

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 2007.

Principal Businesses

The Group is a leading integrated service provider in the PRC which provides specialized telecommunications support services to telecommunications operators. We offer telecommunications infrastructure services, including design, construction and project supervision and management; business process outsourcing services, including network maintenance, facilities management, and distribution of telecommunications services and products; applications, content and other services, including IT applications, Internet services, and value-added voice services, as well as other services. We also provide services to telecommunications equipment manufacturers and large enterprises in the PRC. The principal business of the Company is investment holding.

Results

Results of the Group for the year ended 31 December 2007 and the financial position of the Company and the Group as at that date are set out in the audited financial statements on page 91 to page 98 in this Annual Report.

Dividends

The Board proposed a cash dividend of RMB0.0682 per share for the year ended 31 December 2007, which will be subject to approval at the forthcoming 2007 annual general meeting.

In connection with the disclosure in the Prospectus of the Company dated 27 November 2006, for the period from 1 April 2006 to 7 December 2006, the day immediately prior to the listing of the H shares of the Company on The Stock Exchange of Hong Kong Limited (the “Stock Exchange”), the Group has declared and paid to its then shareholders (being China Telecommunications Corporation (“China Telecom”) and its relevant subsidiaries) a special dividend amounting to RMB535 million in total.

In connection with the disclosure in the circular of the Company dated 20 June 2007 relating to the acquisition of the specialized telecommunications support business (the “Target Business”) from China Telecom in 13 provinces, the changes in net assets between the period from 1 February 2007 to 31 August 2007 of the acquired business, amounting to RMB197 million in total, will be distributed in cash to China Telecom and its relevant subsidiaries.

Further details of dividends and distribution of the Company are set out in note 15 of the audited financial statements on page 133 of this Annual Report.

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 appointment
Wang Xiaochu	Chairman and Non-executive Director	3 August 2006
Li Ping	Vice Chairman, Executive Director, Chief Executive Officer	3 August 2006
Zhang Zhiyong	Executive Director	12 December 2007
	Executive Vice President and Chief Operating Officer	16 October 2006
Yuan Jianxing	Executive Director	12 December 2007
	Executive Vice President and Chief Financial Officer	16 October 2006
Liu Aili	Non-executive Director	12 October 2006
Zhang Junan	Non-executive Director	12 October 2006
Wang Jun	Independent Non-executive Director	26 September 2006
Chan Mo Po, Paul	Independent Non-executive Director	26 September 2006
Zhao Chunjun	Independent Non-executive Director	26 September 2006
Wu Shangzhi	Independent Non-executive Director	26 September 2006
Hao Weimin	Independent Non-executive Director	27 October 2006
Wang Qi	Executive Vice President	16 October 2006
Li Jian	Executive Vice President	16 October 2006
Liu Xiaoyi	Executive Vice President	16 October 2006
Chung Wai Cheung, Terence	Company Secretary, Assistant Chief Financial Officer and Qualified Accountant	16 October 2006

In July 2007, Mr. Li Zhigang resigned from the position of the Company's Executive Vice President.

On 8 April 2008, the Board approved the resignation of Mr. Wang Xiaochu as Non-executive Director and Chairman of the Company and the appointment of Mr. Wang Xiaochu as Honorary Chairman of the Company, the resignation of Mr. Li Ping as Vice Chairman and Chief Executive Officer of the Company and the appointment of Mr. Li Ping as Chairman of the Company, the resignation of Mr. Zhang Zhiyong as Executive Vice President of the Company and the appointment of Mr. Zhang Zhiyong as President of the Company.

Report of the Directors

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

Name	Position in the Group	Date of appointment
Wang Qi	Executive Vice President of the Company and Chief Executive Officer of Guangdong Communications Services Company Limited	17 August 2006
Yuan Jinling	Chief Executive Officer of Shanghai Communications Services Company Limited	17 August 2006
Shi Yongsheng	Chief Executive Officer of Zhejiang Communications Services Company Limited	17 August 2006
Yang Yonghe	Chief Executive Officer of Fujian Communications Services Company Limited	13 March 2007
Gao Liangping	Chief Executive Officer of Hubei Communications Services Company Limited	17 August 2006
Bao Tiejun	Chief Executive Officer of Hainan Communications Services Company Limited	17 August 2006
Cheng Hongyan	Chief Executive Officer of Jiangsu Communications Services Company Limited	5 April 2007
Gu Ping	Chief Executive Officer of Anhui Communications Services Company Limited	5 April 2007
Chen Biao	Chief Executive Officer of Jiangxi Communications Services Company Limited	5 April 2007
Xiao Yafan	Chief Executive Officer of Hunan Communications Services Company Limited	5 April 2007
Qi Yan	Chief Executive Officer of Guangxi Communications Services Company Limited	5 April 2007
Li Xiulin	Chief Executive Officer of Chongqing Communications Services Company Limited	5 April 2007
Deng Chang	Chief Executive Officer of Sichuan Communications Services Company Limited	5 April 2007
Guo Zhihao	Chief Executive Officer of Guizhou Communications Services Company Limited	5 April 2007
Qing Deming	Chief Executive Officer of Yunnan Communications Services Company Limited	5 April 2007
Yang Changlin	Chief Executive Officer of Shaanxi Communications Services Company Limited	5 April 2007

