existing shares on 30 December 2011 at the price of HK\$3.19 per H rights share and RMB2.59 per domestic rights share, respectively. On 10 February 2012, dealings in the H rights shares commenced on the Stock Exchange. After completion of the rights issue, the total number of issued shares of the Company was increased to 6,926,018,400 shares, including 2,391,420,240 H shares and 4,534,598,160 domestic shares.

As at 31 December 2017, the share capital of the Company was RMB6,926,018,400 divided into 6,926,018,400 shares with a nominal value of RMB1.00 each. The share capital of the Company was comprised of the following:

Shares	Number of shares	Approximate percentage of issued share capital (%)
Domestic shares (Total)	4,534,598,160	65.47
Domestic shares held by:		
China Telecommunications Corporation	3,559,362,496	51.39
China Mobile Communications Group Co., Ltd.	608,256,000	8.78
China United Network Communications Group Company Limited	236,300,000	3.41
China National Postal and Telecommunications Appliances Co., Ltd.	130,679,664	1.89
H shares (Total)	2,391,420,240	34.53
Total	6,926,018,400	100.00

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MATERIAL INTERESTS AND SHORT POSITIONS IN SHARES AND UNDERLYING SHARES OF THE COMPANY

As at 31 December 2017, the interests or short positions of persons who at any of the Company's general meetings (excluding the directors and supervisors of the Company) are entitled to exercise or control the exercise of 5% or more of the voting power in the shares and underlying shares of equity derivatives of the Company in each class as recorded in the register required to be maintained under Section 336 of the Securities and Futures Ordinance (Cap 571 of the Laws of Hong Kong) (the "SFO") were as follows:

Name of shareholder	Class of shares	Capacity	Number of shares held	Percentage of the respective class of share (%)	Percentage of the total number of shares in issue (%)
China Telecommunications Corporation	Domestic shares	Beneficial owner	3,559,362,496 (L)	78.49	51.39
China Mobile Communications Group Co., Ltd.	Domestic shares	Beneficial owner	608,256,000 (L)	13.41	8.78
China United Network Communications Group Company Limited	Domestic shares	Beneficial owner	236,300,000 (L)	5.21	3.41
BlackRock, Inc.	H shares	Interests of controlled corporations	216,646,179 (L)	9.06	3.13
		Interests of controlled corporations	172,000 (S)	0.01	0.00
JPMorgan Chase & Co.	H shares	18,150,671 shares as Beneficial owner; 96,000 shares as Investment manager and 175,917,766 shares as Approved lending agent	194,164,437 (L)	8.11	2.80
		Beneficial owner	7,828,748 (S)	0.32	0.11
		Approved lending agent	175,917,766 (P)	7.35	2.54
Citigroup Inc.	H shares	20,481,062 shares as Interests of controlled corporations; 14,146,000 shares as person having a security interest in shares and 156,615,710 shares as approved lending agent	191,242,772 (L)	7.99	2.76
		Interests of controlled corporations	184,000 (S)	0.00	0.00
		Approved lending agent	156,615,710 (P)	6.54	2.26

Note: (L) – Long Position
(S) – Short Position
(P) – Lending Pool

Save as stated above, as at 31 December 2017, in the register required to be maintained under Section 336 of the SFO, no other persons were recorded as holding any interests or short positions in the shares or underlying shares of the equity derivatives of the Company.

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DIRECTORS' AND SUPERVISORS' INTERESTS AND SHORT POSITIONS IN SHARES, UNDERLYING SHARES AND DEBENTURES

As at 31 December 2017, none of the directors and supervisors of the Company had any interests or short positions in the shares, underlying shares of equity derivatives or debentures of the Company or its associated corporations (within the meaning of Part XV of the SFO) as recorded in the register required to be maintained under Section 352 of the SFO or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers. As at 31 December 2017, the Company had not granted its directors or supervisors, or their respective spouses or children below the age of 18 any rights to subscribe for the shares or debentures of the Company or any of its associated corporations and none of them has ever exercised any such right to subscribe for shares or debentures.

