

Management Discussion and Analysis

Financial Performance Summary - Pre-IFRS 16 basis ⁽¹⁾

	2019 HK\$ million	2018 HK\$ million	Change
Revenue	5,582	7,912	-29%
- Net customer service revenue	3,613	3,662	-1%
• Local service revenue	2,875	2,980	-4%
• Roaming service revenue	738	682	+8%
- Data	517	427	+21%
- Non-data	221	255	-13%
- Hardware revenue	1,969	4,250	-54%
• Bundled sales revenue	472	667	-29%
• Standalone handset sales revenue	1,497	3,583	-58%
Net customer service margin	3,266	3,318	-2%
<i>Net customer service margin %</i>	90%	91%	-1% point
Standalone handset sales margin	28	49	-43%
Total margin	3,294	3,367	-2%
CACs	(797)	(959)	+17%
Less: Bundled sales revenue	472	667	-29%
CACs (net of hardware revenue)	(325)	(292)	-11%
Operating expenses	(1,837)	(1,991)	+8%
<i>Operating expenses as a % of net customer service margin</i>	56%	60%	+4% points
Share of EBITDA of a joint venture	69	73	-5%
EBITDA	1,201	1,157	+4%
Service EBITDA	1,173	1,108	+6%
<i>Service EBITDA margin %</i>	32%	30%	+2% points
CAPEX (excluding telecommunications licences)	(503)	(522)	+4%
EBITDA less CAPEX	698	635	+10%
Depreciation and amortisation ⁽²⁾	(808)	(818)	+1%
EBIT	393	339	+16%
Service EBIT	365	290	+26%
Net interest and other finance income ⁽²⁾	147	171	-14%
Profit before tax	540	510	+6%
Tax ⁽²⁾	(104)	(77)	-35%
Profit attributable to non-controlling interests	(8)	(29)	+72%
Profit attributable to shareholders	428	404	+6%

Notes:

(1) Following the adoption of IFRS 16 on 1 January 2019, the Group's statutory results for the year ended 31 December 2019 are on an IFRS 16 basis, whereas the statutory results for the year ended 31 December 2018 are on an IAS 17 basis ("Pre-IFRS 16 basis") as previously reported. Hence, any comparison between the two bases of reporting would not be meaningful. The Group believes that the IAS 17 basis metrics, which are not intended to be a substitute for, or superior to, the reported metrics on an IFRS 16 basis ("Post-IFRS 16 basis"), allows a like-with-like comparison with the prior year results, and better reflects management's view of the underlying operational performance. As a result, the Group has provided an alternative presentation of the Group's EBITDA, EBIT and profit attributable to shareholders prepared under the Pre-IFRS 16 basis relating to the accounting for leases for the year ended 31 December 2019. Unless otherwise specified, the discussion of the Group's operating results in this results announcement is on a Pre-IFRS 16 basis.

(2) Depreciation and amortisation, net interest and other finance income and tax include the Group's share of joint venture's respective items.

Financial Performance Summary - Post-IFRS 16 basis ⁽¹⁾

	2019 HK\$ million	2018 HK\$ million	Change
Revenue	5,582	7,912	-29%
- Net customer service revenue	3,613	3,662	-1%
• Local service revenue	2,875	2,980	-4%
• Roaming service revenue	738	682	+8%
- Data	517	427	+21%
- Non-data	221	255	-13%
- Hardware revenue	1,969	4,250	-54%
• Bundled sales revenue	472	667	-29%
• Standalone handset sales revenue	1,497	3,583	-58%
Net customer service margin	3,266	3,318	-2%
<i>Net customer service margin %</i>	90%	91%	-1% point
Standalone handset sales margin	28	49	-43%
Total margin	3,294	3,367	-2%
CACs	(744)	(959)	+22%
Less: Bundled sales revenue	472	667	-29%
CACs (net of hardware revenue)	(272)	(292)	+7%
Operating expenses	(1,429)	(1,991)	+28%
<i>Operating expenses as a % of net customer service margin</i>	44%	60%	+16% points
Share of EBITDA of a joint venture	69	73	-5%
EBITDA	1,662	1,157	+44%
Service EBITDA	1,634	1,108	+47%
<i>Service EBITDA margin %</i>	45%	30%	+15% points
CAPEX (excluding telecommunications licences)	(503)	(522)	+4%
EBITDA less CAPEX	1,159	635	+83%
Depreciation and amortisation ⁽²⁾	(1,253)	(818)	-53%
EBIT	409	339	+21%
Service EBIT	381	290	+31%
Net interest and other finance income ⁽²⁾	132	171	-23%
Profit before tax	541	510	+6%
Tax ⁽²⁾	(104)	(77)	-35%
Profit attributable to non-controlling interests	(8)	(29)	+72%
Profit attributable to shareholders	429	404	+6%