Name	Position in the Group	Date of appointment
Li Dazhi	Chief Executive Officer of Gansu Communications Services Company Limited	5 April 2007
Deng Xiaohui	Chief Executive Officer of Qinghai Communications Services Company Limited	5 April 2007
Niu Jiangong	Chief Executive Officer of Xinjiang Communications Services Company Limited	5 April 2007
Yang Fan	Chief Executive Officer of China Communications Services (Hong Kong) International Limited	1 November 2007

In March 2007, Mr. Xu Qiude resigned from the position of chief executive officer of Fujian Communications Services Company Limited and the position was taken by Mr. Yang Yonghe.

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 appointment
Xia Jianghua	Chairperson of the Supervisory Committee	3 August 2006
Hai Liancheng	Independent Supervisor	3 August 2006
Yan Dong	Supervisor (Employee Representative)	15 August 2006

Profile of the directors, supervisors and senior management is set out in “Directors, Supervisors and Senior Management” of this Annual Report.

Report of the Directors

Share Capital

The Company was incorporated on 30 August 2006. In December 2006, the Company issued 1,484,986,000 H shares with a par value of RMB1.00 each, at a price of HK\$2.20 per H share by way of an initial public offering (the "IPO") to Hong Kong and overseas investors. In connection with the IPO, the promoters of the Company converted 148,498,600 domestic state-owned shares of RMB1.00 each into H shares on a one domestic share to one H-share basis and transferred them to the National Council for Social Security Fund of the PRC (the "NSSF"). A total of 1,633,484,600 H shares of the Company were listed on the Stock Exchange during the year 2007. Immediately after the IPO, the registered capital of the company amounted to RMB5,444,986,000. As at 31 December 2007, the share capital of the Company was RMB5,444,986,000, divided into 5,444,986,000 shares of RMB1.00 each, and comprised of:

Shares	Number of Shares	Approximate % of issued share capital
Domestic shares (Total)	3,811,501,400	70%
Domestic shares held by:		
China Telecommunications Corporation ⁽¹⁾	3,487,523,782	64.05%
Guangdong Telecom Industry Group Corporation	236,313,086	4.34%
Zhejiang Telecom Industry Corporation	87,664,532	1.61%
H shares (Total)	1,633,484,600	30%
Total	5,444,986,000 ⁽²⁾	100%

(1) Pursuant to the equity transfer arrangements entered into between China Telecom, and China Mobile Communications Corporation ("China Mobile") and China United Telecommunications Corporation ("China Unicom"), China Telecom agreed to transfer 506,880,000 and 236,300,000 domestic shares to China Mobile and China Unicom respectively. China Telecom will hold the said portion of shares until the date on which the conditions precedent to the equity transfer are met. The equity transfer is conditional upon, amongst others, the lapse of at least one year from the listing date, the transfer having been approved by the State-Owned Assets Supervision and Administration Commission of the PRC and the name of the transferee being registered in the Company's share register. Details of the equity transfer arrangements are disclosed in the Company's prospectus dated 27 November 2006.

(2) The Board announced the completion of a placing of an aggregate of 359,365,600 H shares (including 326,696,000 new H shares and 32,669,600 H shares converted from the existing domestic shares of the Company allocated to and placed on behalf of the NSSF) on 9 April 2008. As a result, the total number of issued shares of the Company has increased from 5,444,986,000 shares to 5,771,682,000 shares, and the total number of H shares held by the public has increased from 1,633,484,600 H shares to 1,992,850,200 H shares. Details of the placing are disclosed in the announcements of the Company dated 28 March 2008 and 9 April 2008 respectively.

