

Management Discussion and Analysis

Financial Review

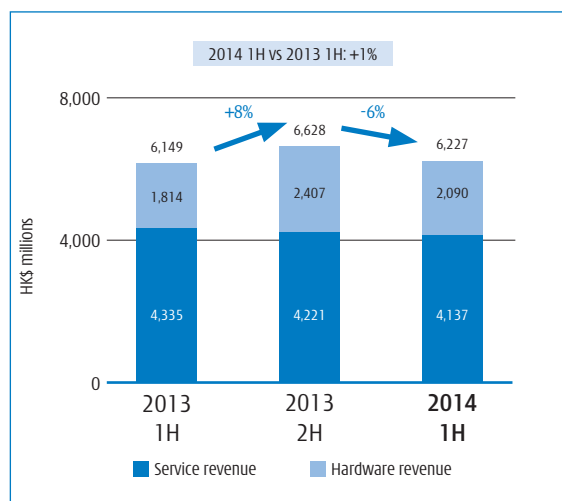
Consolidated turnover for the first half of 2014 was HK\$6,227 million, which increased slightly by 1% when compared with HK\$6,149 million for the first half of 2013. The increase was mainly due to a 15% increase in hardware revenue from HK\$1,814 million in the first half of 2013 to HK\$2,090 million in the first half of 2014. The total service revenue decreased from HK\$4,335 million in the first half of 2013 to HK\$4,137 million in the first half of 2014, mainly due to the decrease in mobile service revenue of 11%, partially offset by the increase in fixed-line service revenue of 4%.

Compared with the second half of 2013, the decrease in total service revenue narrowed to 2% as the 3% growth in fixed-line service revenue partially offset the 6% decrease in mobile service revenue. Hardware revenue decreased by 13% as a popular handset model was launched in the second half of 2013 but no similar handset model was available in the first half of 2014.

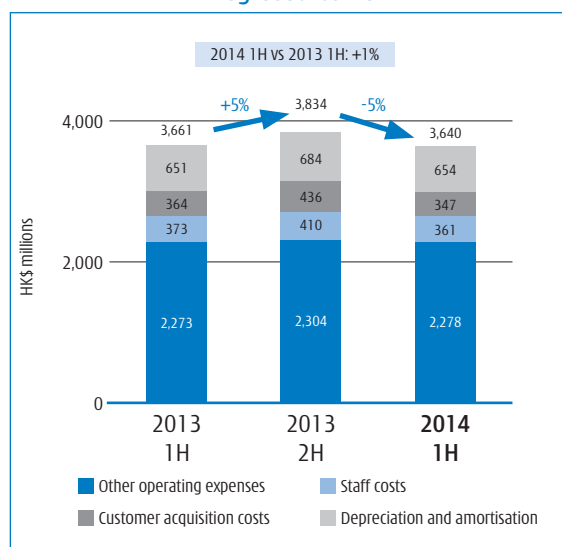
Total operating expenses, excluding cost of inventories sold, amounted to HK\$3,640 million for the first half of 2014, reduced by 1% when compared with HK\$3,661 million for the first half of 2013, and decreased by 5% when compared with HK\$3,834 million for the second half of 2013, as a result of stringent cost controls.

Consolidated EBITDA was HK\$1,181 million in the first half of 2014, a reduction of 20% when compared with the first half of 2013, with EBITDA margin on service revenue decreased from 34% to 29%. Depreciation and amortisation amounted to HK\$654 million in the first half of 2014, maintaining at the same level as the first half of 2013. Consolidated EBIT was HK\$527 million, a decrease of 36% when compared with the first half of 2013, but an improvement of 2% when compared with the second half of 2013.