Notes:

(1) Following the adoption of IFRS 16 on 1 January 2019, the Group's statutory results for the year ended 31 December 2019 are on an IFRS 16 basis, whereas the statutory results for the year ended 31 December 2018 are on an IAS 17 basis ("Pre-IFRS 16 basis") as previously reported. Hence, any comparison between the two bases of reporting would not be meaningful. The Group believes that the IAS 17 basis metrics, which are not intended to be a substitute for, or superior to, the reported metrics on an IFRS 16 basis ("Post-IFRS 16 basis"), allows a like-with-like comparison with the prior year results, and better reflects management's view of the underlying operational performance. As a result, the Group has provided an alternative presentation of the Group's EBITDA, EBIT and profit attributable to shareholders prepared under the Pre-IFRS 16 basis relating to the accounting for leases for the year ended 31 December 2019. Unless otherwise specified, the discussion of the Group's operating results in this results announcement is on a Pre-IFRS 16 basis.

(2) Depreciation and amortisation, net interest and other finance income and tax include the Group's share of joint venture's respective items.

Review of Financial Results

The Group's total revenue decreased by 29% to HK\$5,582 million (2018: HK\$7,912 million).

Service revenue slightly dropped by 1% to HK\$3,613 million, primarily due to a 4% decrease in local service revenue from stiffening market competition in local data tariffs, largely offset by the improvement in roaming service revenue and higher contribution from corporate solutions.

Roaming service revenue, which accounted for 20% of the Group's service revenue (2018: 19%), reported an 8% increase to HK\$738 million, underpinned by a 21% strong growth in data roaming revenue, reflecting the increasing popularity of our innovative roaming products and packages for frequent and leisure travellers.

Hardware revenue of HK\$1,969 million was 54% lower than last year, mainly due to softer demand for new smartphones as the handset replacement cycle lengthened.

During the year, the Group continued to adhere to its strict cost discipline, fostering a low cost high efficiency operational environment. Key costs (Pre-IFRS 16 basis), comprising CACs, staff costs and other operating expenses, decreased by 4% to HK\$2,509 million mainly due to operating expense savings from the implementation of various efficiency measures and initiatives.

On a Pre-IFRS 16 basis, the Group's total EBITDA increased by 4% to HK\$1,201 million (2018: HK\$1,157 million).

Service EBITDA (Pre-IFRS 16 basis) grew 6% to HK\$1,173 million, benefiting from the aforementioned savings in key costs, partly offset by lower service margins from keen market competition. Service EBITDA margin (Pre-IFRS 16 basis) improved to 32% from 30% in 2018.

On a Pre-IFRS 16 basis, the Group's total EBIT increased by 16% to HK\$393 million (2018: HK\$339 million) and profit attributable to shareholders increased by 6% to HK\$428 million (2018: HK\$404 million), mainly due to the same factors noted above in respect of EBITDA.

On a Post-IFRS 16 basis, total EBITDA grew by 44% to HK\$1,662 million. Taking into account the additional amortisation charges of HK\$445 million from the recognition of right-of-use assets under IFRS 16, total EBIT increased by 21% to HK\$409 million and profit attributable to shareholders increased by 6% to HK\$429 million.

