Notes to the Financial Statements

December 31, 2003
(Amount expressed in Hong Kong dollars unless otherwise stated)

1 Group Organization

PCCW Limited (the "Company") was incorporated in Hong Kong and its securities have been listed on The Stock Exchange of Hong Kong Limited (the "Stock Exchange") since October 18, 1994. The principal activities of the Company and its subsidiaries (the "Group") are the provision of local and international telecommunications services, Internet and interactive multimedia services, the sale and rental of telecommunications equipment, and the provision of computer, engineering and other technical services, mainly in the Hong Kong Special Administrative Region ("Hong Kong"); investment in, and development of, systems integration and technology-related businesses; and investment in, and development of, infrastructure and properties in Hong Kong and elsewhere in mainland China.

On June 12, 2003, the Company announced that it had been informed that Pacific Century Regional Developments Limited ("PCRD"), a substantial shareholder of the Company, had ceased to account for the Company as a subsidiary and would treat the Company as an associate. Following this development, Pacific Century Group Holdings Limited, which is a company incorporated in the British Virgin Islands and the ultimate holding company of PCRD, is no longer considered as the ultimate holding company of the Company.

2 Basis of Preparation and Principal Accounting Policies

a. Statement of compliance

The financial statements have been prepared in accordance with applicable Statements of Standard Accounting Practice ("SSAP") issued by the Hong Kong Society of Accountants, accounting principles generally accepted in Hong Kong ("HK GAAP") and the disclosure requirements of the Hong Kong Companies Ordinance. In particular, these financial statements reflect the adoption for the first time of SSAP 35 "Accounting for Government grants and disclosure of government assistance" and SSAP 34 (revised) "Employee benefits" which became effective for periods commencing on or after July 1, 2002 and January 1, 2003 respectively. The adoption of these new and revised SSAPs has not had a material financial impact on the preparation of these financial statements.

b. Basis of preparation of the financial statements

The measurement basis used in the preparation of the financial statements is historical cost modified by the revaluation of investment properties and the marking to market of certain investments in securities as explained in the accounting policies set out below.

c. Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and its subsidiaries made up to December 31 each year. Intra-group balances and transactions, and any unrealized profits arising from intra-group transactions, are eliminated in full in preparing the consolidated financial statements.

Unless otherwise indicated, the results of subsidiaries acquired or disposed of during the year are dealt with in the consolidated income statement from the effective dates of acquisition or to the effective dates of disposal, as appropriate.

The gain or loss on the disposal of a subsidiary represents the difference between the proceeds of the sale and the Group's share of its net assets together with any unamortized goodwill or goodwill taken to reserves and which was not previously charged to the consolidated income statement.

The equity and net income attributable to minority shareholders' interests are shown separately in the balance sheet and income statement.

For subsidiaries which have accounting year ends different from the Group, the subsidiaries prepare, for the purpose of consolidation, financial statements as at the same date as the Group.

2 Basis of Preparation and Principal Accounting Policies *(continued)*

d. Revenue recognition

Provided it is probable that the economic benefits will flow to the Group and the revenue and costs, if applicable, can be measured reliably, revenue is recognized in the income statement as follows:

i. **Telecommunications and other services**

Telecommunications services comprise the fixed line telecommunications network services and equipment businesses mainly in Hong Kong.

Telecommunications service revenue based on usage of the Group's network and facilities is recognized when the services are rendered. Telecommunications revenue for services provided for fixed periods is recognized on a straight-line basis over the respective period.

Other service income is recognized when services are rendered to customers.

ii. **Sales of goods**

Revenue is recognized when goods are delivered at the customers' premises which is taken to be the point in time when the customer has accepted the goods and the related risks and rewards of ownership. Revenue is recorded after deduction of any trade discounts.

iii. **Sales of properties**

Revenue and income arising from sales of completed properties is recognized upon completion of the sale when title passes to the purchaser.

Revenue and income arising from the pre-sale of properties under development is recognized on the percentage of construction completion basis when legally binding unconditional sales contracts are signed and exchanged, provided that the construction work has progressed to a stage where the ultimate realization of profit can be reasonably determined and on the basis that the total estimated profit is apportioned over the entire period of construction to reflect the progress of the development.

iv. **Rental income from operating leases**

Rental income receivable from investment properties under operating leases is recognized in the income statement in equal instalments over the accounting periods covered by the lease term, except where an alternative basis is more representative of the pattern of benefits to be derived from the leased asset. Lease incentives granted are recognized in the income statement as an integral part of the aggregate net lease payments receivable. Contingent rentals are recognized as income in the accounting period in which they are earned.

v. **Contract revenue**

Revenue from a fixed price contract is recognized using the percentage of completion method, measured by reference to the percentage of estimated value of work done to date to total contract revenue.

vi. **Interest income**

Interest income from bank deposits is accrued on a time-apportioned basis by reference to the principal outstanding and the rate applicable.

vii. **Commission income**

Commission income is recognized when entitlement to the income is ascertained.

viii. **Dividend income**

Dividend income is recognized when the shareholder's right to receive payment is established.

