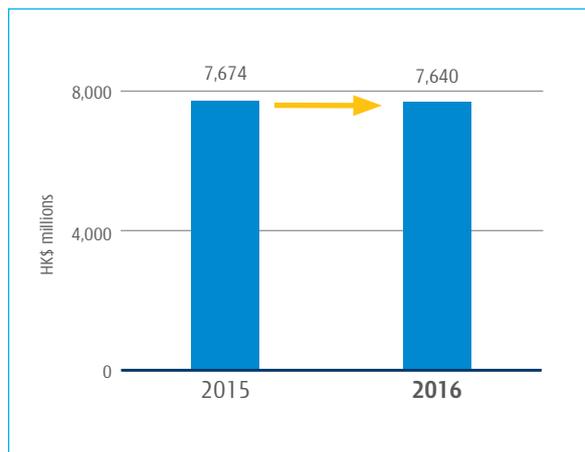


Management Discussion and Analysis

Financial Review

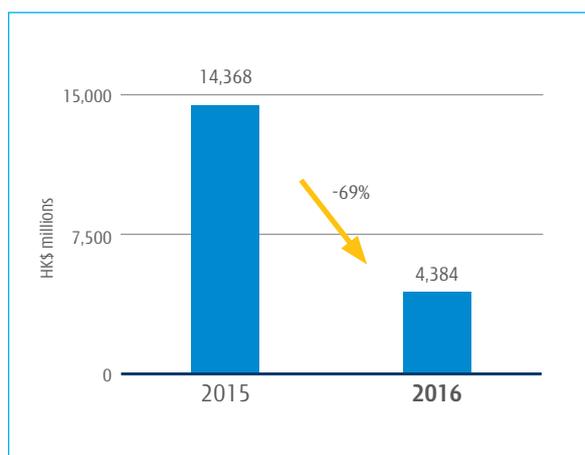
Consolidated service revenue in 2016 was HK\$7,640 million, comparable to HK\$7,674 million in 2015. This was the result of a 4% increase in fixed-line revenue, partially offset by a 4% decrease in mobile service revenue.

Consolidated service revenue



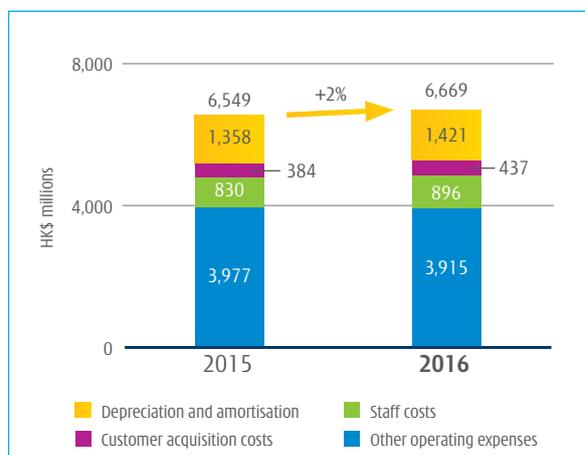
Consolidated hardware revenue was HK\$4,384 million in 2016, a decrease of 69% from HK\$14,368 million in 2015 resulting from lesser demand for new smartphones during the year.

Consolidated hardware revenue



Total operating expenses, excluding cost of inventories sold, amounted to HK\$6,669 million in 2016, slightly higher than HK\$6,549 million in 2015. Overall, total operating expenses were managed such that they had below inflationary incremental change, this outcome was achieved despite higher operating expenses including call centre costs and additional spectrum licence fee amortisation were incurred to help generate future growth.

Key cost items



Consolidated service EBITDA in 2016 was HK\$2,392 million, a decrease of 4% compared to HK\$2,483 million in 2015. Consolidated service EBITDA margin was 31% in 2016.

Depreciation and amortisation amounted to HK\$1,421 million in 2016 compared to HK\$1,358 million in 2015. The increase was mainly a result of enhancement of the 4G LTE network infrastructure as well as an increase in spectrum licence fee amortisation on 2100MHz band and 2300MHz band after its activation in 2016.

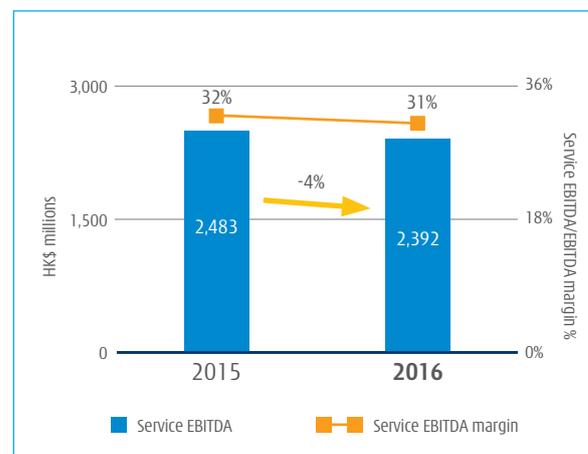
Consolidated service EBIT was HK\$971 million in 2016, a decrease of 14% compared to 2015, mainly due to an increase in depreciation and amortisation mentioned above together with the decrease in consolidated service EBITDA.