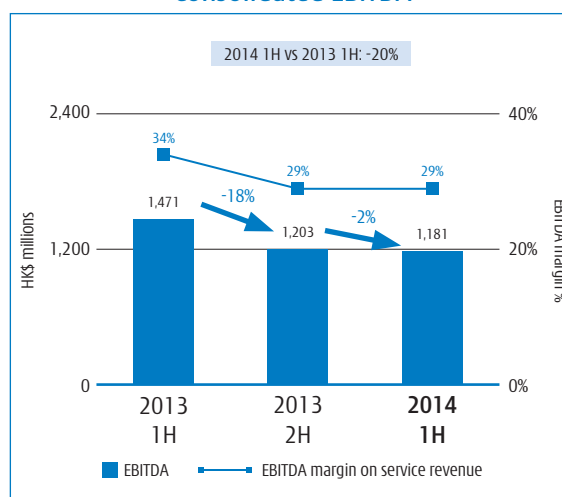
Consolidated turnover



Key cost items



Consolidated EBITDA

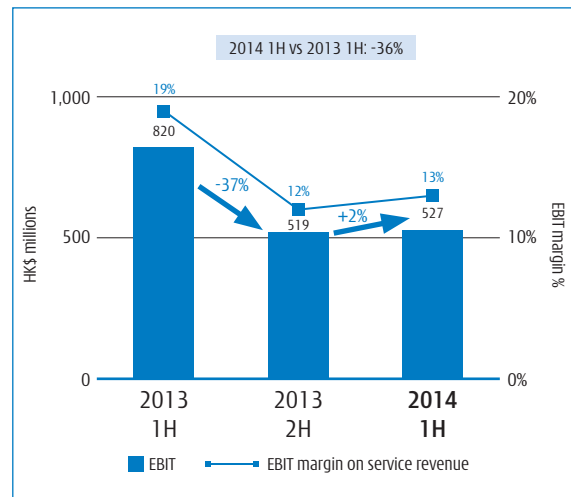


Interest and other finance costs decreased by 6% from HK\$87 million for the first half of 2013 and decreased by 13% from HK\$94 million for the second half of 2013 to HK\$82 million for the first half of 2014 as a result of lower notional finance charge on decreasing licence fees liabilities. Gearing ratio as at 30 June 2014, calculated by dividing net debt by net total capital, was 25% (31 December 2013: 28%). Share of losses of joint ventures for the first half of 2014 amounted to HK\$12 million compared with HK\$4 million in the same period in 2013 and HK\$8 million for the second half of 2013 as the Group continued to develop its data centre facilities, one of which commenced operations in March 2014.

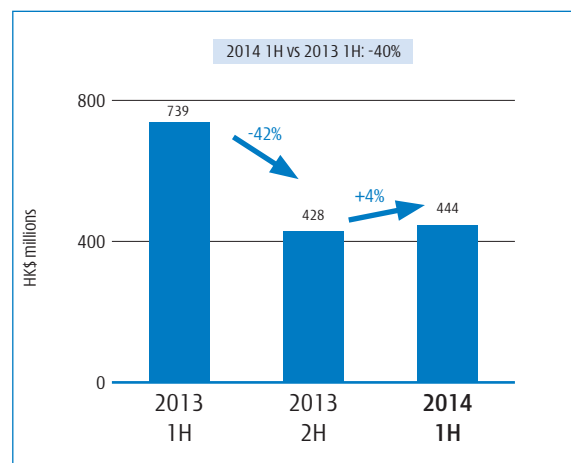
Accordingly, profit before taxation was HK\$444 million for the first half of 2014, a decrease of 40% from HK\$739 million for the same period in 2013, but an improvement of 4% when compared with HK\$428 million for the second half of 2013. Following years of profitability of the mobile business, carried forward tax losses have effectively been utilised, resulting in an increase in a deferred tax expense being booked in the period. Together with increased profitability of the fixed-line business, taxation increased from HK\$39 million for the first half of 2013 and HK\$38 million for the second half of 2013 to HK\$82 million for the first half of 2014.

Overall, profit attributable to shareholders of the Company for the first six months of 2014 was HK\$323 million. This represented a decrease of 44% compared with HK\$572 million for the first half of 2013 and a decrease of 6% compared with HK\$344 million for the second half of 2013.