Notes to the Financial Statements
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2 Basis of Preparation and Principal Accounting Policies *(continued)*

e. Operating leases

Leases of assets under which the lessor has not transferred all the risks and benefits of ownership are classified as operating leases.

i. Assets held for use in operating leases

Where the Group leases out assets under operating leases, the assets are included in the balance sheet according to their nature and, where applicable, are depreciated in accordance with the Group's depreciation policies, as set out in note 2(f). Impairment losses are accounted for in accordance with the accounting policy as set out in note 2(h). Revenue arising from operating leases is recognized in accordance with the Group's revenue recognition policies, as set out in note 2(d)(iv).

ii. Operating lease charges

Where the Group has the use of assets under operating leases, payments made under the leases are charged to the income statement in equal instalments over the accounting periods covered by the lease term. Lease incentives received are recognized in the income statement as an integral part of the aggregate net lease payments made. Contingent rentals are charged to the income statement in the accounting period in which they are incurred.

f. Fixed assets and depreciation

Fixed assets, excluding investment properties, are stated in the balance sheet at cost less accumulated depreciation and impairment losses (see note 2(h)). The cost of an asset comprises its purchase price and any directly attributable costs of bringing the asset to its working condition and location for its intended use. Subsequent expenditure relating to a fixed asset that has already been recognized is added to the carrying amount of the asset and is depreciated over the original remaining useful life of the asset when it is probable that future economic benefits, in excess of the originally assessed standard of performance of the existing asset, will flow to the Group. All other subsequent expenditure, such as repairs and maintenance and overhaul costs, is recognized as an expense in the period in which it is incurred.

Depreciation is calculated to write off the cost on a straight-line basis over their estimated useful lives as follows:

Land and buildings	Over the shorter of the lease term and the estimated useful lives
Exchange equipment	5 to 15 years
Transmission plant	5 to 25 years
Other plant and equipment	Over the shorter of 2 to 16 years and the term of lease

Gains or losses arising from the retirement or disposal of a fixed asset are determined as the difference between the estimated net disposal proceeds and the carrying amount of the asset and are recognized in the income statement on the date of retirement or disposal.

g. Investment properties

Investment properties are interests in land and buildings in respect of which construction work and development have been completed and which are held for their investment potential and for the long term.

Investment properties with an unexpired lease term of more than 20 years are stated in the balance sheet at their open market value, on the basis of an annual valuation by professionally qualified executives of the Group and by independent valuers at intervals of not more than three years. Changes arising on the revaluation of investment properties are generally dealt with in the property revaluation reserve unless the following circumstances arise:

– when a deficit arises on revaluation, it will be charged to the income statement, if and to the extent that it exceeds the amount held in the reserve in respect of the portfolio of investment properties, immediately prior to the revaluation; and

– when a surplus arises on revaluation, it will be credited to the income statement, if and to the extent that a deficit on revaluation in respect of the portfolio of investment properties, had previously been charged to the income statement.

2 Basis of Preparation and Principal Accounting Policies *(continued)*

g. Investment properties *(continued)*

Upon the disposal of an investment property, the relevant portion of the revaluation reserve realized in respect of previous valuations is released from the property revaluation reserve to the income statement as part of the gain or loss on disposal of the investment property.

No depreciation is provided on investment properties unless the unexpired lease term is 20 years or less, in which case depreciation is provided on their carrying value over the unexpired lease term.

h. Impairment of assets

Internal and external sources of information are reviewed at each balance sheet date to identify indications that any of the following assets may be impaired or an impairment loss previously recognized no longer exists or may have decreased:

– fixed assets;

– investments in subsidiaries, associates and jointly controlled companies;

– intangible assets; and

– goodwill (whether taken initially to reserves or recognized as an asset).

If any such indication exists, the asset's recoverable amount is estimated. For intangible assets that are not yet available for use, or are amortized over more than 20 years from the date when the asset is available for use or goodwill that is taken initially to reserves or amortized over more than 20 years from initial recognition, the recoverable amount is estimated at each balance sheet date. An impairment loss is recognized in the income statement whenever the carrying amount of an asset exceeds its recoverable amount.

i. Calculation of recoverable amount

The recoverable amount of an asset is the greater of its net selling price and its value in use. Net selling price is the amount obtainable from the sale of an asset in an arm's length transaction between knowledgeable, willing parties, less the costs of disposal. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. Where an asset does not generate cash inflows largely independent of those from other assets, the recoverable amount is determined for the smallest group of assets that generates cash inflows independently (i.e. a cash-generating unit).

ii. Reversals of impairment losses

In respect of assets other than goodwill, an impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss in respect of goodwill is reversed only if the loss was caused by a specific external event of an exceptional nature that is not expected to recur, and the increase in recoverable amount relates clearly to the reversal of the effect of that specific event.

A reversal of impairment losses is limited to the asset's carrying amount that would have been determined had no impairment loss been recognized in prior years. Reversals of impairment losses are credited to the income statement in the year in which the reversals are recognized.

i. Properties held for development

Properties held for development represent interests in land where construction has not yet commenced. Properties held for development are stated at cost less any provision for impairment in value. Costs include original land acquisition costs, costs of land use rights, and any direct development costs incurred attributable to such properties.

