

ZTE中兴

ZTE CORPORATION

中興通訊股份有限公司

(a joint stock limited company incorporated in the People's Republic of China with limited liability)

(Stock Code: 763)

2007 FIRST QUARTERLY REPORT

This announcement is published simultaneously in Shenzhen pursuant to the Rules Governing Listing of Stocks on Shenzhen Stock Exchange and in Hong Kong pursuant to the disclosure obligations under Rule 13.09 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited.

1. IMPORTANT

- 1.1 The Board of Directors, Supervisory Committee and the Directors, Supervisors and senior management of ZTE Corporation (the "Company") confirm that this quarterly report does not contain any false information, misleading statements or material omissions, and collectively and individually accept responsibility for the truthfulness, accuracy and completeness of its contents.
- 1.2 There are no Directors, Supervisors and senior management who are unable to warrant or are in dispute with the truthfulness, accuracy and completeness of the contents of this quarterly report.
- 1.3 This quarterly report has been considered and approved by the third meeting of the fourth session of the Board of Directors of the Company. Mr. Qiao Wenjun, Independent Director, was unable to attend the meeting due to work reasons, and authorised in writing Mr. Mi Zhengkun, Independent Director, to vote on his behalf.
- 1.4 The financial statements contained in this quarterly report are unaudited. The financial information contained in this report has been prepared in accordance with generally accepted accounting principles in the People's Republic of China ("PRC GAAP"). The Company has also disclosed in this quarterly report a reconciliation of net profits and shareholders' equity of the Company and its subsidiaries (together referred to as the "Group") from PRC GAAP to Hong Kong accounting standards ("HKASs").
- 1.5 Mr. Hou Weigui, Chairman of the Company, Mr. Wei Zaisheng, Chief Financial Officer of the Company and Mr. Shi Chunmao, Head of Finance Division of the Company, hereby declare that they warrant the truthfulness and completeness of the financial report contained in this quarterly report.

2. CORPORATE INFORMATION

2.1 Brief analysis of the overall operating conditions of the Group during the reporting period

During the reporting period, the PRC telecommunications industry continued to sustain growth with the mobile sector providing the main drive, while the market for fixed line products contracted further. The Group has been negotiating contracts for the construction of extended trial networks for large-scale application of TD-SCDMA network technologies organised by carriers. On 7 April 2007 the Group received an official notification from China Mobile Group confirming that our TD-SCDMA wireless network products had been selected for networks in Beijing, Tianjin, Shenzhen, Shenyang, Qinghuangdao and Xiamen and our core network products had been selected for networks in Beijing, Guangzhou, Xiamen and Qinhuangdao.

During the reporting period, the international business of the Group expanded rapidly to account for 60% of its revenue. Emerging countries, such as those in the Asia Pacific region, continued to be a major source of revenue for the Group during the period.

Analysed by product segments, a 23% growth was recorded for our wireless products compared to the same period last year mainly as a result of the substantial growth in revenues from international CDMA, GSM. Sales of wireline switch and access decreased by 48% compared to the same period last year. On the other hand, sales of optical and data communications products increased by 48% year-on-year, driven mainly by growth in the international sales of optical communications products. Sales of handset products grew by 51% compared to the same period last year as export grew substantially to offset the decline in domestic sales. Sales of telecommunications software systems, services and other products also achieved an increase of 48% compared to the same period last year.

In a move to better adapt to requirements of developments in the telecommunications industry and telecommunications carriers, the Group make certain moves in organisational restructuring and optimisation during the reporting period, with a view to providing more efficient and comprehensive solutions and services to carriers.

Prospects for the next quarter will be underpinned by further development of 3G building in the PRC, which should generate sound opportunities for the Group to drive the sales of other products. In the international market, the Group will continue to closely monitor investment trends of carriers in the emerging markets in sectors such as mobile communications, broadband and transmission. We will also actively track the development of latest technologies in the market of developed countries, such as broadband, transmission and WiMax. We intend to expand both in terms of the depth of market coverage and sales volumes, capitalising on opportunities for the sales of terminal products presented by the speedy growth of the global population of mobile phone users.