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

As at 31 December 2007, the interests or short positions of persons who are entitled to exercise or control the exercise of 5% or more of the voting power at any of the Company's general meetings (excluding the directors and supervisors of the Company) in the shares and underlying shares of equity derivatives of the Company as recorded in the register required to be maintained under Section 336 of the Securities and Futures Ordinance (Cap 571 of the Laws of Hong Kong) (the "SFO") are as follows:

Name of shareholder	Number of shares held	Type of shares	Percentage of the respective type of shares (%)	Percentage of the total number of shares in issue (%)	Capacity
China Telecommunications Corporation ⁽¹⁾	3,811,501,400	Domestic shares	100.00	70.00	Beneficial Owner
China Mobile Communications Corporation ⁽²⁾	506,880,000	Domestic shares	13.30	9.31	Beneficial Owner
China United Telecommunications Corporation ⁽²⁾	236,300,000	Domestic shares	6.20	4.34	Beneficial Owner
Guangdong Telecom Industry Group Corporation ⁽¹⁾	236,313,086	Domestic shares	6.20	4.34	Beneficial Owner
Cisco Systems International B.V.	176,676,000 (L)	H shares	10.82	3.24	Beneficial Owner
INVESCO Hong Kong Limited (previously known as INVESCO Asia Limited)	154,479,000 (L)	H shares	9.45	2.84	Investment Manager
Commonwealth Bank of Australia	147,499,100 (L)	H shares	9.03	2.71	Interests in an entity controlled by a significant shareholder
JPMorgan Chase & Co.	99,714,500 (L)	H shares	6.10	1.83	Beneficial Owner,
	13,986,000 (S)	H shares	0.86	0.26	Investment Manager,
	50,032,000 (P)	H shares	3.06	0.92	Custodian – Licensed Corporation/Approved Lending Agent
Fidelity International Limited	88,268,000 (L)	H shares	5.40	1.62	Investment Manager
Atlantis Investment Management Ltd	83,000,000 (L)	H shares	5.08	1.52	Investment Manager

Remarks: (L): Long Position; (S): Short Position; (P): Lending Pool

- (1) Since China Telecom indirectly holds 100% of the shares in Guangdong Telecom Industry Group Corporation and Zhejiang Telecom Industry Corporation, the 236,313,086 and 87,664,532 domestic shares held by Guangdong Telecom Industry Group Corporation and Zhejiang Telecom Industry Corporation respectively are considered and aggregated into the equity interest held by China Telecom.
- (2) Please refer to the note in the paragraph of this report headed "Share Capital" for details of the equity transfer arrangements entered into between China Telecom and China Mobile and China Unicom, respectively, and the conditions precedents to the equity transfers.

Report of the Directors

Save as stated above, as at 31 December 2007, 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.

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

As at 31 December 2007, 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 2007, 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 37 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 2007.

Public Float

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 Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules") for the period from the date of listing to the date of this report.

Directors' and Supervisors' Service Contract

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 3 years and is renewable in accordance with the Articles of Association of the Company when the initial term expires. 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.

Directors' and Supervisors' Interests in Contracts

For the year ended 31 December 2007, no director or supervisor of the Company had any material interest, whether direct or indirect, in any contract of significance entered into by the Company, any of its holding companies or subsidiaries or fellow subsidiaries, apart from service contracts.

Emoluments of the Directors and Supervisors

Based on the overall remuneration policy of the Company and with reference to the payroll standard of 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 of the audited financial statements for details of the emoluments of the directors and supervisors of the Company in 2007.

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 187 to 188 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 2007.

Bank Loans and Other Borrowings

Please refer to note 32 to the audited financial statements for details of bank loans and other borrowings of the Group.

Property, Plant and Equipment

Please refer to note 17 to the audited financial statements for movements in the fixed assets of the Group for the year ended 31 December 2007.

Distributable Reserves

Please refer to note 44 to the audited financial statements for details of the movements in the reserves of the Company for 2007.

Report of the Directors

Donations

For the year ended 31 December 2007, the Group made charitable and other donations to a total amount of RMB1.12 million.

Subsidiaries and Associated Companies

Please refer to note 22 and note 23 to the audited financial statements for details of the Company's subsidiaries and the Group's interests in associated companies as at 31 December 2007.

Changes in Equity

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

Plan of Employees' Retirement Benefits

Please refer to note 36 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.

Major Customers and Suppliers

For the reporting period, the sales to the five largest customers of the Group represented 65.5% of the operating revenue of the Group; of which, the sales to the largest customers of the Group represented 49.0% of the operating revenue of the Group. The purchases from the five largest suppliers of the Group accounted for less than 8.7% of the total annual purchases of the Group.