Notes to the Financial Statements
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2 Basis of Preparation and Principal Accounting Policies *(continued)*

j. Properties under development

Properties under development represent interests in land and buildings under construction. Properties under development for long-term purposes are stated at cost less any provision for impairment in value. Properties under development for sale, pre-sales of which have not yet commenced are carried at the lower of cost and the estimated net realizable value. Properties under development for sale for which pre-sales have commenced are stated at cost plus attributable profits less sale deposits, instalments received and receivable and any foreseeable losses.

Cost includes original land acquisition costs, costs of land use rights, construction expenditure incurred and other direct development costs attributable to such properties, including interest incurred on loans directly attributable to the development prior to the completion of construction.

Properties under development for long-term retention, on completion, are transferred to fixed assets or investment properties.

Properties under development for sale with occupancy permits expected to be granted within one year from the balance sheet date, which have either been pre-sold or are intended for sale, are classified under current assets.

k. Goodwill

Goodwill arising on consolidation represents the excess of the cost of the acquisition over the Group's share of the fair value of the identifiable assets and liabilities acquired. In respect of controlled subsidiaries:

– for acquisitions before January 1, 2001, goodwill is eliminated against reserves and is reduced by impairment losses (see note 2(h)); and

– for acquisitions on or after January 1, 2001, goodwill is amortized to the consolidated income statement on a straight-line basis over its estimated useful life ranging from 10 to 20 years. Goodwill is stated in the consolidated balance sheet at cost less any accumulated amortization and any impairment losses (see note 2(h)).

In respect of acquisitions of jointly controlled companies and associates, goodwill is amortized to the consolidated income statement on a straight-line basis over its estimated useful life ranging from 10 to 20 years. The cost of goodwill less any accumulated amortization and any impairment losses (see note 2(h)) is included in the carrying amount of the interest in jointly controlled companies or associates.

On disposal of a controlled subsidiary, a jointly controlled company or an associate during the year, any attributable amount of purchased goodwill not previously amortized or impaired through the consolidated income statement or which has previously been dealt with as a movement on group reserves and which has not been impaired is included in the calculation of the gain or loss on disposal.

l. Intangible assets (other than goodwill)

Intangible assets that are acquired by the Group are stated in the balance sheet at cost less accumulated amortization and impairment losses (see note 2(h)). Expenditure on internally generated goodwill and brands is recognized as an expense in the period in which it is incurred.

Subsequent expenditure on an intangible asset after its purchase or its completion is recognized as an expense when it is incurred unless it is probable that this expenditure will enable the asset to generate future economic benefits in excess of its originally assessed standard of performance and this expenditure can be measured and attributed to the asset reliably. If these conditions are met, the subsequent expenditure is added to the cost of the intangible assets.

Amortization of intangible assets is charged to the income statement on a straight-line basis over the assets' estimated useful lives as follows:

Trademarks	20 years
Content licence	10 years
Wireless broadband licence	Over the term of licence

2 Basis of Preparation and Principal Accounting Policies *(continued)*

m. Subsidiaries

A subsidiary is a company in which the Company, directly or indirectly, holds more than half of the issued share capital, or controls more than half the voting power, or controls the composition of the board of directors. Subsidiaries are considered to be controlled if the Company has the power, directly or indirectly, to govern its financial and operating policies, so as to obtain benefits from their activities.

In the Company's balance sheet, investments in subsidiaries are stated at cost less any impairment losses (see note 2(h)). The results of subsidiaries are recognized by the Company to the extent of dividends received and receivable at the balance sheet date.

n. Associates

An associate is an entity in which the Group or the Company has significant influence, but not control or joint control, over its management, including participating in the financial and operating policy decisions.

In the consolidated financial statements, investments in associates are accounted for under the equity method and are initially recorded at cost and adjusted thereafter for the post-acquisition change in the Group's share of the associates' net assets. The consolidated income statement reflects the Group's share of post-acquisition results of the associates for the year, including any amortization of goodwill charged during the year in accordance with note 2(k).

In the Company's balance sheet, investments in associates are stated at cost less any impairment losses (see note 2(h)), on an individual entity basis. The results of associates are recognized by the Company to the extent of dividends received and receivable at the balance sheet date.

o. Joint ventures and jointly controlled companies

A jointly controlled company or a joint venture is an entity which operates under a contractual arrangement between the Group or the Company and other parties, where the contractual arrangement establishes that the Group or the Company and one or more of the other parties share joint control over the economic activity of the entity. The Group has made investments in joint ventures in the People's Republic of China (the "PRC") in respect of which the partners' profit-sharing ratios during the joint venture period and share of net assets upon the expiration of the joint venture period may not be in proportion to their equity ratios, but are as defined in the respective joint venture contracts.

Investments made by means of joint venture structures where the Group or the Company controls the composition of the board of directors or equivalent governing body and/or is in a position to exercise control over the financial and operating policies of the joint ventures are accounted for as subsidiaries.

Investments in jointly controlled companies or joint ventures are accounted for under the equity method, as described in note 2(n) above, in the Group's consolidated financial statements.