SHARE APPRECIATION RIGHTS

Please refer to note 39 to the audited financial statements for details of the share appreciation rights scheme of the Company and the share appreciation rights granted during the year ended 31 December 2017.

PUBLIC FLOAT

As at the date of this annual report, based on information that is publicly available to the Company and within the knowledge of the directors, the Company has maintained the prescribed public float under the Listing Rules.

DIRECTORS' AND SUPERVISORS' SERVICE CONTRACTS

Each of the directors and supervisors has entered into a service contract with the Company. According to the service contract, each of the contracts has an initial term of three years and is renewable in accordance with the Articles of Association of the Company when the initial term expires except for Ms. Han Fang, Mr. Liu Linfei, Mr. Shao Guanglu and Mr. Zhang Zhiyong. These contracts are terminable at the option of either party by giving three months' notice in writing or according to the terms of the contract prior to the expiry of the contract. No such service contract is not determinable by the Company within one year without payment of compensation (other than statutory compensation). The term of service of Ms. Han Fang commenced from 11 December 2015 (the date of the extraordinary general meeting approving her appointment) to the 2017 AGM to be held in 2018. The term of service of Mr. Liu Linfei commenced from 24 June 2016 (the date of the annual general meeting approving his appointment) to the 2017 AGM to be held in 2018. The term of service of Mr. Shao Guanglu commenced from 23 June 2017 (the date of the annual general meeting approving his appointment) to the 2017 AGM to be held in 2018. The term of service of Mr. Zhang Zhiyong commenced from 16 March 2018 (the date of the extraordinary general meeting approving his appointment) to the 2017 AGM to be held in 2018.

PERMITTED INDEMNITY PROVISION

The Company has maintained appropriate directors and officers liability insurance coverage for the directors, supervisors and senior management of the Company during the course of the financial year ended 31 December 2017 and such insurance remained in force as of the date of this report.

DIRECTORS' AND SUPERVISORS' INTERESTS IN TRANSACTIONS, ARRANGEMENTS OR CONTRACTS

Save for the transactions, arrangements or contracts set out in the "Management Discussion and Analysis of Financial Conditions and Results of Operations" section and "Directors' and Supervisors' Service Contracts", "Major Customers and Suppliers", "Preferential Treatment and Non-competition Arrangement with China Tower Corporation Limited" and "Continuing Connected Transactions" in the "Report of the Directors" section of this annual report and note 43 to the Consolidated Financial Statements, no other transaction, arrangement or contract that is significant in relation to the Group's business to which the Company or any of its subsidiaries was a party and in which a person who was a Director or Supervisor of the Company or his or her connected entity had, directly or indirectly, a material interest subsisted at any time during the year ended 31 December 2017.

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EMOLUMENTS OF THE DIRECTORS AND SUPERVISORS

Based on the overall remuneration policy of the Company and with reference to the payroll standard of the same industry companies in the market, the remuneration of directors and supervisors is determined after taking into account the scope and complexities of their duties. Please refer to note 12 to the audited financial statements for details of the emoluments of the directors and supervisors of the Company in 2017.

PURCHASE, SALE AND REDEMPTION OF SHARES

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

SUMMARY OF FINANCIAL INFORMATION

Please refer to pages 181 to 182 of this annual report for a summary of the operating results, assets and liabilities of the Group for each of the years in the five-year period ended 31 December 2017.

BANK LOANS AND OTHER BORROWINGS

Please refer to note 33 to the audited financial statements for details of bank loans and other borrowings of the Group.

PROPERTY, PLANT AND EQUIPMENT

Please refer to note 16 to the audited financial statements for movements in the fixed assets of the Group for the year ended 31 December 2017.

DISTRIBUTABLE RESERVES

Please refer to note 46 to the audited financial statements for details of the movements in the reserves of the Group for the year ended 31 December 2017.

DONATIONS

For the year ended 31 December 2017, the Group made charitable and other donations of a total amount of RMB0.22 million.