So far as the directors are aware, as disclosed in the paragraph headed "Share Capital" of this report, of the five largest customers of the Group during the reporting period, China Telecom held 70% equity interest of the Company, and has agreed to transfer 506,880,000 and 236,300,000 domestic shares of the Company to China Mobile and China Unicom, respectively. China Telecom will keep holding the aforementioned shares prior to the completion of the transfer. As at 31 December 2007, Mr. Liu Aili, a non-executive director of the Company, held 299,100 share purchase options in China Mobile Limited, a subsidiary of China Mobile, one of our five largest customers, and Mr. Zhang Junan, a non-executive director of the Company, held 500,000 share purchase options in China Unicom Corporation Limited, a subsidiary of China Unicom, one of our five largest customers.

Other than that, no director of the Group, their associates, or any person holding more than 5% of the issued share capital of the Company has any interests in such suppliers or customers.

Continuing Connected Transactions

Pursuant to Chapter 14A of the Listing Rules, the transactions between the Group and China Telecom and its subsidiaries (excluding our Group and including China Telecom Corporation Limited, collectively the “China Telecom Group”) constitute connected transactions of the Group.

The following table sets out the amounts of continuing connected transactions of the Group during the year ended 31 December 2007:

Transaction		The Group (RMB million)	Annual cap of continuing connected transaction (RMB million)
Engineering related services provided to China Telecom Group		6,179.59	8,000.00
Ancillary telecommunications services provided to China Telecom Group		3,124.79	3,660.00
Operation support services provided to/by China Telecom Group	Revenue	1,528.44	1,750.00
	Expenditure	245.53	260.00
IT application services provided to/by China Telecom Group	Revenue	649.21	700.00
	Expenditure	181.75	210.00
Property leasing provided to/by China Telecom Group	Revenue	51.52	76.00
	Expenditure	94.33	106.50
Centralized services provided to China Telecom Group		139.25	350.00

Report of the Directors

Continuing Connected Transactions Agreements Between the Group and China Telecommunications Corporation

The Company and China Telecom entered into six continuing connected transactions agreements on 16 November 2006 to manage the connected transactions between the Group and China Telecom Group. These agreements are the Engineering Framework Agreement, the Ancillary Telecommunications Services Framework Agreement, the Operation Support Services Framework Agreement, the IT Application Services Framework Agreement, the Property Leasing Framework Agreement and the Centralized Services Agreement.

The Company completed its acquisition of the Target Business from China Telecom on 31 August 2007. Accordingly, it entered into a supplementary agreement on 15 June 2007 to the above mentioned six continuing connected transactions agreements with China Telecom (the “Supplementary Agreement”) to extend the effective periods of the six continuing connected transactions agreements to 31 December 2009, and to extend the applicable scopes of such agreements to the 19 provinces, being the Group’s current primary service areas after completion of the Company’s acquisitions of the Target Business as in 13 provinces. The terms of the six agreements (as amended by the Supplementary Agreement) are automatically renewable for further periods of no more than three years subject to shareholders’ approval (excluding the Property Leasing Framework Agreement) unless terminated early by either party with three months’ written notification. The Company also set new annual caps for transactions under the six continuing agreements (see the above stated table) at the time of the acquisition of the Target Business as in 13 provinces and the new annual caps for the three years ended 31 December 2009 (excluding the new annual caps for transactions under the Property Leasing Framework Agreement, which did not require independent shareholders approval under the Listing Rules) were approved by the independent shareholders of the Company in the extraordinary general meeting on 7 August 2007.

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 payable for engineering-related services rendered under the Engineering Framework Agreement shall be determined by reference to market rates or as reflected by prices obtained through the tender process. The Company would be accorded 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 favourable than those offered by the Company for the same 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 favourable than those offered by the Company to independent third parties.

