

Management Discussion and Analysis

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

	1H 2020 HK\$ million	1H 2019 HK\$ million	Change
Revenue	1,982	2,515	-21%
Net customer service revenue	1,664	1,782	-7%
• Local service revenue	1,443	1,424	+1%
• Roaming service revenue	221	358	-38%
- Data	146	246	-41%
- Non-data	75	112	-33%
Hardware revenue	318	733	-57%
• Bundled sales revenue	149	213	-30%
• Standalone handset sales revenue	169	520	-68%
Net customer service margin	1,462	1,617	-10%
Net customer service margin %	88%	91%	-3% points
Standalone handset sales margin	3	9	-67%
Total margin	1,465	1,626	-10%
CACs	(258)	(371)	+30%
Less: Bundled sales revenue	149	213	-30%
CACs (net of hardware revenue)	(109)	(158)	+31%
Operating expenses	(830)	(949)	+13%
Operating expenses as a % of net customer service margin	57%	59%	+2% points
Share of EBITDA of a joint venture	33	35	-6%
EBITDA	559	554	+1%
Service EBITDA	556	545	+2%
Service EBITDA margin %	33%	31%	+2% points
CAPEX (excluding telecommunications licences)	(105)	(154)	+32%
EBITDA less CAPEX	454	400	+14%
Depreciation and amortisation ⁽²⁾	(416)	(403)	-3%
EBIT	143	151	-5%
Service EBIT	140	142	-1%
Net interest and other finance income ⁽²⁾	51	90	-43%
Profit before taxation	194	241	-20%
Taxation ⁽²⁾	(45)	(46)	+2%
Profit attributable to non-controlling interests	-	(8)	+100%
Profit attributable to shareholders	149	187	-20%

Note 1: Following the adoption of IFRS 16 "Leases" on 1 January 2019, the Group's statutory results for the six months ended 30 June 2019 and 2020 are on an IFRS 16 basis. The Group believes that the precedent lease accounting standard IAS 17 basis ("Pre-IFRS 16 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"), better reflect 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 six months ended 30 June 2019 and 2020. Unless otherwise specified, the discussion of the Group's operating results in this interim report is on a Pre-IFRS 16 basis.

Note 2: Depreciation and amortisation, net interest and other finance income and taxation include the Group's share of joint venture's respective items.

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

	1H 2020 HK\$ million	1H 2019 HK\$ million	Change
Revenue	1,982	2,515	-21%
Net customer service revenue	1,664	1,782	-7%
• Local service revenue	1,443	1,424	+1%
• Roaming service revenue	221	358	-38%
- Data	146	246	-41%
- Non-data	75	112	-33%
Hardware revenue	318	733	-57%
• Bundled sales revenue	149	213	-30%
• Standalone handset sales revenue	169	520	-68%
Net customer service margin	1,462	1,617	-10%
Net customer service margin %	88%	91%	-3% points
Standalone handset sales margin	3	9	-67%
Total margin	1,465	1,626	-10%
CACs	(234)	(343)	+32%
Less: Bundled sales revenue	149	213	-30%
CACs (net of hardware revenue)	(85)	(130)	+35%
Operating expenses	(635)	(744)	+15%
Operating expenses as a % of net customer service margin	43%	46%	+3% points
Share of EBITDA of a joint venture	33	35	-6%
EBITDA	778	787	-1%
Service EBITDA	775	778	-
Service EBITDA margin %	47%	44%	+3% points
CAPEX (excluding telecommunications licences)	(105)	(154)	+32%
EBITDA less CAPEX	673	633	+6%
Depreciation and amortisation ⁽²⁾	(631)	(627)	-1%
EBIT	147	160	-8%
Service EBIT	144	151	-5%
Net interest and other finance income ⁽²⁾	43	82	-48%
Profit before taxation	190	242	-21%
Taxation ⁽²⁾	(44)	(46)	+4%
Profit attributable to non-controlling interests	-	(8)	+100%
Profit attributable to shareholders	146	188	-22%

Note 1: Following the adoption of IFRS 16 "Leases" on 1 January 2019, the Group's statutory results for the six months ended 30 June 2019 and 2020 are on an IFRS 16 basis. The Group believes that the precedent lease accounting standard IAS 17 basis ("Pre-IFRS 16 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"), better reflect 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 six months ended 30 June 2019 and 2020. Unless otherwise specified, the discussion of the Group's operating results in this interim report is on a Pre-IFRS 16 basis.

Note 2: Depreciation and amortisation, net interest and other finance income and taxation include the Group's share of joint venture's respective items.

Review of Financial Results

The Group's total revenue for the first half of 2020 decreased by 21% to HK\$1,982 million (1H 2019: HK\$2,515 million).

Service revenue decreased by 7% to HK\$1,664 million, largely due to a 38% decline in roaming service revenue which accounted for 13% of the Group's service revenue for the period (1H 2019: 20%).