Net interest and other finance costs amounted to HK\$95 million in 2016, representing a decrease of 8% compared to HK\$103 million in 2015. This decrease was the result of lower notional finance charge on decreasing spectrum licence fee liabilities, partially offset by higher finance costs on increased level of bank borrowings to finance one-off payment of mobile spectrum licence fee on 2100MHz band, the licence period of which was renewed for another 15 years to 2031. Gearing ratio as of 31 December 2016, calculated by dividing net debt by net total capital, was 26% (2015: 20%) as a result of higher net debt position.

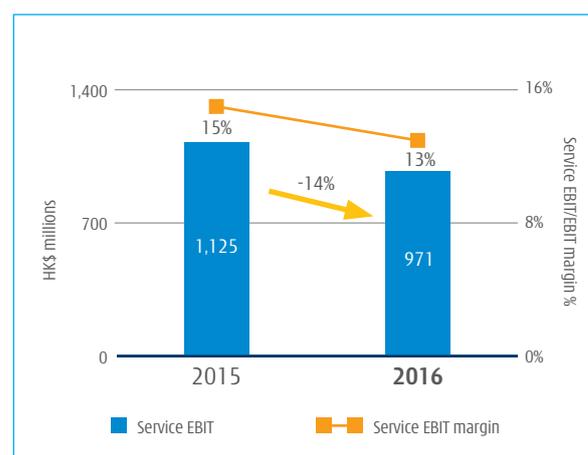
Share of joint venture losses in 2016 decreased to HK\$21 million compared to HK\$34 million in 2015 mainly due to improved occupancy performance of the data centre joint venture business in 2016.

Overall, profit attributable to shareholders of the company in 2016 was HK\$701 million, a decrease of 23% compared to HK\$915 million in 2015.

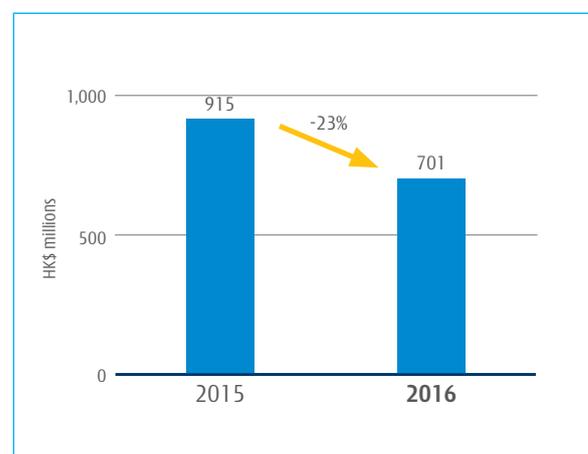
Consolidated service EBITDA



Consolidated service EBIT



Profit attributable to shareholders



Business Review

The Group is engaged in two principal businesses - mobile and fixed-line.

Hong Kong and Macau mobile business highlights

	For the year ended 31 December 2016 HK\$ millions	For the year ended 31 December 2015 HK\$ millions	Favourable/ (unfavourable) change
Total revenue	8,332	18,477	-55%
- Net customer service revenue	3,946	4,106	-4%
- Local service revenue	3,224	3,275	-2%
- Roaming service revenue	722	831	-13%
- Hardware revenue	4,386	14,371	-69%
- Bundled sales revenue	712	815	-13%
- Standalone handset sales revenue	3,674	13,556	-73%
Net customer service margin	3,656	3,823	-4%
<i>Net customer service margin %</i>	93%	93%	-
Standalone handset sales margin	73	308	-76%
Total CACs	(1,037)	(1,085)	+4%
Less: Bundled sales revenue	712	815	-13%
Total CACs (net of handset revenue)	(325)	(270)	-20%
Operating expenses	(2,071)	(2,224)	+7%
<i>Opex as a % of net customer service margin</i>	57%	58%	+1% point
EBITDA	1,333	1,637	-19%
Service EBITDA	1,260	1,329	-5%
<i>Service EBITDA margin %</i>	32%	32%	-
Depreciation and amortisation	(733)	(661)	-11%
EBIT	600	976	-39%
Service EBIT	527	668	-21%
CAPEX (excluding licence)	(589)	(574)	-3%
EBITDA less CAPEX	744	1,063	-30%
Spectrum licence fee	(1,779)	(3)	

Mobile business revenue in 2016 was HK\$8,332 million, a decrease of 55% compared to HK\$18,477 million in 2015. 98% of the decline in revenue was due to lower hardware revenue because of reduced demand for new smartphones during the year. Hardware revenue decreased significantly by 69% from HK\$14,371 million in 2015 to HK\$4,386 million in 2016.