SUBSIDIARIES AND ASSOCIATED COMPANIES

Please refer to note 45 and note 22 to the audited financial statements for details of the Company's subsidiaries and the Company's associated companies as at 31 December 2017.

CHANGES IN EQUITY

Please refer to the consolidated statement of changes in equity contained in the audited financial statements (pages 103 to 104 of this annual report).

PLAN OF EMPLOYEES' RETIREMENT BENEFITS

Please refer to note 38 to the audited financial statements for details of the retirement benefits provided by the Group.

PRE-EMPTIVE RIGHTS

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

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MAJOR CUSTOMERS AND SUPPLIERS

For the reporting period, the revenue from sales of goods or rendering of services to the five largest customers (including China Telecom, China Mobile, China Unicom and China Tower) of the Group represented 69.5% of the total revenues of the Group; of which, the revenue from the largest customer of the Group represented 43.9% of the total revenues of the Group. The purchases from the five largest suppliers of the Group accounted for less than 3.1% of the total annual purchases of the Group.

To the knowledge of the Board, other than China Telecom and China Mobile (both of them being the shareholders holding more than 5% of the issued share capital of the Company), Mr. Zhang Zhiyong, Mr. Si Furong, Mr. Li Zhengmao and Mr. Shao Guanglu (positions of them setting out in the “Profiles of Directors, Supervisors and Senior Management” section of this annual report), none of the directors of the Company, their close associates, or any shareholder (holding more than 5% of the issued share capital of the Company) has any interests in such suppliers or customers.

PREFERENTIAL TREATMENT AND NON-COMPETITION ARRANGEMENT WITH CHINA TOWER CORPORATION LIMITED (“CHINA TOWER”)

In July 2014, China Telecom Corporation Limited, a subsidiary of China Telecom, jointly established China Tower with China Mobile and China Unicom. Pursuant to the relevant arrangements for the establishment of China Tower, China Tower has indicated to the Company that:

1. on condition that it will not result in a breach by China Telecom and the Company of the Non-Competition Agreement signed between them, when China Tower invites public tender for the design, construction, supervision and maintenance of its telecommunications towers and related ancillary facilities, China Tower will select the Company on a preferential basis, provided that the terms are the same;
2. in the event of an injection of telecommunications assets into China Tower (acquisition by China Tower), the existing maintenance agreements entered into between the Company and the respective promoters of China Tower will remain valid. Upon the expiration of such maintenance agreements and when China Tower invites tender for the maintenance services, China Tower will consider the Company on a preferential basis, provided that the terms are the same; and
3. China Tower will not compete in contravention of the contents of the Non-Competition Agreement.

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CONTINUING CONNECTED TRANSACTIONS

China Telecom is the controlling shareholder of the Company. Pursuant to Chapter 14A of the Listing Rules, the transactions between the Group and China Telecom and its subsidiaries (excluding the Group and including China Telecom Corporation Limited, collectively the "China Telecom Group") constitute connected transactions of the Group.

The Company revised the annual caps of engineering related services provided to China Telecom Group and operation support services provided by China Telecom Group in 2015, which were approved by the independent shareholders of the Company at the extraordinary general meeting held on 11 December 2015. The following table sets out the annual caps and actual amounts of the continuing connected transactions of the Group during the year ended 31 December 2017:

Unit: RMB million

	Year ended 31 December 2017		Year ending
	Annual Caps	Actual Amounts	31 December 2018 Annual Caps
Engineering related services provided to China Telecom Group	24,000	21,155	24,000
Ancillary telecommunications services provided to China Telecom Group	13,300	11,041	15,600
Operations support service provided to/by China Telecom Group			
Revenue	3,400	2,791	3,600
Expenditure	1,000	950	1,100
IT application services provided to/by China Telecom Group			
Revenue	2,700	2,382	2,900
Expenditure	490	268	490
Centralized services provided to China Telecom Group	440	329	450
Property leasing provided to/by China Telecom Group			
Revenue	210	105	220
Expenditure	220	200	240
Supplies procurement services provided to/by China Telecom Group			
Revenue	8,100	4,094	10,000
Expenditure	5,900	2,122	7,000

