

Management Discussion and Analysis

MANAGEMENT REVIEW

Consolidated revenue for the year ended 31st December 2005 remained stable at HK\$1,159 million. The increase in mobile phones and accessories sales was partially offset by the decrease in mobile services revenue.

As at 31st December 2005, SUNDAY's 2G subscribers increased by 54,000, or 8% year-on-year, to 738,000 while average ARPU for post-paid services declined by 6% to HK\$169 as compared to 2004. As a result, mobile services revenue decreased by 4% year-on-year to HK\$993 million. More mobile phones and accessories were sold during the year as more new handset models were launched.

Total cost of sales increased by 22% primarily due to higher usage of free minutes and increased customer acquisition costs during the year. As a result, gross profit declined by 10% to HK\$724 million and to a margin of 62%.

Operating expenses, excluding depreciation and amortisation increased 21% largely due to increases in network costs primarily related to 3G. During the year, SUNDAY continued to roll-out its 3G network by doubling the number of cell sites. The 2G/2.5G network coverage has also been improved by adding approximately 10% more cell sites.

The SUNDAY Group achieved operating efficiency by saving 11% in operating costs year-on-year for its 2G operations although, as expected, 3G operating costs increased in the lead up to the trial service launch in early 2006.

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	For the year ended 31st December	
	2005	2004
	HK\$ million	HK\$ million (Restated)
Operating expenses		
(excluding depreciation and amortisation):		
2G business	428	479
3G business	199	41
SUNDAY Group total	627	520

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Finance costs increased by 60% year-on-year in 2005 primarily due to the increased loan amount drawn down under the long-term facilities provided by Huawei (the “Huawei Facilities”) and the PCCW Group to support the 3G network build up. The finance costs for 2005 also included arrangement fees and early repayment charges in respect of the Huawei Facilities. In July 2005, SUNDAY repaid the outstanding loans under the Huawei Facilities by drawing down inter-company loan facilities arranged with the PCCW Group at normal commercial rates.

The loss attributable to shareholders was HK\$197 million for the year ended 31st December 2005 compared to a profit of HK\$4 million in 2004, mainly due to increases in cost of sales and network costs primarily related to 3G.

The SUNDAY Group has changed certain of its accounting policies following its adoption of the new Hong Kong Financial Reporting Standards, Hong Kong Accounting Standards and Interpretations (collectively referred to as the “new HKFRSs”), which became effective for accounting periods beginning on or after 1st January 2005. Accordingly, certain balance sheet items have been adjusted with no significant impact on the consolidated profit and loss account for the 2005 year. Comparative figures in 2004 have been restated as required. The effects of changes in the accounting policies are summarised in note 2(b) of the consolidated accounts. None of these changes affect the SUNDAY Group’s underlying business operations or cash flows.

CONNECTED TRANSACTIONS

The SUNDAY Group has entered into a variety of transactions with the PCCW Group in relation to various aspects of the SUNDAY Group’s telecommunications business, each constituting a continuing connected transaction of the Company under the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the “Listing Rules”). Details were set out in the two announcements of the Company dated 29th July 2005 and 12th January 2006.

The Company and PCCW are in the process of developing longer-term arrangements between their respective subsidiaries, to supplement or supersede and replace certain of the continuing connected transactions referred to in the aforementioned announcements. Under the requirements of the Listing Rules, certain of these arrangements require approval by the Company’s independent shareholders. The Company will issue further announcements and convene an extraordinary general meeting to approve such arrangements, as and when appropriate.

CAPITAL EXPENDITURE

Capital expenditure for 2005 aggregated HK\$546 million (2004: HK\$301 million) which primarily included HK\$411 million (2004: HK\$247 million) incurred for the 3G network roll-out. Capital expenditure incurred in respect of ongoing enhancements to the 2G/2.5G mobile network and service quality amounted to HK\$135 million (2004: HK\$54 million).

The SUNDAY Group will continue to invest in its 2G and 3G networks to further enhance its coverage and service quality.

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LIQUIDITY AND FINANCIAL RESOURCES

The SUNDAY Group recorded a net cash inflow from operating activities of approximately HK\$32 million for the year ended 31st December 2005, compared with a net cash inflow of HK\$210 million for 2004. The decrease was mainly attributable to lower operating results and higher interest paid during the year.

In the first half of 2005, the capital expenditure and working capital requirements of the SUNDAY Group were mainly funded by the cash flow generated from operating activities and drawdowns on the Huawei Facilities.

In July 2005, the PCCW Group provided financial resources to SUNDAY to repay the loans and to refinance the performance bonds outstanding under the Huawei Facilities. The SUNDAY Group fully repaid the outstanding principal, accrued interest, commitment fees and early repayment charges under the Huawei Facilities aggregating approximately HK\$874 million by drawing down long-term inter-company loan facilities provided by the PCCW Group; and cancelled the whole of the remaining available Huawei Facilities. Since then, the SUNDAY Group has entered into various additional facility agreements with the PCCW Group to finance capital expenditure in relation to the network expansion programmes. These facilities with PCCW were arranged at normal commercial rates.

As at 31st December 2005, the inter-company long-term loans due by the SUNDAY Group to the PCCW Group was HK\$1,204 million with cash reserves of HK\$34 million and a net debt to equity ratio of 2.3 times (2004: 0.7 times). The long-term loans outstanding as at 31st December 2005 will mature in three to five years from the drawdown date.

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FOREIGN EXCHANGE EXPOSURE

Substantially all revenues, expenses, assets and liabilities are denominated in Hong Kong Dollars.

International roaming payables and receivables are netted and settled on a monthly basis under Special Drawing Rights ("SDR") arrangements. As at 31st December 2005, the net SDR-denominated payables were insignificant. The SUNDAY Group has not experienced significant foreign exchange movements and does not anticipate substantial foreign exchange losses as long as the Hong Kong SAR Government's policy to peg the Hong Kong Dollar to the US Dollar remains in effect. The SUNDAY Group will continue monitoring its foreign exchange exposure and market conditions to determine if any hedging is required.

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HUMAN RESOURCES

The SUNDAY Group employed 908 employees as at 31st December 2005 (2004: 831), of which 612 employees were in Hong Kong and 296 employees were in Shenzhen. The SUNDAY Group offers comprehensive remuneration and benefits packages to all employees. Remuneration of employees is maintained at competitive levels, and promotion and salary increments are assessed based on individual and SUNDAY Group performances. Other staff benefits include provident fund schemes, subsidised medical care and subsidies for external educational and training programmes.

No share options were granted or exercised during the year ended 31st December 2005. All outstanding share options granted by the Company under its share option scheme had either been cancelled or had lapsed under the terms of the scheme by 9th August 2005, being one month after the date on which the unconditional mandatory general cash offer made by PCCW Mobile Holding No. 2 Limited, an indirect wholly-owned subsidiary of PCCW, became unconditional. Hence, there were no outstanding share options held by employees as at 31st December 2005.

DIVIDENDS

No interim dividend was paid for the year (2004: Nil) and the Directors do not recommend the payment of a final dividend for the year ended 31st December 2005 (2004: Nil).