The Company's interests in joint ventures and jointly controlled companies are stated at cost in the Company's balance sheet less any impairment losses (see note 2(h)), on an individual entity basis. The results of joint ventures and jointly controlled companies are recognized by the Company to the extent of dividends received and receivable at the balance sheet date.

Notes to the Financial Statements
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2 Basis of Preparation and Principal Accounting Policies *(continued)*

p. Investments in securities

The Group's policy for investments in securities other than investments in subsidiaries, associates, joint ventures and jointly controlled companies is as follows:

i. Held-to-maturity securities are investments which the Group has the ability and intention to hold to maturity. Held-to-maturity securities are stated in the balance sheet at amortized cost less any provisions for diminution in value. Any discount or premium is amortized over the period to maturity and is included in the income statement.

   The carrying amounts of held-to-maturity securities are reviewed at the balance sheet date in order to assess the credit risk and whether the carrying amounts are expected to be fully recovered. Provisions are made when the carrying amounts are not expected to be fully recovered and are recognized as an expense in the income statement, such provisions being determined for each investment individually.

ii. Investments, which include both debt and equity securities, held on a continuing basis for an identified long-term purpose are classified as investment securities. Investment securities are stated in the balance sheet at cost less any provisions for diminution in value.

   The carrying amounts of investment securities are reviewed at the balance sheet date in order to assess whether fair values have declined below the carrying amounts. Provisions are made when the fair values have declined below the carrying amounts, unless there is evidence that the decline is temporary, and are recognized as an expense in the income statement, such provisions being determined for each investment individually.

iii. Provisions against the carrying values of held-to-maturity securities and investment securities are written back when the circumstances and events that led to the write-down or write-off cease to exist and there is persuasive evidence that the new circumstances and events will persist for the foreseeable future.

iv. Investments other than held-to-maturity securities and investment securities are classified as other investments and are stated in the balance sheet at fair value. Any unrealized holding gains or losses on other investments arising from the changes in fair value are recognized in the income statement as they arise.

v. The transfer of investments between categories is accounted for at fair value. For an investment transferred into the other investment category, the unrealized holding gain or loss at the date of transfer is recognized in the income statement immediately. Previously recognized unrealized holding gains or losses on investments transferred from other investment category are not reversed.

vi. Profits or losses on disposal of investments in securities are determined as the difference between the estimated net disposal proceeds and the carrying amount of the investments and are accounted for in the income statement as they arise.

q. Properties held for sale

Properties held for sale are stated at the lower of cost and the estimated net realizable value. Cost includes development and construction expenditure incurred, interest incurred during the construction period and other direct costs attributable to such properties. Net realizable value is estimated by the directors based on prevailing market prices, on an individual property basis, less any further costs expected to be incurred in selling the property.

r. Inventories

Inventories consist of trading inventories, work in progress and consumable inventories.

Trading inventories are carried at the lower of cost and net realizable value. Net realizable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

Work-in-progress is stated at cost, which comprises labor, materials and overheads where appropriate.

2 Basis of Preparation and Principal Accounting Policies *(continued)*

r. Inventories *(continued)*

Consumable inventories, held for use in the maintenance and expansion of the Group's telecommunications systems, are stated at cost less provision for deterioration and obsolescence.

Cost is calculated using the weighted average cost formula and comprises all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition.

s. Construction contracts

The accounting policy for contract revenues is set out in note 2(d)(v) above. When the outcome of a construction contract can be estimated reliably, contract costs are recognized as expenses by reference to the stage of completion of the contract activity at the balance sheet date. When it is probable that total contract costs will exceed total contract revenue, the expected loss is recognized as an expense immediately. When the outcome of a construction contract cannot be estimated reliably, revenue is recognized only to the extent that it is probable that the contract costs incurred will be recoverable and contract costs are recognized as an expense in the period in which they are incurred.

Construction contracts in progress at the balance sheet date are recorded in the balance sheet at the net amount of costs incurred plus recognized profits less recognized losses and estimated value of work performed, and are presented in the balance sheet as the "Gross amounts due from customers for contract work" (as an asset) or the "Gross amounts due to customers for contract work" (as a liability), as applicable. Progress billings for work performed on a contract not yet paid by customers are included in the balance sheet under "Accounts receivable".

t. Cash equivalents

Cash and cash equivalents comprise cash at bank and on hand, demand deposits with banks and other financial institutions, and short-term, highly liquid investments that are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value, having been within three months of maturity at acquisition, less bank overdrafts that are repayable on demand and form an integral part of the Group's cash management, and also advances from banks repayable within three months from the dates of advances.

u. Provisions and contingent liabilities

Provisions are recognized for liabilities of uncertain timing or amount when the Company or Group has a present obligation (legal or constructive) as a result of a past event, it is probable (i.e. more likely than not) that an outflow of economic benefits will be required to settle the obligation and a reliable estimate can be made. Provisions are reviewed at each balance sheet date and adjusted to reflect the current best estimate of amount required. Where the time value of money is material, provisions are stated at the present value of the expenditures expected to settle the obligation.