2.2 Financial Information

2.2.1 Major Accounting Data and Financial Indicators of the Group

Item	End of the reporting period	End of last year	Change as at the end of the reporting period compared with the end of last year (%)
Total assets (RMB in thousands)	28,720,952	25,727,237	11.64
Shareholders' equity (excluding minority interests) (RMB in thousands)	10,771,805	10,656,956	1.08
Net assets per share (excluding minority interests) (RMB)	11.23	11.11	1.08

Item	Beginning of year to end of reporting period	Change compared with the same period last year (%)	
Net cashflow from operating activities (RMB in thousand)	(1,283,985)	43.47	
Net cashflow from operating activities per share (RMB)	(1.34)	43.47	

Item	Reporting period	Same period last year	Change compared with the same period last year (%)
Net profit (excluding minority interests) (RMB in thousands)	42,445	33,418	27.01
Earnings per share, basic (RMB)	0.044	0.035	25.71
Earnings per share, diluted (RMB)	0.044	0.035	25.71
Return on net assets (%)	0.39	0.33	Increase by 0.06 percentage points
Return on net assets after extraordinary gains or losses (%)	0.34	0.35	Decrease by 0.01 percentage points

Extraordinary gain or loss items

Item	Amount during the period from the beginning of the year to the end of the reporting period (RMB in thousands)	
Non-operating income (non-recurrent)	11,331	
Less: Non-operating expenses	4,218	
Less: Effect of income tax	1,067	
Total	6,046	

Note: There was no change in share capital of the Company for the period commencing from 1 January 2006 to 31 March 2007, and the share capital of the Company comprised 959,521,650 shares.

2.2.2 Differences in financial statements prepared in accordance with PRC GAAP and HKASs

The effects on the net profit and the shareholders' equity arising from material differences between the consolidated financial statements prepared under PRC GAAP and HKASs standards are summarised as follows:

(Unit: RMB'000)

	Net profit for the three months ended 31 March 2007 (unaudited)	Shareholders' equity at 31 March 2007 (unaudited)
Under PRC GAAP	42,445	10,771,805
Add back/(deduct)		
R&D expenses under different accounting standards	(13,089)	91,147
Deferred tax	1,665	4,420
Under Hong Kong accounting standards	31,021	10,867,372

(i) Deferred development expenses

Before 1 January 2007, according to PRC GAAP, all research and development expenses should be charged to profit and loss when incurred.

According to HKASs, expenses incurred in the development of new products will only be capitalised and deferred for recognition if the projects concerned are clearly defined, the expenses can be separately accounted for and reliably measured and the project can be reasonably ascertained to be technically feasible and the products derived therefrom are commercially viable. Product development expenses that do not meet the aforesaid conditions should be recognised as expenses when incurred.

(ii) Deferred taxation

As a result of the differences in accounting estimates and between PRC GAAP and HKASs, differences in revenue and profit before taxation will arise in the Group's financial statements prepared under PRC GAAP and HKASs. Deferred taxation is recognised as the impact of the temporary differences in income tax, deferred development expenses, and government grants.

2.3 Total number of shareholders and top ten holders of shares not subject to lock-up as at the end of the reporting period

Total number of shareholders as at the end of the reporting period The Company had 42,433 shareholders in total (of which 42,041 were holders of A shares and 392 were holders of H shares).

Top ten holders of shares not subject to lock-up

Name of shareholder	Number of shares not subject to lock-up at the end of the reporting period (shares)	Class
HKSCC Nominees Limited	159,656,639	H shares
ICBC Credit Suisse Stable Growth Stock Securities Investment Fund	18,674,923	A shares
China Life Insurance Company Limited — Dividends — Individual Dividends — 005L-FH002 Shen	14,906,499	A shares
Hunan Nantian (Group) Co., Ltd	11,431,810	A shares
Guotai Junan — Citibank — DEUTSCHE BANK AKTIENGESELLSCHAFT	9,782,806	A shares
JADE DRAGON (MAURITIUS) LIMITED	9,500,000	A shares
ICBC Credit Suisse Selected and Balanced Hybrid Fund	7,925,265	A shares
Fuguo Tianhui Selected Mixed Growth Fund (富國天惠精選成長混合型證券投資基金)	7,766,205	A shares
China Life Insurance Company Limited — Traditional — General Insurance Products	6,915,593	A shares
ICBC Credit Suisse Core Value Stock Securities Investment Fund	6,792,153	A shares