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 application, content and other services such as fixed-line value-added services, wireless value-added services, Internet value-added services, and the development of online gaming, certificate authentication and the value-added business platform of Internet cafes (the “Ancillary Telecommunications Services”). Pursuant to the Supplementary Agreement, the Company also agreed to provide China Telecom Group with comprehensive logistics services (including purchase agency, warehousing, transportation, delivery, testing and inspection, logistics information management and distribution). The Ancillary Telecommunications Services Framework Agreement stipulates that the Ancillary Telecommunications Services be provided at:

- (1) government-prescribed price;
- (2) where there is no government-prescribed price but where there is a government-guidance price, the government-guidance price applies;
- (3) where there is neither a government-prescribed price nor a government-guidance price, the market price applies. The market price is defined as the price at which the same type of services are provided by independent third parties in the ordinary course of business; or
- (4) where none of the above is applicable, the price is to be agreed between the relevant parties for the provision of the above services, which shall be the reasonable cost incurred in providing the same plus a reasonable profit (for this purpose, “reasonable costs” means the costs confirmed by both parties after negotiations, and “reasonable profits” means a profit ratio confirmed by both parties during the course of normal commercial negotiation, taking 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).

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 favourable than those offered by us for the same services, and in return, we have undertaken to China Telecom Group that we shall not provide Ancillary Telecommunications Services to it on terms which are less favourable than those offered by us to independent third parties.

Report of the Directors

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, labour resources management, equipment maintenance, advertisements, conferencing services, vehicles, and certain repair and leasing of equipment. Under the same Operation Support Services Framework Agreement, China Telecom Group has agreed to provide operation support services such as logistic services, warehouse, medical care, food and beverages, educational, hotel and travelling services, labour services and other services to us. Each of the parties 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 favourable 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 favourable than those offered to independent third parties. The operation support services under the Operation Support Services Framework Agreement are provided in accordance with the same pricing policy as that of the Ancillary Telecommunications Services Framework Agreement.

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 has also agreed to provide to the Company certain IT application services including but not limited to, basic telecommunications services such as voice and data, value-added services and information application services. The charges payable for such IT application services under the IT Application Services Framework Agreement shall be determined by reference to market rates, for example, rates as reflected by prices obtained through the tender process (with a minimum of three parties tendering bids). The party receiving the relevant services will accord priority to the party providing such services, provided that the terms and conditions offered by independent third parties to the relevant party are no more favourable 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 favourable than those offered to independent third parties.

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 Group's retained specialised telecommunications support businesses in the PRC other than the Company's current primary service areas of 19 provinces and any remaining assets resulting from the restructuring of the Company in these 19 provinces, such as hotels, manufacturing plants, schools and hospitals which are not in association with the specialized telecommunications support businesses; and
2. the provincial headquarters management function to manage remaining assets resulting from the restructuring of the Company in the above mentioned current primary service areas of the Company.

Except otherwise agreed by the parties, the aggregate administrative expenses incurred by us for the provision of the centralized services referred to above (all expenses incurred in connection with the above-mentioned headquarters management functions except remuneration for 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

Pursuant to the Property Leasing Framework Agreement, the rental charges of each property of the Group and China Telecom Group leased by each party from another party are based on market rates. Rental charges are payable monthly in arrears, except as otherwise agreed by parties, and are 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

Continuing Connected Transaction Agreement Between the Group and China Telecom Corporation Limited (Our Fellow Subsidiary)

Strategic Cooperation Agreement

We have entered into a Strategic Cooperation Agreement dated 30 August 2006 with China Telecom Corporation Limited, a subsidiary of China Telecom, for a period of three years commencing 1 January 2007 until 31 December 2009, renewable by mutual agreement and extendable in geographical areas. The areas for strategic business cooperation between the parties shall include engineering related services in connection with our design, construction, project supervision and management businesses; maintenance and management services including but not limited to our network maintenance and facilities management; and certain business process outsourcing services such as integrated information solutions and call centres; and provision of applications, content and other services such as system integration and value-added services.

In connection with the acquisition of the Target Business in 13 provinces from China Telecom, the Company entered into a supplementary agreement to the Strategic Cooperation Agreement (the “Supplementary Strategic Agreement”) with China Telecom Corporation Limited to extend the geographic scope of cooperation between the Company and China Telecom Corporation Limited to 19 provinces.

Pursuant to the Strategic Cooperation Agreement (as amended by the Supplementary Strategic Agreement), in relation to the Company’s provision of engineering related services in design, construction, project supervision and management businesses, China Telecom Corporation Limited has undertaken that the relevant subsidiaries of China Telecom Corporation Limited in the 19 provinces (municipalities and autonomous regions) shall spend an annual minimum amount of not less than 10.6% of the total annual capital expenditure of the relevant wholly-owned provincial subsidiaries of China Telecom Corporation Limited to purchase such services provided by the Company.