Where it is not probable that an outflow of economic benefits will be required, or the amount cannot be estimated reliably, the obligation is disclosed as a contingent liability, unless the probability of outflow of economic benefits is remote. Possible obligations, whose existence will only be confirmed by the occurrence or non-occurrence of one or more future events are also disclosed as contingent liabilities unless the probability of outflow of economic benefits is remote.

v. Borrowing costs

Borrowing costs are expensed in the income statement in the period in which they are incurred, except to the extent that they are capitalized as being directly attributable to the acquisition, construction or production of an asset which necessarily takes a substantial period of time to get ready for its intended use or sale.

The capitalization of borrowing costs as part of the cost of a qualifying asset commences when expenditures for the asset are being incurred, borrowing costs are being incurred and activities that are necessary to prepare the asset for its intended use or sale are in progress. Capitalization of borrowing costs is suspended or ceases when substantially all the activities necessary to prepare the qualifying asset for its intended use or sale are interrupted or complete.

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2 Basis of Preparation and Principal Accounting Policies *(continued)*

v. Borrowing costs *(continued)*

Discounts or premiums relating to borrowings, ancillary costs incurred in connection with arranging borrowings and exchange differences arising from foreign currency borrowings, to the extent that they are regarded as adjustments to interest costs, are recognized as expenses over the period of the borrowing.

w. Income tax

i. Income tax for the year comprises current and deferred tax. Income tax is recognized in the income statement except to the extent that it relates to items recognized directly in equity, in which case it is recognized in equity.

ii. Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the balance sheet date, and any adjustment to tax payable in respect of previous year.

iii. Deferred tax assets and liabilities arise from deductible and taxable temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the tax bases respectively. Deferred tax assets also arise from unused tax losses and unused tax credits.

All deferred tax liabilities, and all deferred tax assets to the extent that it is probable that future taxable profits will be available against which the asset can be utilized, are recognized.

The amount of deferred tax provided is based on the expected manner of realization or settlement of the carrying amount of the assets and liabilities, using tax rates enacted or substantively enacted at the balance sheet date. Deferred tax assets and liabilities are not discounted.

x. Employee benefits

i. Salaries, annual bonuses, annual leave entitlements, leave passage and the cost to the Group of non-monetary benefits are accrued in the year in which the associated services are rendered by employees of the Group. Where payment or settlement is deferred and the effect would be material, provisions are made for the estimated liability as a result of services rendered by employees up to the balance sheet date.

ii. The Group operates both defined benefit and defined contribution retirement schemes (including the Mandatory Provident Fund) for its employees, the assets of which are generally held in separate trustee – administered funds. The schemes are generally funded by payments from the relevant Group companies and, in some cases, employees themselves, taking account of the recommendations of independent qualified actuaries.

The Group's contributions to the defined contribution schemes are recognized as an expense in the income statement in the period to which the contributions relate.

Retirement costs under defined benefit retirement schemes are assessed using the projected unit credit method. Under this method, the cost of providing defined benefits is charged to the income statement so as to spread the regular cost over the service lives of employees in accordance with the advice of the actuaries who carry out a full valuation of the schemes on an annual basis. The defined benefit obligation is measured as the present value of the estimated future cash outflows using interest rates determined by reference to market yields at the balance sheet date based on Exchange Fund Notes, which have terms to maturity approximating the terms of the related liability. Scheme assets are measured at fair value. Actuarial gains and losses, to the extent that the amount is in excess of 10 percent of the greater of the present value of the defined benefit obligations and the fair value of the scheme assets, are recognized in the income statement over the expected average remaining service lives of the participating employees. Past service costs are recognized as an expense on a straight-line basis over the average period until the benefits become vested.

2 Basis of Preparation and Principal Accounting Policies *(continued)*

x. Employee benefits *(continued)*

In prior years, long service payments under the Hong Kong Employment Ordinance were accounted for as "other long-term employee benefits" that expenses were recognized when payments were made to the employees. In May 2003, paragraph 162 of SSAP 34 was revised that long service payments are accounted for as post employment benefits with effect from January 1, 2003. The adoption of the revised SSAP 34 in 2003 does not have a significant effect on the Group's financial statements as at January 1, 2003 and December 31, 2003. Accordingly, comparative financial statements have not been restated.

iii. The Group grants employees shares of the Company under its share award schemes at nil consideration. The cost of shares is recognized in the balance sheet as prepaid expenses at the date of grant and amortized over the respective vesting period and recognized in the income statement as staff costs.

The Group also operates share option schemes where directors or employees are granted options to acquire shares of the Company at specified exercise prices. No compensation costs are recognized in the income statement in respect of such options.

iv. Employee termination benefits are recognized only after either an agreement is in place with the appropriate employee representatives specifying the terms of redundancy and the numbers of employees affected, or, after individual employees have been advised of the specific terms.

y. Foreign currencies

Companies comprising the Group maintain their books and records in the primary currencies of their operations (the "respective reporting currencies").

In the financial statements of individual companies, transactions in other currencies during the year are translated into the respective reporting currencies at the exchange rates ruling at the transaction dates. Monetary assets and liabilities denominated in other currencies are translated into the respective reporting currencies at the exchange rates ruling at the balance sheet date. Exchange gains and losses are dealt with in the income statement.