Mobile net customer service revenue in 2016 was HK\$3,946 million, a 4% decrease compared to HK\$4,106 million in 2015. The decrease in mobile net customer service revenue was mainly due to a HK\$109 million, or 13% decrease in roaming revenue during the year. Excluding roaming revenue, local service revenue was slightly lower than that in 2015 as a result of a drop in customer number in the first quarter of 2016 and such drop was turnaround since the second quarter of 2016. The net customer service margin in 2016 was maintained at 93% despite a lower roaming revenue during the year.

EBITDA and EBIT in 2016 were HK\$1,333 million and HK\$600 million respectively, a decrease of 19% and 39% respectively compared to those of 2015. Service EBITDA in 2016 was 5% lower than that of 2015 mainly as a result of decrease in roaming margin as well as increase in selling expenses from higher volume of service transactions completed in 2016, partially offset by savings in operating expenses. Corresponding service EBITDA margin was maintained at 32%.

As of 31 December 2016, the Group was serving approximately 3.2 million customers in Hong Kong and Macau (2015: approximately 3.0 million), of which the number of postpaid customers was approximately 1.5 million (2015: approximately 1.5 million). The overall churn rate of postpaid customers was substantially improved to 1.3% in 2016 from 1.8% in 2015, which reflected much improved customers' satisfaction on the 4G LTE network quality and enhanced customer service.

Customer response from various segments was overwhelming and the number of data-centric customers increased in 2016 following the introduction of innovative lifestyle-related tariff plans with various offerings in speed, content and VAS. The blended local postpaid net ARPU improved 4% from HK\$161 in 2015 to HK\$168 in 2016 as a result of higher data consumption during the year. Blended local postpaid net AMPU improved 5% to HK\$161 in 2016 from HK\$154 in 2015. Growing popularity around OTT applications and IoT usage prompted the Group to prepare for a new era of digitalisation and automation, in which more personalised content will be offered to customers. The Group will focus on developing local and roaming products and tariff plans to meet demand from various customer base and to boost revenue. At the same time, the Group is committed to developing customer loyalty initiatives for long-term benefits.

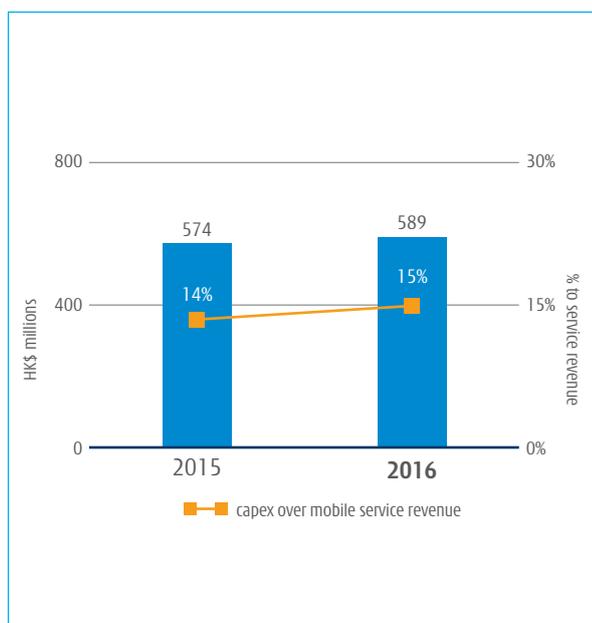
In 2016, the Group enhanced its mobile network by refarming a portion of existing 900MHz spectrum band to enhance indoor 4G LTE coverage, while a new 2300MHz spectrum band was activated to meet the rising demand for data. Small-cell technology was deployed to enhance both coverage and capacity in heavy traffic areas and growing data demand into the 5G era.

Key performance indicators for mobile business

	For the year ended 31 December 2016	For the year ended 31 December 2015	Favourable/ (unfavourable) change
Number of postpaid customers ('000)	1,486	1,484	-
Number of prepaid customers ('000)	1,736	1,547	+12%
Total customers ('000)	3,222	3,031	+6%
Postpaid customers to the total customer base (%)	46%	49%	-3% points
Postpaid customers' contribution to the net customer service revenue (%)	93%	93%	-
Monthly postpaid churn rate (%)	1.3%	1.8%	+0.5% point
Local postpaid gross ARPU (HK\$)	210	212	-1%
Local postpaid net ARPU (HK\$)	168	161	+4%
Local postpaid net AMPU (HK\$)	161	154	+5%

Capital expenditure on property, plant and equipment in 2016 amounted to HK\$589 million (2015: HK\$574 million), accounting for 15% (2015: 14%) of mobile service revenue. The slight increase in capital expenditure in 2016 was mainly a result of long-term investment in network enhancement for 4.5G technology and preparation for coming 5G technology for better service and long-term cost savings in future.