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CONTINUING CONNECTED TRANSACTIONS AGREEMENTS BETWEEN THE COMPANY AND CHINA TELECOM

The Company and China Telecom entered into seven continuing connected transactions agreements on 29 September 2015 to govern the continuing connected transactions between the Group and China Telecom Group. These agreements include the Engineering Framework Agreement, the Ancillary Telecommunications Services Framework Agreement, the Operation Support Services Framework Agreement, the IT Application Services Framework Agreement, the Centralized Services Agreement, the Property Leasing Framework Agreement and the Supplies Procurement Services Framework Agreement (the "2015 Agreements"). Each of the 2015 Agreements had an initial term expired on 31 December 2018 and, subject to approval from the shareholders (if applicable), the 2015 Agreements would be automatically renewed for a further period of not more than three years each time, unless terminated by either party by giving a written notice three months in advance. All of the 2015 Agreements (excluding the Centralized Services Agreement and the Property Leasing Framework Agreement that did not require independent shareholders' approval under the Listing Rules) were approved by the independent shareholders of the Company at the extraordinary general meeting held on 11 December 2015.

The Board considers that it is in the interest of the Company to enter into the 2015 Agreements and cooperate with China Telecom Group to ensure a stable revenue source from one of the largest telecommunications operators in the PRC so as to benefit the Company's future growth and development.

Details of each of the 2015 Agreements are set out below.

ENGINEERING FRAMEWORK AGREEMENT

Pursuant to the Engineering Framework Agreement, the Company agreed to provide certain engineering related services, such as design, construction, project supervision and management for telecommunications infrastructure projects undertaken by China Telecom Group.

The charges for engineering related services rendered under the Engineering Framework Agreement shall be determined at prices fixed through tender process or market price. According to the relevant regulations and under the internal policy of China Telecom Group, whenever the value of any design and/or project supervision and management contracts exceeds RMB0.5 million, or the value of any construction contracts exceeds RMB2 million, the award of the relevant contract must be subject to a tender process (with a minimum of three parties tendering bids) in accordance with the Bidding Law of the PRC and Regulation on the Implementation of the Bidding Law of the PRC, except as otherwise provided by related laws and regulations. In determining the market price, the business and financial department of the relevant subsidiary of the Company shall collect the relevant market information (including but not limited to the change in price for the same or similar type of services), review and compare the costs and profits of transactions conducted in the most recent year of the same or similar type entered into with China Telecom Group or independent third parties, and prepare fee quotes for review by the marketing department of the relevant subsidiary of the Company, or the marketing department of the relevant subsidiary will further submit the fee quotes to the management of such subsidiary for review depending on the actual situations (such as the amount and size of the transaction). The marketing department or management of the relevant subsidiary of the Company shall primarily consider the following factors: (1) cost of service; (2) prices of the same or similar type of services provided to China Telecom Group by other service providers in the market; (3) prices of the same or similar type of services provided to China Telecom Group and independent third parties previously by the Company.

The Company will be given priority by China Telecom Group in the provision of the engineering related services except in the tender process, provided that the terms and conditions offered by independent third parties to China Telecom Group are no more favorable than those offered by the Company for the same type of services, and in return, the Company has undertaken to China Telecom Group that the Company shall not provide services to it on terms which are less favorable than those offered by the Company to independent third parties.

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ANCILLARY TELECOMMUNICATIONS SERVICES FRAMEWORK AGREEMENT

Pursuant to the Ancillary Telecommunications Services Framework Agreement, the Company agreed to provide to China Telecom Group certain ancillary telecommunications services such as maintenance of network facilities including equipment, ducts and cables, equipment rooms and base stations; distribution of telecommunications products and services; provision of comprehensive logistics services, including purchasing agent, warehousing, transportation, delivery, testing and inspection, logistics information management and distribution; provision of application, content and other services such as fixed-line value added services, wireless value added services, Internet value added services, and development of online gaming, certificate authentication and value added business platform of Internet cafes (the "Ancillary Telecommunications Services").

