

Management Discussion and Analysis

Financial Summary

	1H 2019 HK\$ million	1H 2018 HK\$ million	Change
Revenue	2,515	4,021	-37%
- Net customer service revenue	1,782	1,843	-3%
• Local service revenue	1,424	1,494	-5%
• Roaming service revenue	358	349	+3%
- Data	246	211	+17%
- Non-data	112	138	-19%
- Hardware revenue	733	2,178	-66%
• Bundled sales revenue	213	339	-37%
• Standalone handset sales revenue	520	1,839	-72%
Net customer service margin	1,617	1,681	-4%
<i>Net customer service margin %</i>	91%	91%	-
Standalone handset sales margin	9	22	-59%
CACs (before net of handset revenue)	(308)	(412)	+25%
Less: Bundled sales revenue	213	339	-37%
CACs	(95)	(73)	-30%
Operating expenses and staff costs ⁽²⁾	(779)	(1,065)	+27%
<i>Operating expenses and staff costs as a % of net customer service margin</i>	48%	63%	+15% points
Post-IFRS 16 basis			
EBITDA	787	601	+31%
Service EBITDA	778	579	+34%
<i>Service EBITDA margin %</i>	44%	31%	+13% points
Depreciation and amortisation	(603)	(381)	-58%
EBIT	160	195	-18%
Service EBIT	151	173	-13%

Note 2: Operating expenses and staff costs (Pre-IFRS 16 basis) for the first six months of 2019 was HK\$1,012 million, representing 63% of net customer service margin.

Financial Summary (Continued)

	1H 2019 HK\$ million	1H 2018 HK\$ million	Change
<u>Pre-IFRS 16 basis</u>			
EBITDA	554	601	-8%
Service EBITDA	545	579	-6%
<i>Service EBITDA margin %</i>	31%	31%	-
Depreciation and amortisation	(379)	(381)	+1%
EBIT	151	195	-23%
Service EBIT	142	173	-18%
CAPEX (excluding spectrum licences)	(154)	(282)	+45%
EBITDA (Post-IFRS 16 basis) less CAPEX	633	319	+98%
EBITDA (Pre-IFRS 16 basis) less CAPEX	400	319	+25%

Review of Financial Results

Revenue for the first half of 2019 was HK\$2,515 million, a 37% decrease compared with HK\$4,021 million for the first half of 2018.

Service revenue was HK\$1,782 million, a 3% decrease compared with the same period last year, while local service revenue decreased by 5%, mainly as a result of stiffening market competition in local data tariffs. Roaming service revenue, which accounted for 20% of the service revenue of the Group (1H 2018: 19%), continued to grow after introduction of innovative products and packages for frequent and leisure travellers. It increased by 3% to HK\$358 million, the highest half-year amount since 2017, in particular, roaming data revenue increased by 17%.

Hardware revenue of HK\$733 million was 66% lower than that of the same period in 2018, reflecting softer demand for new smartphones.

The Group continued to adhere to its strict cost discipline during the first six months of 2019, fostering a high-efficiency, low-key cost spending operational environment. Key cost items (Pre-IFRS 16 basis, total of CACs, staff costs and other operating expenses) decreased by 2% to HK\$1,272 million for the first half of 2019.

EBITDA (Pre-IFRS 16 basis) and service EBITDA (Pre-IFRS 16 basis) decreased by 8% and 6% respectively. Service margins remained under pressure as intense market competition prevailed during the first half of 2019 which led to service revenue decline as mentioned above, partially compensated by lower key cost spending. Service EBITDA margin (Pre-IFRS 16 basis) remained stable at 31% (1H 2018: 31%).

Depreciation and amortisation was HK\$603 million for the first half of 2019, compared with HK\$381 million for the same period last year. Excluding additional amortisation charges of HK\$224 million from recognition of right-of-use assets under IFRS 16, depreciation and amortisation was 1% lower, on a like-for-like basis.

The impact of IFRS 16 on the EBIT of the Group was not significant. EBIT for the first half of 2019 was HK\$160 million, an 18% decrease compared with HK\$195 million for the first half of 2018, as a result of the same factors noted above in respect of EBITDA.

Key Performance Indicators

	1H 2019	2H 2018	1H 2018	1H 2019 vs 2H 2018 Change
Number of postpaid customers ('000)	1,491	1,499	1,499	-1%
Number of prepaid customers ('000)	1,837	1,777	1,915	+3%
Total customers ('000)	3,328	3,276	3,414	+2%
Postpaid customers to the total customer base (%)	45%	46%	44%	-1% point
Postpaid customers' contribution to the net customer service revenue (%)	87%	90%	91%	-3% points
Monthly churn rate of postpaid customers (%)	1.1%	1.4%	1.2%	+0.3% point
Postpaid gross ARPU (HK\$)	205	217	222	-6%
Postpaid net ARPU (HK\$)	175	184	188	-5%
Postpaid net AMPU (HK\$)	160	166	172	-4%

As of 30 June 2019, the total number of customers in Hong Kong and Macau was approximately 3.3 million (31 December 2018: approximately 3.3 million). Postpaid customers accounted for 45% (31 December 2018: 46%) of the total customer base. The Group focused on retention programme, compared with the second half of 2018, postpaid churn improved to 1.1% (2H 2018: 1.4%) in an environment with keen competition. The blended postpaid gross ARPU decreased by 6% to HK\$205 for the first half of 2019 (2H 2018: HK\$217), mainly the result of intense market competition in tariff pricing, despite rapid growth in mobile data demand.

Net Interest and Other Finance Income

Net interest and other finance income amounted to HK\$92 million for the first half of 2019, compared with HK\$79 million for the same period last year. This increase mainly aligned with a lift in HIBOR during the first half of 2019. The Group maintains a robust financial position with a net cash position of HK\$5,353 million as of 30 June 2019 (31 December 2018: HK\$9,555 million). The reduction in net cash balance was mainly due to the settlement of special interim dividend and final dividend of HK\$4,009 million in total and the acquisition of non-controlling interests of key subsidiaries of the Group.

Acquisition of Non-Controlling Interests

On 31 May 2019, the Group completed the acquisition of non-controlling interests in its key subsidiaries for a consideration of US\$60 million (approximately HK\$471 million). After the transaction, the Group is able to gain full control of all its mobile subsidiaries and enhance operational efficiency from savings in communications to non-controlling shareholder.

Capital Expenditure

Capital expenditure on property, plant and equipment, which accounted for 9% (1H 2018: 15%) of the service revenue of the Group, amounted to HK\$154 million (1H 2018: HK\$282 million) for the first six months of 2019. This substantial decrease was mainly the result of stringent control of capital expenditure and rescheduling of projects to better match future benefits. The Group continues to scrutinise capital expenditure with care, while ensuring adequate resources are made available in accordance with operational and technological needs.

Summary of spectrum investment

as of 30 June 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
Macau		
900 MHz	15.6 MHz	2023
1800 MHz	28.8 MHz	2023
2100 MHz	10 MHz	2023

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

[#] After the spectrum auction and licence renewal in 2018, the licence period of the existing 16.6 MHz in the 900 MHz band has been 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.