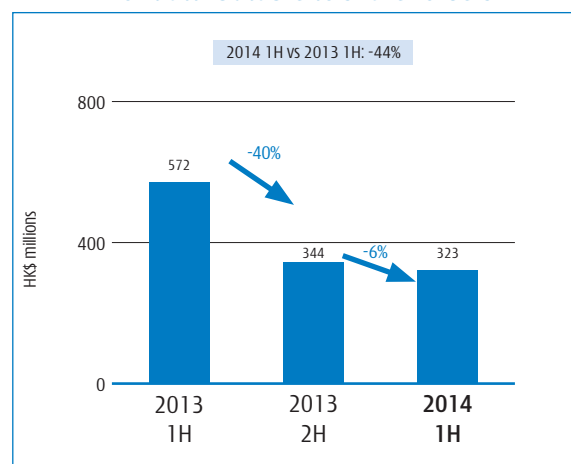
Consolidated EBIT



Profit before taxation



Profit attributable to shareholders



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Business Review

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

Hong Kong and Macau Mobile business highlights

	For the six months ended 30 June 2014 HK\$ millions	For the six months ended 31 December 2013 HK\$ millions	For the six months ended 30 June 2013 HK\$ millions	2014 1H vs 2013 2H Change	2014 1H vs 2013 1H Change
Total revenue	4,438	4,907	4,452	-10%	No change
- Service revenue	2,348	2,500	2,638	-6%	-11%
- Hardware revenue	2,090	2,407	1,814	-13%	+15%
<i>Net customer service revenue margin %⁽¹⁾</i>	89%	87%	87%	+2% points	+2% points
EBITDA	614	629	941	-2%	-35%
<i>EBITDA margin %</i>	26%	25%	36%	+1% point	-10% points
Depreciation and amortisation	(306)	(318)	(291)	+4%	-5%
EBIT	308	311	650	-1%	-53%
CAPEX	220	331	326	+34%	+33%
EBITDA less CAPEX	394	298	615	+32%	-36%

Total revenue of the mobile business for the first six months of 2014 was HK\$4,438 million, maintaining at the same level for the same period in 2013. The mobile service revenue decreased by 11% when compared with the first half of 2013 as a result of continued intense price competition as well as a significant decrease in demand for non-data and roaming services. Total data service revenue⁽²⁾ from local and overseas accounted for 55% of mobile service revenue, which was higher than 52% for the first half of 2013. Service revenue margin improved to 89% due to lower roaming-related service revenue generated, compared with 87% for the first half and second half of 2013. Hardware revenue grew by 15% to HK\$2,090 million when compared with the first half of 2013 as a result of more standalone hardware sales during the period.

EBITDA was HK\$614 million for the first half of 2014, representing a decrease of 35% when compared with the first half of 2013. Corresponding EBIT was HK\$308 million for the first half of 2014, representing a decrease of 53% when compared with the first half of 2013 as a result of lower mobile service revenue.

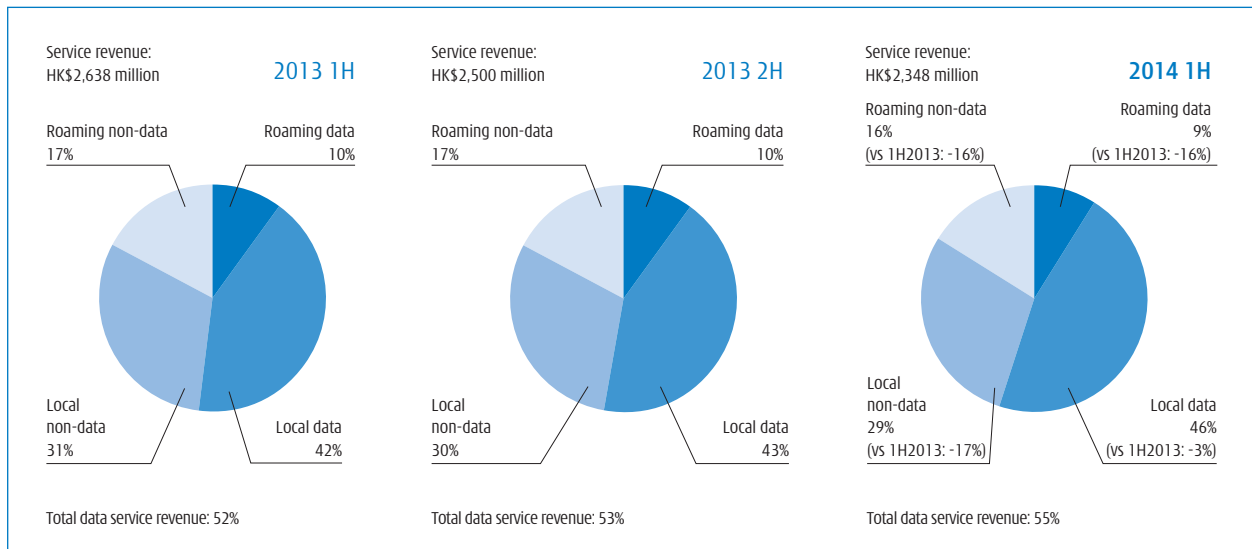
Compared with the second half of 2013, the mobile hardware revenue reduced by 13% while mobile service revenue reduced by 6% as a result of change in the sales mix and a greater number of customers on lower-tier service plans. The impact of lower revenue was partially offset by savings from continued focus on cost management resulting in EBITDA and EBIT declines of only 2% and 1% respectively. Correspondingly, EBITDA margin on service revenue improved from 25% for the second half of 2013 to 26% for the first half of 2014.