For the purpose of preparing consolidated financial statements, the financial statements of the individual companies with reporting currencies other than Hong Kong dollars are translated into Hong Kong dollars using the net investment method. Under this method, assets and liabilities of these individual companies are translated into Hong Kong dollars at the rates of exchange ruling at the balance sheet date. Income and expenses are translated at the average exchange rates for the year. Share capital and other reserves are translated into Hong Kong dollars at historical rates. Exchange differences arising on translation are dealt with as movements in reserves.

z. Off balance sheet financial instruments and derivatives

Gains and losses on the revaluation and maturity of spot and forward foreign exchange contracts used for hedging purposes are recorded in the income statement and are offset against gains and losses arising from the foreign exchange transactions and revaluation of foreign currency denominated assets and liabilities which these contracts are hedging. Forward contracts undertaken for trading purposes are marked to market and the gain or loss arising is recognized in the income statement.

Interest rate swaps, forward interest rate agreements and interest rate options are used to manage exposure to interest rate fluctuations. The notional amounts are recorded off balance sheet. Interest flows are accounted for on an accrual basis. Interest income or expense arising from the interest rate swap contracts are netted off against the related interest income or expense applicable to the on-balance sheet items, which these financial instruments are hedging.

The notional amounts of equity and currency options are not reflected in the balance sheet.

Premiums received or paid on the respective written or purchased equity and currency options are amortized over the terms of these options (see note 36(a)). Premiums received or paid or unamortized balance of premium received or paid resulting from early termination of the financial instruments and derivatives are recognized in the income statement in the year of termination.

Notes to the Financial Statements
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2 Basis of Preparation and Principal Accounting Policies *(continued)*

aa. Management estimates

The presentation of financial statements in accordance with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts and disclosures reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

bb. Segment reporting

A segment is a distinguishable component of the Group that is engaged either in providing particular products or services (business segment), or in providing products or services within a particular economic environment (geographical segment), and which is subject to risks and rewards that are different from those of other segments.

In accordance with the Group's internal financial reporting, the Group has chosen business segment information as the primary reporting format and geographical segment information as the secondary reporting format for the purposes of these financial statements.

Segment revenues, expenses, results, assets and liabilities include items directly attributable to a segment as well as those that can be allocated on a reasonable basis to that segment. Segment revenues, segment expenses and segment performance include transactions between segments. Inter-segment pricing is based on similar terms as those available to unaffiliated customers for similar services. These transactions are eliminated upon consolidation.

Segment capital expenditure is the total cost incurred during the year to acquire segment assets (both tangible and intangible) that are expected to be used for more than one period.

Unallocated items mainly comprise financial and corporate assets and liabilities, interest-bearing loans, borrowings, corporate and financing expenses and minority interests.

3 Related Party Transactions

For the purposes of these financial statements, parties are considered to be related to the Group if the Group has the ability, directly or indirectly, to control the party or exercise significant influence over the party in making financial and operating decisions, or vice versa, or where the Group and the party are subject to common control or common significant influence. Related parties may be individuals or other entities.

a. During the year, the Group had the following significant transactions with related companies:

In HK$ million	The Group 2003	2002
Convertible bond interest payable to a substantial shareholder	**293**	293
Capital injection to a jointly controlled company	**117**	117
Telecommunication service fees, rental charges and subcontracting charges receivable from:		
– an associate	**–**	594
– a jointly controlled company	**221**	254
System integration charges receivable from a shareholder of a PRC subsidiary	**59**	–
Telecommunications service fees and rental charges payable to:		
– an associate	**–**	162
– a jointly controlled company	**1,086**	1,474

The above transactions were carried out after negotiations between the Group and the related parties in the ordinary course of business and on the basis of estimated market value as determined by the directors. In respect of transactions for which the price or volume has not yet been agreed with the relevant related parties, the directors have determined the relevant amounts based on their best estimation.

b. Advances from customers include an amount of HK$24 million (2002: HK$107 million) which represents prepaid advertising fees received and receivable from investee companies for advertising space on the broadband Internet and television network operated by the Group.

3 Related Party Transactions *(continued)*

c. An indirect wholly-owned subsidiary of the Company and a jointly controlled company ("JV") have entered into a Hong Kong Domestic Connectivity Agreement and an International Services Agreement for the provision of domestic and international connectivity services in Hong Kong and between Hong Kong and other countries. Pursuant to the International Services Agreement, for the first five years of operations subsequent to the formation of the JV, the Group is required to acquire 90 percent, 90 percent, 80 percent, 70 percent and 60 percent per annum, respectively, of its total annual purchases of "Committed Services" (being international public switched telephone network terminating access, international transmission capacity and Internet gateway access services) from the JV. The Hong Kong Domestic Connectivity Agreement contemplates a reciprocal arrangement, whereby the Group will provide local connectivity services in Hong Kong to the JV under similar terms and conditions. These agreements were subsequently amended on January 30, 2001 and further amended on April 15, 2003 such that each of the Group and Telstra Corporation Limited ("Telstra") have agreed to purchase 90 percent per annum of the Group's and Telstra's respective Committed Services from the JV and its subsidiaries until repayment of the amended US$1,200 million (approximately HK$9,360 million) syndicated term loan facility of the JV on December 31, 2010 or earlier at rates benchmarked at least annually to prevailing market prices. The JV similarly must acquire 90 percent per annum of its local connectivity services from the Group under the amended agreement for domestic connectivity services, similarly extended for the same period.