The Ancillary Telecommunications Services Framework Agreement stipulates that the Ancillary Telecommunications Services shall be provided at:

- (1) market price. In determining the market price, the business and financial department of the relevant subsidiary of the Company shall collect the relevant market information (including but not limited to the change in price for the same or similar type of services), review and compare the costs and profits of transactions conducted in the most recent year of the same or similar type entered into with China Telecom Group or independent third parties, and prepare fee quotes for review by the marketing department of the relevant subsidiary of the Company, or the marketing department of the relevant subsidiary will further submit the fee quotes to the management of such subsidiary for review depending on the actual situations (such as the amount and size of the transaction). The marketing department or management of the relevant subsidiary of the Company shall primarily consider the following factors: (i) cost of service; (ii) prices of the same or similar type of services provided to China Telecom Group by other service providers in the market; (iii) prices of the same or similar type of services provided to China Telecom Group and independent third parties previously by the Company; or
- (2) in the absence of market price or where the market price cannot be determined, the price shall be agreed between both parties, which shall be the aggregate amount of reasonable costs, the relevant taxes in sales and reasonable profits. In determining such price, the business and financial department of the relevant subsidiary of the Company will review and compare the costs and profits of transactions conducted in the most recent year of the same or similar type entered into with China Telecom Group or independent third parties, take into account factors such as historical price, transaction size, average profit ratio within the relevant industry, supply and demand, labor cost, local commodity prices and economic development levels, and prepare fee proposals for review by the marketing department of the relevant subsidiary of the Company, or the marketing department of the relevant subsidiary will further submit the fee quotes to the management of such subsidiary for review depending on the actual situations (such as the amount and size of the transaction).

The Company will be given priority by China Telecom Group in the provision of the Ancillary Telecommunications Services, provided that the terms and conditions offered by independent third parties to China Telecom Group are no more favorable than those offered by the Company for the same services, and in return, the Company has undertaken to China Telecom Group that the Company and its subsidiaries shall not provide Ancillary Telecommunications Services to it on terms which are less favorable than those offered by the Company to independent third parties.

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OPERATION SUPPORT SERVICES FRAMEWORK AGREEMENT

Pursuant to the Operation Support Services Framework Agreement, the Company agreed to provide to China Telecom Group operation support services, including but not limited to facilities management and renovation, network facilities management in relation to buildings used for telecommunications purposes, human resources management, equipment maintenance, advertisement, conferencing services, vehicles, and certain repair and leasing of equipment. China Telecom Group also agreed to provide operation support services such as logistics services, warehousing, medical care, food and beverages, education, hotel and travelling services, labor services and so on to the Company.

The Operation Support Services Framework Agreement shall adopt the same pricing policy as the Ancillary Telecommunications Services Framework Agreement. In addition, in determining the market price of the operation support services provided to the Company by the China Telecom Group, the Company primarily considered the following factors: (i) prices of the same or similar type of services provided to the Company by other service providers in the market; (ii) prices of the same or similar type of services provided to the Company by China Telecom Group and independent third parties previously.

Each of the parties to the Operation Support Services Framework Agreement will accord priority to the other party in the provision of the operation support services, provided that the terms and conditions offered by independent third parties to the relevant party are no more favorable than those offered by the other party for the same services, and in return, each of the parties has undertaken to the other that it shall not provide services to the other on terms which are less favorable than those offered to independent third parties.

IT APPLICATION SERVICES FRAMEWORK AGREEMENT

Pursuant to the IT Application Services Framework Agreement, the Company agreed to provide China Telecom Group with telecommunications network support services, software and hardware development and other related IT services. China Telecom Group also agreed to provide to the Company certain IT application services including voice and data, value added services and information application services.