Notes:

(1) *Net customer service revenue margin is defined as service revenue less direct variable costs (including interconnection charges and roaming costs).*

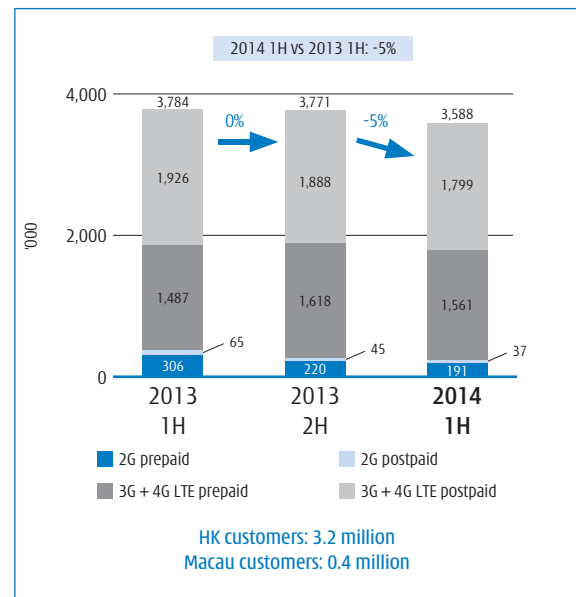
(2) *Data service revenue is defined as customer payment for internet and data access services, excluding messaging, content and related services. Non-data service revenue is defined as customer payment for items including voice, messaging, content and related services.*

Mobile service revenue



As of 30 June 2014, the Hong Kong and Macau customers amounted to approximately 3.6 million (31 December 2013: 3.8 million), of which postpaid customers totalled approximately 1.8 million (31 December 2013: 1.9 million), being 51% of total customer base (31 December 2013: 51%). The decrease in customer number was mainly due to increased churn among lower-tier customer group since the second half of 2013. Churn rate of postpaid customers was 1.8% in the first six months of 2014, compared with 1.9% in the first six months of 2013.

Total customers



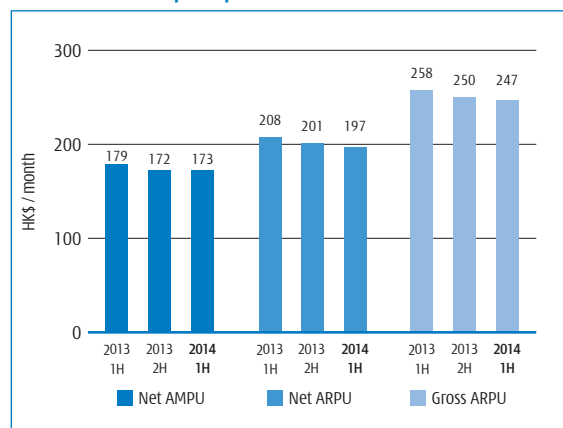
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As of 30 June 2014, 62% of 3G and 4G LTE postpaid customers in Hong Kong and Macau were smart device users (31 December 2013: 61%). Blended postpaid net ARPU⁽³⁾ for the first half of 2014 was HK\$197, compared with HK\$208 for the first half of 2013. Blended postpaid net AMPU⁽⁴⁾ for the first half of 2014 was HK\$173, compared with HK\$179 for the first half of 2013. Lower average net ARPU and net AMPU when compared with that in the first half of 2013 were due to slower smartphone adoption and customers being more cautious in choosing their tariff plans.