Hardware revenue of HK\$318 million was 57% lower than the same period in 2019, reflecting lower spending on consumables and a fall in demand for new smartphones.

The Group continued to adhere to a strict cost discipline regime during the first six months of 2020, with the aim of creating a low-cost, high-efficiency operational environment. Key costs (Pre-IFRS 16 basis), comprising CACs, staff costs and other operating expenses, decreased by 10% to HK\$1,141 million.

On a Pre-IFRS 16 basis, the Group's total EBITDA increased by 1% to HK\$559 million (1H 2019: HK\$554 million), while EBIT decreased by 5% to HK\$143 million against the same period last year due to higher depreciation and amortisation.

Service EBITDA (Pre-IFRS 16 basis) increased by 2% to HK\$556 million for the first half of 2020, benefiting from the aforementioned savings in key costs, partly offset by lower total margin. Service EBITDA margin (Pre-IFRS 16 basis) improved to 33% (1H 2019: 31%).

On a Post-IFRS 16 basis, the Group's total EBITDA and EBIT decreased by 1% and 8% respectively against the same period last year. Profit attributable to shareholders and earnings per share were HK\$146 million and 3.03 HK cents, a 22% decrease compared with HK\$188 million and 3.90 HK cents respectively of the same period last year. The decrease was mainly due to lower interest income as the cash balance has significantly reduced from HK\$9,555 million in the beginning of 2019 to HK\$5,536 million as of 30 June 2020 subsequent to the distribution of HK\$3,855 million special interim dividend and HK\$471 million cash paid for the acquisition of a 24.1% interest in the Group's mobile operation in May 2019. The interest income forgone corresponded to an approximately 0.77 HK cents decrease in earnings per share. Excluding the effect of interest income reduction, profit attributable to shareholders dropped marginally by 3% against the same period last year. The impact of IFRS 16 on total EBIT and profit attributable to shareholders of the Group was insignificant.

Key Performance Indicators

	1H 2020	1H 2019	Change
Number of postpaid customers ('000)	1,458	1,491	-2%
Number of prepaid customers ('000)	1,851	1,837	+1%
Total customers ('000)	3,309	3,328	-1%
Postpaid customers to the total customer base (%)	44%	45%	-1% point
Postpaid customers' contribution to the net customer service revenue (%)	90%	87%	+3% points
Monthly churn rate of postpaid customers (%)	1.1%	1.1%	-
Postpaid gross ARPU (HK\$)	196	205	-4%
Postpaid net ARPU (HK\$)	170	175	-3%
Postpaid net AMPU (HK\$)	151	160	-6%
Local postpaid gross ARPU (HK\$)	175	173	+1%
Local postpaid net ARPU (HK\$)	150	143	+5%

As of 30 June 2020, the total number of customers in Hong Kong and Macau remained steady at approximately 3.3 million (as of 30 June 2019: approximately 3.3 million). The Group continued to focus on enhancing its customer retention programmes, and was able to maintain a stable monthly postpaid churn rate of 1.1% (1H 2019: 1.1%). Local postpaid net ARPU increased by 5% to HK\$150 as a result of higher contribution from the corporate market.

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\$43 million for the first half of 2020, compared with HK\$82 million for the same period last year. This was mainly due to lower interest income as net cash balance reduced from HK\$9,555 million in the beginning of 2019 to HK\$5,536 million as of 30 June 2020 subsequent to the distribution of HK\$3,855 million special interim dividend and HK\$471 million cash settlement for the acquisition of the 24.1% interest in the mobile business in May 2019.

The Group continues to maintain a healthy financial position with a net cash position of HK\$5,536 million as of 30 June 2020 (31 December 2019: HK\$5,416 million). The improvement in net cash position during the first six months of the year was mainly due to better working capital management.

Capital Expenditure

Capital expenditure on property, plant and equipment, which accounted for 6% (1H 2019: 9%) of the Group's service revenue, reduced by 32% to HK\$105 million. The decrease was mainly due to timing of the 5G capital expenditure and rescheduling of other projects to better align with expected future benefits. The Group continues to be disciplined in scrutinising its projects with care and prudence and ensuring that 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. Other than that, spectrum investment remained unchanged compared with the position as at 31 December 2019.

Summary of spectrum investment

as of 30 June 2020

Spectrum band	Bandwidth	Year of expiry
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Hong Kong

900 MHz	10 MHz	2026
900 MHz	16.6 MHz	2021 ¹
1800 MHz	23.2 MHz	2021 ¹
2100 MHz	29.6 MHz	2031
2300 MHz	30 MHz	2027
2600 MHz	30 MHz ²	2024
2600 MHz	10 MHz ²	2028
3300 MHz	30 MHz	2034
3500 MHz	40 MHz	2035

Spectrum band	Bandwidth	Year of expiry
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Macau

900 MHz	10 MHz	2023
1800 MHz	20 MHz	2023
2100 MHz	10 MHz	2023

¹ 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.

² The spectrum band was shared under 50/50 joint venture - Genius Brand Limited.