The IT Application Services Framework Agreement shall adopt the same pricing policy as the Engineering Framework Agreement. In addition, in determining the market price of the IT application services provided to the Company by the China Telecom Group, the Company primarily considers the following factors: (i) prices of the same or similar type of services provided to the Company by other service providers in the market; (ii) prices of the same or similar type of services provided to the Company by China Telecom Group and independent third parties previously.

Each of the parties to the IT Application Services Framework Agreement will accord priority to the other party in the provision of the IT application services, provided that the terms and conditions offered by independent third parties to the relevant party are no more favorable than those offered by the other party for the same services, and in return, each of the parties has undertaken to the other that it shall not provide services to the other on terms which are less favorable than those offered to independent third parties.

REPORT OF THE DIRECTORS

CENTRALIZED SERVICES AGREEMENT

Pursuant to the Centralized Services Agreement, the centralized services to be provided by the Company to China Telecom Group include:

- (1) the corporate headquarters management function to manage assets of China Telecom's certain retained specialized telecommunications support businesses in the PRC other than the Group and any remaining assets, such as hotels, manufacturing plants, schools and hospitals which are not in association with the specialized telecommunications support businesses in the primary service areas of the Group; and
- (2) the provincial headquarters management function to manage remaining assets of China Telecom in the primary service areas of the Group.

Except as otherwise agreed by the parties, the aggregate administrative expenses incurred by the Company for the provision of the centralized services referred to above (all expenses incurred in connection with the above-mentioned headquarters management functions excluding remuneration for the Directors, share appreciation rights and provision of bad debts) will be apportioned pro rata between the Company and China Telecom Group according to the proportional net asset value of each of the relevant parties.

PROPERTY LEASING FRAMEWORK AGREEMENT

China Telecom Group have been leasing from the Company and its subsidiaries certain properties for use as business premises, offices, equipment storage facilities and sites for network equipment. The Company and its subsidiaries also have been leasing from China Telecom Group certain properties for use as business premises, offices and equipment storage facilities. These arrangements fall within the Property Leasing Framework Agreement.

Pursuant to the Property Leasing Framework Agreement, the rental charges in respect of each property are determined at market price. In determining the market price, the business and financial department of the relevant subsidiary of the Company shall collect the relevant market information (including but not limited to the change in price for the same or similar type of services), review and compare the costs and profits of transactions conducted in the most recent year of the same or similar type entered into with China Telecom Group or independent third parties, and prepare fee quotes for review by the marketing department of the relevant subsidiary of the Company, or the marketing department of the relevant subsidiary will further submit the fee quotes to the management of such subsidiary for review depending on the actual situations (such as the amount and size of the transaction). The marketing department or management of the relevant subsidiary of the Company shall primarily consider the following factors: (1) cost of property depreciation; (2) rental charges of the same or similar type of property provided to China Telecom Group and the Company by other service providers in the market; (3) rental charges of the same or similar type of property provided to China Telecom Group and independent third parties by the Company previously, or rental charges of the same or similar type of property provided to the Company by China Telecom Group and independent third parties previously. Rental charges are payable monthly in arrears, except as otherwise agreed by the parties, and subject to review every three years by both parties confirming after negotiations whether to adjust the rental charges and the amount of such adjustment.

REPORT OF THE DIRECTORS

SUPPLIES PROCUREMENT SERVICES FRAMEWORK AGREEMENT

Pursuant to the Supplies Procurement Services Framework Agreement, the Company agreed to provide to China Telecom Group with comprehensive supplies procurement services, including, among others, (i) procurement of imported telecommunications supplies, domestic telecommunications supplies and domestic non-telecommunications supplies; (ii) agency services of supplies procurement; (iii) sales of telecommunications supplies manufactured by the Group; (iv) resale of supplies purchased from independent third parties; and (v) management of biddings, verification of technical specifications, warehousing, transportation and installation services. According to the same agreement, China Telecom agreed to provide to the Group with comprehensive supplies procurement services, including, among others, (i) sales of telecommunications supplies manufactured by China Telecom Group, (ii) resale of supplies purchased from independent third parties; (iii) agency services of supplies procurement; and (iv) warehousing, transportation and installation services.