In relation to the Company’s provision of maintenance and management services including but not limited to our network maintenance and facilities management businesses, China Telecom Corporation Limited has undertaken that the relevant subsidiaries of China Telecom Corporation Limited in the 19 provinces (municipalities and autonomous regions) shall spend an annual minimum amount of not less than RMB1,780 million to purchase such services provided by the Company.

The Company shall offer at least 5% discount for the engineering-related services to be provided to the relevant wholly-owned provincial subsidiaries of China Telecom Corporation Limited based on the applicable standard prices. Such discount is on normal commercial terms and it is in-line with market practice to give a discount as favourable treatment offered to large enterprise customers which are able to commit to a minimum purchase volume per annum. The percentage discount depends on a number of factors, such as the committed minimum purchase volume, competition and so on.

In relation to the Company's provision of business process outsourcing services, integrated information solutions, call centre and other services such as system integration and value-added services, China Telecom Corporation Limited has undertaken to use its best endeavours to grant us business opportunities, provided our terms and conditions for the provision of such services are no less favourable than those offered by any independent third parties. In return, the Company will utilize its capacities and resources to support the strategic transformation of China Telecom Corporation Limited into an integrated information service provider.

The annual caps for the provision of the relevant services contemplated under the Strategic Cooperation Agreement have already been subsumed respectively under the Engineering Framework Agreement, the Ancillary Telecommunications Services Framework Agreement, the Operation Support Services Framework Agreement and the IT Application Services Framework Agreement referred to above and therefore no separate annual caps shall be applied to the Strategic Cooperation Agreement.

The independent non-executive directors of the Company have confirmed that all continuing connected transactions for the year ended 31 December 2007 to which the Group was a party:

1. had been entered into, and that the agreements governing those transactions had been entered into, by the Group in the ordinary and usual course of business;
2. had been entered into either:
 - (i) on normal commercial terms; or
 - (ii) where there was no available comparison to judge whether they are on normal commercial terms, are on terms no less favourable than those available to or (if applicable) from independent third parties; and

Report of the Directors

3. had been entered into on terms that are fair and reasonable so far as the overall interests of the independent shareholders of the Company are concerned.

The independent non-executive directors have further confirmed that:

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

The auditors of the Company have performed procedures on the continuing connected transactions and issued a letter to the Board to advise that:

- (i) the continuing connected transactions entered into between the Group and China Telecom Group during the year ended 31 December 2007 have been approved by the Directors;
- (ii) they have performed sample checks on the continuing connected transactions entered into between the Group and China Telecom Group during the year ended 31 December 2007 and have not found that the continuing connected transactions were not in accordance with the pricing policies as stated in the relevant agreements;
- (iii) they have performed sample checks on the continuing connected transactions entered into between the Group and China Telecom Group during the year ended 31 December 2007 and have not found that the continuing connected transactions were not in accordance with the terms of the agreements governing the transactions;
- (iv) they note that the continuing connected transactions have not exceeded the 2007 annual caps as disclosed in the circular dated 20 June 2007 of the Company and approved by the independent shareholders of the Company on 7 August 2007.

Employees

As at 31 December 2007, the Group had 106,931 employees as follows:

	Number of staff	Percentage
Management	7,565	7%
Technical and marketing	35,656	33%
Operations	63,710	60%
Total	106,931	100%

The Company has implemented a performance-linked remuneration system. Remuneration for employees includes basic salary, performance-based bonus and welfare. In addition, the Company also emphasizes the importance of employee training and uses various means of training to improve the quality and capability of key employees.

Compliance with Code on Corporate Governance Practices

Please see the “Corporate Governance Report” set out in this Annual Report for details of our compliance with the Code on Corporate Governance Practices.

Material Legal Proceedings

As at 31 December 2007, so far as the directors are aware, the Company was not involved in any material litigation or arbitration and no material litigation claims had been made against, or were pending or threatened against the Company.

Non-adjusting Post Balance Sheet Event

Details of the Company's non-adjusting post balance sheet events are set out on page 186 in this Annual Report.

Report of the Directors

Auditors

KPMG and KPMG Huazhen were engaged respectively as the international and domestic auditors of the Company for the year ended 31 December 2007. KPMG has audited the accompanying financial statements, which have been prepared in accordance with International Financial Reporting Standards. The Company has retained KPMG and KPMG Huazhen since the date of its listing. A resolution for the reappointment of KPMG and KPMG Huazhen as the international and domestic auditors of the Company for the year ending 31 December 2008 will be proposed at the annual general meeting of the Company.

By order of the Board

Wang Xiaochu

Chairman

Beijing, China

8 April 2008