3. MATERIAL MATTERS

3.1 Substantial changes in major accounting items and financial indicators of the Company and the reasons therefor

✓ Applicable □ N/A

Balance Sheet

Items	At		Change	Reasons
	31 March 2007	31 December 2006		
Cash in bank and on hand	2,990,861	4,311,060	-30.62%	Increase in purchase of raw materials and fixed assets
Tradable financial assets	0	33,288	/	Disposal of tradable financial assets by the Group
Trade receivables	7,050,904	5,329,628	32.30%	Deferred payment as part of the favourable credit terms granted to customers by the Group
Prepayments	101,525	51,757	96.16%	Increase in purchase of raw materials by prepayment at the beginning of the year
Inventory	3,595,600	2,481,155	44.92%	Increase in the purchase of raw materials at the beginning of the year following expansion in scale
Investments held to maturity	610,802	0	/	Recognition of forward contract of foreign currency at fair value
Tradable financial liabilities	613,051	3,689	16,518.35%	Recognition of forward contract of foreign currency at fair value
Notes payable	3,586,780	2,242,566	59.94%	Increase of purchase of raw materials using notes
Advances from customers	842,638	635,875	32.52%	Increase in advances from customers in tandem with increased sales
Remuneration payable to staff	582,109	1,090,862	-46.64%	Performance bonus payment and adjustments in the financial policies relating to welfare expenses
Tax payable	(1,039,682)	(690,767)	-50.51%	Increase in deduction in VAT tax as a result of increased purchase volume
Dividend payable	58,753	83,941	-30.01%	Dividend payment by subsidiaries
Long-term loans	2,439,419	1,679,242	45.27%	Increase in long-term bank loans

Income Statement

Items	For the three months ended		Change	Reason
	31 March 2007	31 March 2006		
Operating income	6,010,780	4,603,289	30.58%	Increase in sales and faster progress for construction projects
Cost of sales	4,134,320	3,087,252	33.92%	Increase in sales and slight rise in cost ratios
Taxes and surcharges	30,111	16,418	83.40%	Increase in service income
Finance expenses	129,319	13,141	884.09%	Increase in interest expense, foreign exchange loss and increase in the cost for factoring and guarantee letters
Asset impairment losses	19,535	(131,026)	114.91%	Increase in bad debt provision
Investment gains	6,776	(3,408)	298.83%	Increase in investment gains from short-term stock trading
Operating profit	1,522	54,940	-97.23%	Decrease in gross profit margin and increase in R&D expenses
Non-operating income	98,706	14,925	561.35%	Increase in software tax rebate
Non-operating expenses	4,218	7,425	-43.19%	Decrease in loss on retirement of fixed assets
Total profit	96,010	62,440	53.76%	Increase in software tax rebate
Income tax expenses	22,048	14,665	50.34%	Increase in profit before taxation
Net profit (including minority interests)	73,962	47,775	54.81%	Increase in software tax rebate
Net profit attribute to minority interests	31,517	14,357	119.52%	Increase in the percentage of profit contribution from non-wholly owned subsidiaries

Unit: RMB'000

	For the three months ended 31 March 2007		For the three months ended 31 March 2006	
	Group	Company	Group	Company
III. Total profit	<u>96,010</u>	<u>47,206</u>	62,440	228,615
Less: Profit tax expenses	<u>22,048</u>	<u>0</u>	14,665	5,416
IV. Net profit	<u>73,962</u>	<u>47,206</u>	47,775	223,199
Attributable to owners of the parent	42,445	47,206	33,418	223,199
Minority interests	31,517	—	14,357	—
V. Earnings per share				
(I) Earnings per share, basic	0.044		0.035	
(II) Earnings per share, diluted	0.044		0.035	
Legal representative: Hou Weigui	Chief Financial Officer: Wei Zaisheng		Head of Finance Division: Shi Chunmao	