The price for the provision of comprehensive supplies procurement services under the Supplies Procurement Services Framework Agreement is determined as follows:

- (1) 1% of the contract value at the maximum for procurement services relating to imported telecommunications supplies;
- (2) 3% of the contract value at the maximum for procurement services relating to domestic telecommunications supplies and other domestic non-telecommunications materials; and
- (3) for other services:
 - (i) market price. In determining the market price, the business and financial department of the relevant subsidiary of the Company shall collect the relevant market information (including but not limited to the change in price for the same or similar type of services), review and compare the costs and profits of transactions conducted in the most recent year of the same or similar type entered into with China Telecom Group or independent third parties, and prepare fee quotes for review by the marketing department of the relevant subsidiary of the Company, or the marketing department of the relevant subsidiary will further submit the fee quotes to the management of such subsidiary for review depending on the actual situations (such as the amount and size of the transaction). The marketing department or management of the relevant subsidiary of the Company shall primarily consider the following factors: (i) cost of service; (ii) prices of the same or similar type of services provided to China Telecom Group or the Company by other service providers in the market; (iii) prices of the same or similar type of services provided to China Telecom Group and independent third parties by the Company, or prices of the same or similar type of services provided to the Company by China Telecom Group and independent third parties; or
 - (ii) in the absence of market price or where the market price cannot be determined, the price shall be agreed between both parties, which shall be the aggregate amount of reasonable costs, the taxes in sales and reasonable profits. In determining such price, the business and financial department of the relevant subsidiary of the Company will review and compare the costs and profits of transactions conducted in the most recent year of the same or similar type entered into with China Telecom Group or independent third parties, take into account factors such as historical price, transaction size, average profit ratio within the relevant industry, supply and demand, labour cost, local commodity prices and economic development levels, and prepare fee proposals for review by the marketing department of the relevant subsidiary of the Company, or the marketing department of the relevant subsidiary will further submit the fee quotes to the management of such subsidiary for review depending on the actual situations (such as the amount and size of the transaction).

REPORT OF THE DIRECTORS

The Group will be given priority by China Telecom Group in the provision of comprehensive logistics services, provided that the terms and conditions offered by independent third parties to China Telecom Group are no more favorable than those offered by the Company for the same services, and in return, the Company has undertaken to China Telecom that the Company and its subsidiaries shall not provide supplies procurement related comprehensive logistic services to it on terms which are less favorable than those offered by the Company and its subsidiaries to independent third parties.

The independent non-executive directors of the Company have confirmed that all the continuing connected transactions for the year ended 31 December 2017 to which the Group was a party:

1. had been entered into by the Group in the ordinary and usual course of business;
2. had been entered into on normal commercial terms or better; and
3. had been entered into according to the agreements governing them on terms that are fair and reasonable and in the interests of the shareholders of the Company as a whole.

The independent non-executive directors have further confirmed that:

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

The auditors of the Company have performed procedures in accordance with Hong Kong Standard on Assurance Engagements 3000 (Revised) "Assurance Engagements Other Than Audits or Reviews of Historical Financial Information" and with reference to Practice Note 740 "Auditor's Letter on Continuing Connected Transactions under the Hong Kong Listing Rules" issued by the Hong Kong Institute of Certified Public Accountants on the continuing connected transactions and issued a letter to the Board to advise that:

1. nothing has come to their attention that causes them to believe that the continuing connected transactions disclosed above have not been approved by the Board;
2. for transactions involving the provision of goods or services by the Group, nothing has come to their attention that causes them to believe that the transactions were not, in all material respects, in accordance with the pricing policies of the Company;
3. nothing has come to their attention that causes them to believe that the transactions were not entered into, in all material respects, in accordance with the relevant agreements governing such transactions;
4. with respect to the actual amounts of the continuing connected transactions, nothing has come to their attention that causes them to believe that those actual amounts have exceeded the annual caps disclosed in the previous announcement dated 29 September 2015 of the Company which were approved by the independent shareholders of the Company on 11 December 2015.