In addition, the Group entered into one-year fixed price bulk purchase arrangements for international connectivity services from January 1, 2002 to December 31, 2002, which committed the Group to aggregate purchase levels in 2002. The Group's commitments under these arrangements had regard to its future capacity needs and opportunities for growth as well as the JV's minimum earnings requirements under its financing arrangements. Regulated services in Hong Kong were acquired in accordance with tariffs approved by the relevant regulatory authority and unregulated services were acquired in accordance with market prices. The agreement expired on December 31, 2002.

On April 15, 2003, the Company, the indirect wholly-owned subsidiary of the Company, and Telstra entered into a capacity prepayment agreement with the JV and certain of its subsidiaries whereby each of the Company and Telstra agreed to make a prepayment of US$143 million (approximately HK$1,115 million) for the purchase of capacity as stated above. These prepayments (which will be compounded to reflect the time value of money) are to be applied against the cost of services and capacity supplied to Telstra and the Group by the JV and certain of its subsidiaries as and when the JV and certain of its subsidiaries have available surplus cash in accordance with a prescribed formula. The total balance of HK$1,139 million (2002: Nil), comprising the prepayment of HK$1,115 million and the accrued interest receivable of HK$24 million as at December 31, 2003, has been included in "Loan due from a jointly controlled company" in the balance sheet of the Company and subsequently written down to zero (see note 23).

Purchases made by the Group from the JV for the year ended December 31, 2003 were HK$1,036 million (2002: HK$1,443 million).

d. Other than as specified in this note and note 24, balances with related parties are unsecured, non-interest bearing and have no fixed repayment terms.

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4 Turnover

In HK$ million	The Group 2003	2002
Telecommunications and other service revenues	**16,535**	18,227
Amounts received and receivable in respect of goods sold	**1,626**	1,470
Amounts received and receivable in respect of properties sold	**4,111**	20
Amounts received and receivable from the rental of investment properties	**276**	332
Revenues from construction contracts	**2**	63
	22,550	20,112

5 Segment Information

Segment information is presented in respect of the Group's business and geographical segments. Business segment information is chosen as the primary reporting format because this is consistent with the Group's internal financial reporting.

a. Business segments

The Group comprises the following main business segments:

Telecommunications Services ("TSS") is the leading provider of telecommunications services, Internet access and multimedia services and related equipment in Hong Kong.

Business eSolutions offers IT solutions, business broadband Internet access, hosting and facilities management services and directories businesses within Hong Kong, Taiwan and mainland China.

Infrastructure and Property ("Infrastructure") covers the Group's property portfolio in Hong Kong and mainland China including the Cyberport development in Hong Kong.

Others include the Group's other businesses in mainland China, JALECO LTD. ("JALECO"), Internet Services and CyberWorks Ventures.

5 Segment Information *(continued)*

a. Business segments *(continued)*

In HK$ million	TSS		Business eSolutions		Infrastructure		Others		Eliminations		Consolidated	
	2003	2002	**2003**	2002	**2003**	2002	**2003**	2002	**2003**	2002	**2003**	2002
REVENUE												
External revenue	**15,865**	17,248	**1,762**	1,661	**4,497**	503	**426**	700	**–**	–	**22,550**	20,112
Inter-segment revenue	**707**	759	**564**	573	**103**	182	**–**	93	**(1,374)**	(1,607)	**–**	–
Total revenue	**16,572**	18,007	**2,326**	2,234	**4,600**	685	**426**	793	**(1,374)**	(1,607)	**22,550**	20,112
RESULT												
Segment results	**5,156**	6,348	**(148)**	(102)	**102**	267	**(2,317)**	(1,930)	**–**	–	**2,793**	4,583
Unallocated corporate expenses											**(537)**	(203)
Profit from operations											**2,256**	4,380
Finance costs, net											**(2,117)**	(1,997)
Share of results of jointly controlled companies and associates	**(750)**	1,060	**(49)**	(34)	**(1)**	1	**(26)**	(196)	**–**	–	**(826)**	831
Impairment losses on interests in jointly controlled companies and associates	**(4,170)**	(8,263)	**–**	–	**–**	–	**(294)**	–	**–**	–	**(4,464)**	(8,263)
Losses on disposal of interests in RWC and MobileOne, net	**–**	(1,433)	**–**	–	**–**	–	**–**	–	**–**	–	**–**	(1,433)
Loss before taxation											**(5,151)**	(6,482)
Taxation											**(1,165)**	(1,406)
Loss after taxation											**(6,316)**	(7,888)
Minority interests											**216**	126
Loss for the year attributable to shareholders											**(6,100)**	(7,762)