Mobile capex



Summary of spectrum investment

as of 31 December 2016

Spectrum band	Bandwidth	Year of expiry
Hong Kong		
900 MHz	10 MHz	2026
900 MHz	16.6 MHz	2020
1800 MHz	23.2 MHz	2021
2100 MHz	29.6 MHz	2031
2300 MHz	30 MHz	2027
2600 MHz	30 MHz*	2024
2600 MHz	10 MHz*	2028
Macau		
900 MHz	15.6 MHz	2023
1800 MHz	38.8 MHz	2023
2100 MHz	20 MHz	2023

* Shared under 50/50 joint venture - Genius Brand Limited

Fixed-line business highlights

	For the year ended 31 December 2016 HK\$ millions	For the year ended 31 December 2015 HK\$ millions	Favourable/ (unfavourable) change
Revenue	4,127	3,973	+4%
Operating expenses	(2,875)	(2,699)	-7%
<i>Opex as % of revenue</i>	70%	68%	-2% points
EBITDA	1,252	1,274	-2%
<i>EBITDA margin %</i>	30%	32%	-2% points
Depreciation and amortisation	(688)	(697)	+1%
EBIT	564	577	-2%
CAPEX (excluding licence)	(509)	(485)	-5%
EBITDA less CAPEX	743	789	-6%

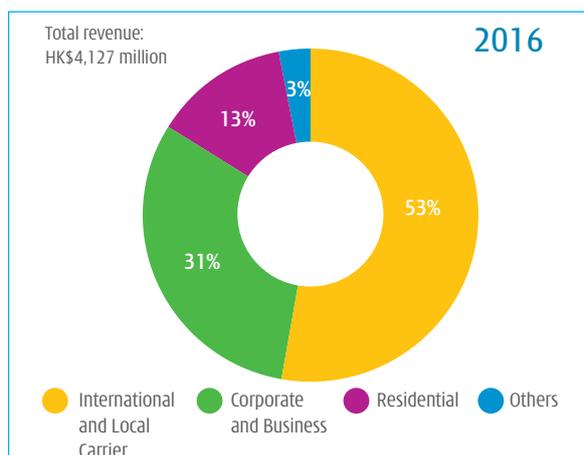
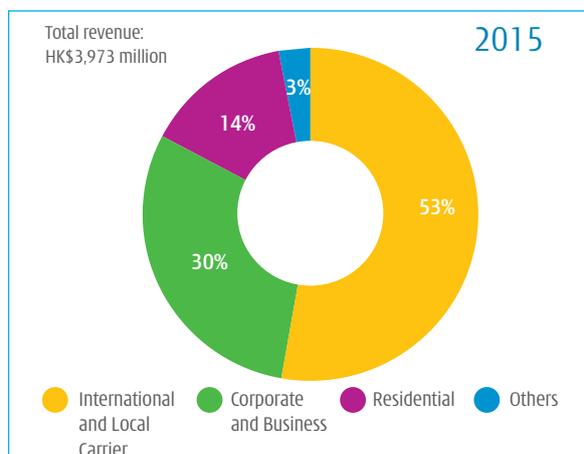
Fixed-line service revenue in 2016 was HK\$4,127 million, an increase of 4% compared to HK\$3,973 million in 2015. This improvement was mainly due to higher revenue from corporate and business market segments as well as the international and local carrier markets, partially offset by lower revenue from residential market due to keen competition.

More revenue was generated by developing ICT solutions for corporate customers with sophisticated needs when compared to 2015. During 2016, the Group deepened penetration of various market segments such as banking, insurance, logistics and healthcare. Moving forward, the Group will place more focus on penetrating new industry segments and offer industry-specific one-stop ICT solutions. In addition, the Group will leverage its data centre capabilities and sophisticated network infrastructure to develop high security cloud solutions to help customers achieve greater cost efficiency, while accelerating digital transformation.

EBITDA and EBIT in 2016 slightly decreased by 2% to HK\$1,252 million and HK\$564 million respectively compared to those of 2015.

Capital expenditure on property, plant and equipment in 2016 amounted to HK\$509 million (2015: HK\$485 million), representing 12% (2015: 12%) of fixed-line service revenue. The slight increase in capital expenditure in 2016 was mainly a result of additional network equipment acquired to meet corporate customer requirements.

Fixed-line service revenue



Fixed-line capex