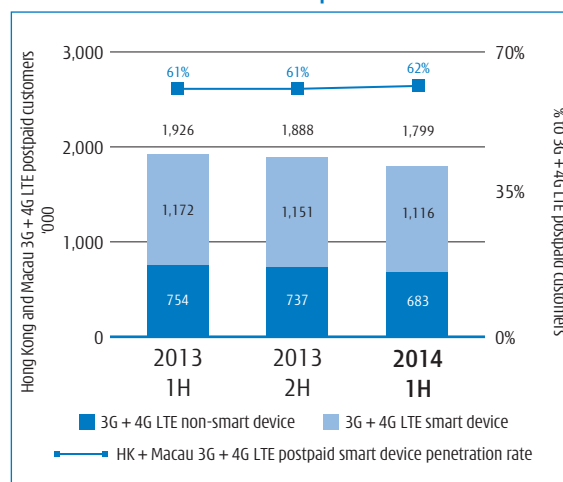
When compared with the second half of 2013, net ARPU decreased by 2% but net AMPU was in line with the second half of 2013 due to lower roaming-related revenue during the first half of 2014.

Capital expenditure on property, plant and equipment for the first six months of 2014 amounted to HK\$220 million (1H 2013: HK\$326 million, 2H 2013: HK\$331 million), accounting for 9% (1H 2013: 12%, 2H 2013: 13%) of mobile service revenue. A lower capital expenditure was recorded in the first six months of 2014 as major 4G LTE-related network establishment investment was completed in 2013.

Blended postpaid ARPU and net AMPU



Smart device penetration

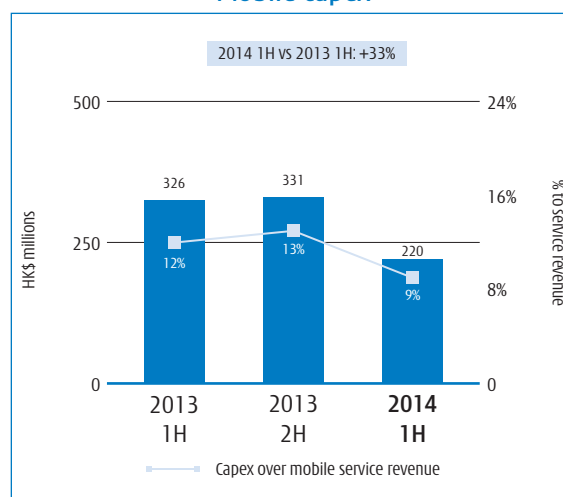


Summary of spectrum investment

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	34.6 MHz	2016
2300 MHz	30 MHz	2027
2600 MHz	30 MHz*	2024
2600 MHz	10 MHz*	2028
Macau		
900 MHz	15.6 MHz	2015
1800 MHz	10 MHz	2015
2100 MHz	20 MHz	2015

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

Mobile capex



Notes:

(3) ARPU represents average revenue per user. Gross ARPU is defined as monthly average spending per user including a customer's contribution to handset, or other devices, in a bundled service and hardware plan. Net ARPU is defined as monthly average spending per user excluding a customer's contribution to handset, or other devices, in a bundled service and hardware plan.

(4) Net AMPU represents average net margin per user. Net AMPU equals net ARPU less direct variable costs (including interconnection charges and roaming costs).