COMPLIANCE WITH CORPORATE GOVERNANCE CODE

Please see the "Corporate Governance Report" set out in this annual report for details of our compliance with the Corporate Governance Code.

MATERIAL LEGAL PROCEEDINGS

As at 31 December 2017, so far as the directors are aware, the Company was not involved in any material litigation or arbitration and no material litigation or claims had been made against, or were pending or threatened against the Company.

REPORT OF THE DIRECTORS

RISK FACTORS

The following section lists out the principal risks and uncertainties faced by the Group. It is a non-exhaustive list and there may be other risks and uncertainties further to the key risk areas outlined below.

1. The business of the Group may be affected by the economic, political and social conditions as well as government policies in China

As substantially all businesses, assets and operations of the Group are located in China, the Group's operating results, financial status and business prospect depend on the economic, political and social developments of China to a large extent.

In recent years, China is one of the countries with the fastest pace of economic growth around the globe in terms of GDP. However, the current growth rate may not be sustainable. Moreover, any future disaster, such as natural disaster and outbreak of epidemics would potentially slow down the level of economic activities, and in turn affect the economic growth of China, Asia and even the world. If any of the above mentioned reasons causes serious economic downturn in China, the Group's financial status, operating results and prospect may be adversely affected.

2. The business of the Group hinges on the investment and operating conditions in the Chinese telecommunications sector

Demands in the Group's services will be affected by the level of capital expenditures of the fixed-line, broadband and mobile telecommunications infrastructure of the telecommunications operators in China. Such decreases in capital expenditures may have adverse effect to the Group's revenue and profits.

Moreover, in the event that the competition in the Chinese telecommunications sector continues to intensify, the telecommunications operator customers of the Group may be under the pressure to reduce prices of their products or services, thus leading to the decrease in their revenue. If that happens, such telecommunications customers may reduce the service fees to our Company in relation to certain businesses for cost cutting, with a view to maintaining their profitability.

3. The business of the Group is working capital intensive in respect of services offered to customers

During our course of business, the Group shall incur considerable working capital expenditures to make procurements for goods and services required for the provision of services to the clients of the Group and for the completion of projects. In the past, the Company has satisfied the working capital needs primarily by cash from operating activities and its own fund. A deficiency in working capital may affect the Group's business, financial status and operating results. Moreover, the Group's customers may delay payment or default in accounts receivables, which may have adverse effect on the cash flows, working capital, financial status and operating results of the Company.

4. The Group is under certain risks in relation to international business and operation

The Group is dedicated in expanding into overseas market and strategically expanding overseas operations. The expansion into markets outside China will subject us to considerable risks, including differences in business environment, high entry barrier imposed on foreign enterprises, existing market players, exchange rate fluctuations, legal and regulatory requirements, potentially unfavorable tax liabilities, inexperience in new markets, competition in the local markets and protectionism.

Part of our business is conducted overseas and mainly located in developing countries and regions, where the local political and economic conditions are often unstable and such factors are beyond our control. As we have engaged in overseas business, we are subject to various risks related to the countries and regions where we operate.

REPORT OF THE DIRECTORS

AUDITORS

Deloitte Touche Tohmatsu and Deloitte Touche Tohmatsu Certified Public Accountants LLP were engaged as the international and domestic auditors of the Company respectively for the year ended 31 December 2017. Deloitte Touche Tohmatsu and Deloitte Touche Tohmatsu Certified Public Accountants LLP have audited the accompanying financial statements, which were prepared in accordance with International Financial Reporting Standards. A resolution for the reappointment of Deloitte Touche Tohmatsu and Deloitte Touche Tohmatsu Certified Public Accountants LLP as the international and domestic auditors of the Company for the year ending 31 December 2018 will be proposed at the upcoming AGM.



By order of the Board
Zhang Zhiyong
Chairman

Beijing, PRC
27 March 2018