Key performance indicators

	2019	2018	Change
Number of postpaid customers ('000)	1,475	1,499	-2%
Number of prepaid customers ('000)	2,180	1,777	+23%
Total customers ('000)	3,655	3,276	+12%
Postpaid customers to the total customer base (%)	40%	46%	-6% points
Postpaid customers' contribution to the net customer service revenue (%)	87%	90%	-3% points
Monthly churn rate of postpaid customers (%)	1.2%	1.3%	+0.1% point
Postpaid gross ARPU (HK\$)	205	219	-6%
Postpaid net ARPU (HK\$)	176	186	-5%
Postpaid net AMPU (HK\$)	161	169	-5%

As of 31 December 2019, the total number of customers in Hong Kong and Macau was approximately 3.7 million (31 December 2018: approximately 3.3 million). The increase was mainly due to growing subscriptions in the prepaid segment, which accounted for 60% of the total customer base (31 December 2018: 54%), as a result of increasing popularity of prepaid roaming cards for travellers.

During the year, as the Group continued to focus on enhancing its customer retention programmes, monthly postpaid churn rate improved to 1.2% (2018: 1.3%). Postpaid gross ARPU decreased by 6% to HK\$205 in 2019 (2018: HK\$219), reflecting tariff pricing pressure from keen market competition, despite rapid growth in data demand.

Net interest and other finance income

Net interest and other finance income (Post-IFRS 16 basis, with share of a joint venture) amounted to HK\$132 million in 2019, compared with HK\$171 million in 2018, mainly due to lower net cash balance subsequent to the distribution of special interim dividend in May 2019.

The Group continues to maintain a healthy financial position, despite a 43% decrease in net cash from HK\$9,555 million at 31 December 2018 to HK\$5,416 million at 31 December 2019. The lower net cash position was mainly due to the distribution of 2018 special interim dividend and final dividend as well as 2019 interim dividend totalling HK\$4,150 million, and the acquisition of non-controlling interests in key subsidiaries of the Group during the year.

Acquisition of non-controlling interests

On 31 May 2019, the Group completed the acquisition of non-controlling interests in its key subsidiaries at a consideration of US\$60 million (approximately HK\$471 million). Post the acquisition, the Group now has 100% interest in its mobile business.

Capital expenditure

Capital expenditure on property, plant and equipment, which accounted for 14% (2018: 14%) of the Group's service revenue, reduced by 4% to HK\$503 million. The decrease was mainly attributable to stringent control on capital expenditure and rescheduling of projects to better match future benefits. The Group continues to scrutinise capital expenditure with care and prudence, ensuring adequate resources are made available in accordance with operational and technological needs.

Spectrum investment

In October 2019, the Group acquired 40 MHz in the 3500 MHz band for 15 years from 2020 for a spectrum utilisation fee of HK\$202 million through auction. In November 2019, the Group further acquired 30 MHz in the 3300 MHz band for a spectrum utilisation fee of HK\$199.5 million for 15 years from 2019 through another auction.

Summary of spectrum investment

as of 31 December 2019

	Spectrum band	Bandwidth	Year of expiry
Hong Kong	900 MHz	10 MHz	2026
	900 MHz	16.6 MHz	2021 [#]
	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
	3300 MHz	30 MHz	2034
Macau	900 MHz	10 MHz	2023
	1800 MHz	20 MHz	2023
	2100 MHz	10 MHz	2023

[#] After the spectrum auction and licence renewal in 2018, the licence period of the existing 16.6 MHz in the 900 MHz band was extended from November 2020 to January 2021 to align with the new spectrum assignment period. Subsequently, the Group will hold 10 MHz in the 900 MHz band and 30 MHz in the 1800 MHz band from 2021 to 2036.

* The spectrum band was shared under 50/50 joint venture – Genius Brand Limited.