Fixed-line business highlights

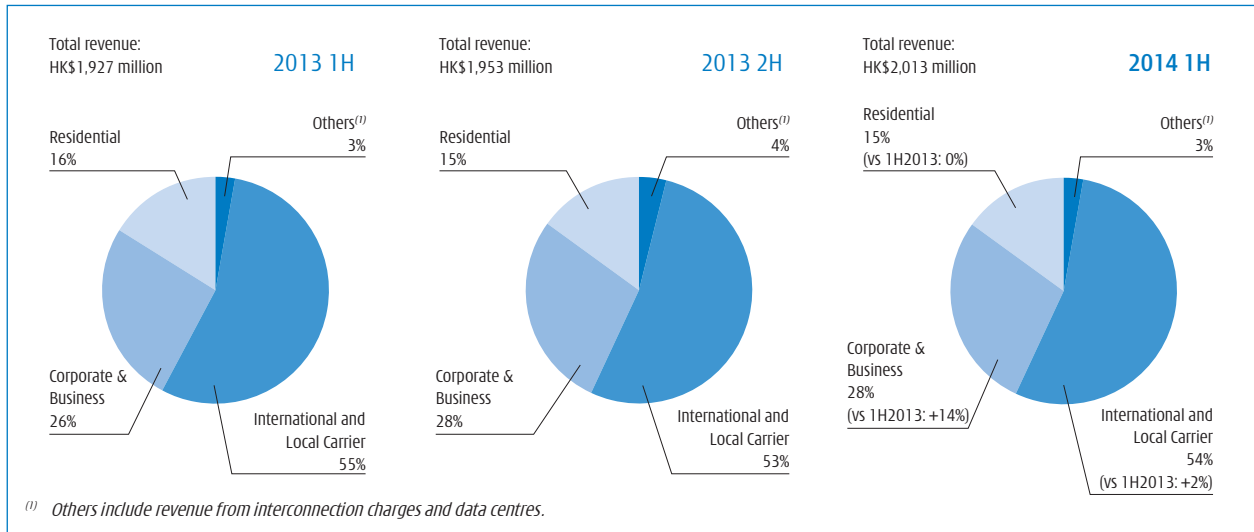
	For the six months ended 30 June 2014 HK\$ millions	For the six months ended 31 December 2013 HK\$ millions	For the six months ended 30 June 2013 HK\$ millions	2014 1H vs 2013 2H Change	2014 1H vs 2013 1H Change
Total revenue	2,013	1,953	1,927	+3%	+4%
EBITDA	631	641	593	-2%	+6%
<i>EBITDA margin %</i>	<i>31%</i>	<i>33%</i>	<i>31%</i>	<i>-2% points</i>	<i>No change</i>
Depreciation and amortisation	(348)	(366)	(360)	+5%	+3%
EBIT	283	275	233	+3%	+21%
CAPEX	200	387	236	+48%	+15%
EBITDA less CAPEX	431	254	357	+70%	+21%

Total revenue increased from HK\$1,927 million for the first six months of 2013 to HK\$2,013 million for the same period in 2014, representing an increase of 4%. The overall increase was mainly contributed by the increase in revenue generated from the corporate and business market. Due to increased demand for comprehensive solution-based services by corporate and business market customers, revenue from corporate and business market increased by 14% from HK\$493 million for the first half of 2013 to HK\$560 million for the same period in 2014. International and local carrier market continued to be the main contributor to the fixed-line revenue, which increased by 2% to HK\$1,077 million when compared with HK\$1,059 million for the same period in 2013. Revenue from the residential market remained stable at HK\$302 million, which was HK\$301 million for the first half of 2013.

EBITDA for the first half of 2014 amounted to HK\$631 million, an increase of 6% from HK\$593 million for the first half of 2013. EBITDA margin for the first half of 2014 was 31%, maintaining at the same level as the first half of 2013. EBIT for the first half of 2014 amounted to HK\$283 million, representing an increase of 21% compared with HK\$233 million for the first half of 2013.

Compared with the second half of 2013, the fixed-line revenue increased by 3% as a result of higher revenue generated from carrier business as well as from corporate and business market. EBITDA of the fixed-line business decreased by 2% while EBIT increased by 3%. EBITDA margin on service revenue reduced slightly from 33% for the second half of 2013 to 31% for the first half of 2014. The lower EBITDA and EBITDA margin were due to a different country mix of revenue generated from the international carrier business during the different periods. Lower depreciation and amortisation expenses resulted in the increase in EBIT.

Fixed-line revenue



Capital expenditure on property, plant and equipment for the first six months of 2014 amounted to HK\$200 million (1H 2013: HK\$236 million, 2H 2013: HK\$387 million), representing 10% (1H 2013: 12%, 2H 2013: 20%) of fixed-line service revenue. A lower capital expenditure in the first six months of 2014 as compared with the first half and second half of 2013 was mainly due to re-scheduling of certain projects to the second half of 2014.

Fixed-line capex