4.3 CASH FLOW STATEMENT (unaudited)

Unit: RMB'000

Item	For the three months ended 31 March 2007		For the three months ended 31 March 2006	
	Group	Company	Group	Company
I. Cash flow from operating activities				
Cash received from sales of goods or rendering of services	4,652,094	4,089,960	3,814,520	3,678,242
Cash received from taxes returned	133,023	95,968	56,481	45,045
Cash received relating to other operating activities	<u>22,394</u>	<u>16,177</u>	<u>26,264</u>	<u>15,052</u>
Sub-total of cash inflow	<u>4,807,511</u>	<u>4,202,105</u>	<u>3,897,265</u>	<u>3,738,339</u>
Cash paid for goods and services	3,927,465	4,465,948	4,339,288	4,472,143
Cash paid to and on behalf of employees	1,234,179	482,732	723,951	308,209
Payments of taxes and levies	312,240	48,492	172,123	45,236
Cash paid relating to other operating activities	<u>617,612</u>	<u>143,198</u>	<u>933,146</u>	<u>825,699</u>
Sub-total of cash outflow	<u>6,091,496</u>	<u>5,140,370</u>	<u>6,168,508</u>	<u>5,651,287</u>
Net cash flows from operating activities	<u>(1,283,985)</u>	<u>(938,265)</u>	<u>(2,271,243)</u>	<u>(1,912,948)</u>
II. Cash flows from investing activities				
Cash received from sale of investments	16,225	—	—	—
Cash received from gains of investment	21,415	—	—	—
Net cash received from disposal of fixed assets, intangible assets and other long-term assets	1,214	—	691	605
Net cash received from disposal of subsidiaries and other business units	—	—	—	—
Sub-total of cash inflow	<u>38,854</u>	<u>—</u>	<u>691</u>	<u>605</u>
Cash paid to acquire fixed asset, intangible assets and other long-term assets	494,534	279,366	81,038	62,592
Cash paid for investment	—	—	2,247	—
Cash paid for the acquisition of subsidiaries and other business units	—	—	—	—
Sub-total of cash outflow	<u>494,534</u>	<u>279,366</u>	<u>83,285</u>	<u>62,592</u>
Net cash flow from investing activities	<u>(455,680)</u>	<u>(279,366)</u>	<u>(82,594)</u>	<u>(61,987)</u>
III. Cash flows from financing activities				
Cash received from investments	—	—	—	—
Cash received from borrowings	787,489	673,144	121,100	100,000
Sub-total of cash inflow	<u>787,489</u>	<u>673,144</u>	<u>121,100</u>	<u>100,000</u>
Cash paid for debt repayment	310,373	309,368	55,696	—
Cash paid in dividend distribution or interest repayment	49,774	48,261	34,644	25,714
Cash paid in relation to other financing activities	—	—	—	—
Sub-total of cash outflow	<u>360,147</u>	<u>357,629</u>	<u>90,340</u>	<u>25,714</u>
Net cash flow from financing activities	<u>427,342</u>	<u>315,515</u>	<u>30,760</u>	<u>74,286</u>
IV Effect of foreign exchange rate changes on cash	<u>(7,876)</u>	<u>(302)</u>	<u>3,829</u>	<u>(30)</u>
V Net increase in cash and cash equivalents	<u>(1,320,199)</u>	<u>(902,418)</u>	<u>(2,319,248)</u>	<u>(1,900,679)</u>
Add: Opening balance of cash and cash equivalents	4,311,060	2,957,920	5,573,132	4,258,936
VI Closing balance of cash and cash equivalents	<u>2,990,861</u>	<u>2,055,502</u>	<u>3,253,884</u>	<u>2,358,257</u>
Legal representative: Hou Weigui	Chief Financial Officer: Wei Zaisheng		Head of Finance Division: Shi Chunmao	

By order of the Board
Hou Weigui
Chairman