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5 Segment Information *(continued)*

a. Business segments *(continued)*

In HK$ million	TSS 2003	TSS 2002	Business eSolutions 2003	Business eSolutions 2002	Infrastructure 2003	Infrastructure 2002	Others 2003	Others 2002	Eliminations 2003	Eliminations 2002	Consolidated 2003	Consolidated 2002
OTHER INFORMATION												
Capital expenditure (including fixed assets, intangible assets and goodwill) incurred during the year	**1,746**	1,353	**190**	117	**13**	19	**165**	718				
Depreciation and amortization	**2,228**	2,183	**136**	95	**151**	206	**176**	255				
Impairment losses recognized in income statement	**5,190**	8,263	**71**	147	**–**	–	**1,643**	387				
Significant non-cash expenses (excluding depreciation, amortization and impairment losses)	**82**	108	**8**	16	**9**	10	**328**	742				
ASSETS												
Segment assets	**17,685**	20,122	**1,495**	1,474	**16,474**	10,662	**1,569**	3,082	**–**	–	**37,223**	35,340
Interests in jointly controlled companies and associates	**487**	4,443	**20**	110	**1**	1	**13**	78	**–**	–	**521**	4,632
Unallocated corporate assets											**6,903**	9,791
Consolidated total assets											**44,647**	49,763
LIABILITIES												
Segment liabilities	**4,527**	5,593	**746**	734	**5,146**	977	**672**	736	**–**	–	**11,091**	8,040
Unallocated corporate liabilities											**41,092**	47,231
Consolidated total liabilities											**52,183**	55,271

b. Geographical segments

The Group's businesses are managed on a worldwide basis, but operate in three principal economic environments. In presenting information on the basis of geographical segments, segment revenue is based on the geographical location of customers. Segment assets and capital expenditure are based on the geographical location of the assets.

In HK$ million	Revenue from external customers 2003	Revenue from external customers 2002	Segment assets 2003	Segment assets 2002	Capital expenditure incurred during the year 2003	Capital expenditure incurred during the year 2002
Hong Kong	**21,172**	19,063	**31,611**	29,000	**1,894**	1,550
Mainland China (excluding Hong Kong) and Taiwan	**948**	701	**5,011**	4,708	**115**	62
Others	**430**	348	**601**	1,632	**150**	616
	22,550	20,112	**37,223**	35,340	**2,159**	2,228

6 Operating Profit before Net Gains on Investments, Provisions for Impairment Losses and Restructuring Costs

In HK$ million	The Group 2003	2002
Turnover	**22,550**	20,112
Cost of sales	**(8,730)**	(5,295)
General and administrative expenses	**(9,481)**	(9,605)
Operating profit before net gains on investments, provisions for impairment losses and restructuring costs	**4,339**	5,212

7 Gains on Investments, Net

In HK$ million	The Group 2003	2002
Net unrealized holding gains/(losses) on other investments	**8**	(142)
Net realized gains/(losses) from disposals of investments in jointly controlled companies and associates, investment securities and other investments	**103**	(92)
Provision for impairment of investments	**(258)**	(581)
Amortization of premium received from equity options	**12**	32
Release of provision for an onerous contract	**–**	464
Gain on termination and amendment of the terms of cross currency swap contracts (note 36(c))	**532**	332
Dividend income	**10**	–
	407	13

8 Provisions for Impairment Losses

In HK$ million	The Group 2003	2002
Provisions for impairment of:		
Fixed assets (note a)	**1,167**	204
Multimedia business related assets (note b)	**301**	309
Game business related assets (note c)	**893**	–
Other non-current assets	**91**	21
	2,452	534

a. Due to technology and market changes in the sectors in which the Group operates, certain of the Group's fixed assets have become obsolete or impaired. Accordingly, the Group has recognized an impairment loss of approximately HK$1,155 million in the income statement for the year ended December 31, 2003. Further, an impairment loss of approximately HK$12 million on the fixed assets of the game business has been recognized as described in note (c) below.

b. Following the launch of certain new value-added services in 2003, the Group has reviewed the recoverable amount of its multimedia business related assets and identified that the usage of certain content archive will be diminishing. The income to be generated from such assets is expected to be insignificant. Accordingly, the Group has fully written down the remaining carrying value of a content licence as at December 31, 2003 to zero and recognized an impairment loss of approximately HK$301 million.

c. During the year, JALECO, a subsidiary incorporated under the laws of Japan with shares registered on the Over the Counter market in Japan, has restructured its on-line game and game development businesses and exited certain legacy businesses. In view of the continual losses incurred by JALECO, management has performed an assessment of the fair value of its interest in JALECO, including the related goodwill that had previously been eliminated against reserves, as at December 31, 2003. As a result, based on the estimated value in use of JALECO determined using a discount rate of 12.5 percent (2002: 12.5 percent), the Group has recognized impairment losses for goodwill and other assets of HK$742 million and HK$151 million respectively in the income statement for the year.

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9 Restructuring Costs

During the current year, JALECO incurred restructuring costs of approximately HK$38 million representing mainly the severance payments and the write-off of development cost and inventory in relation to the restructuring exercise described in note 8(c) above.

During 2002, the Group subcontracted a significant portion of its network maintenance function to 17 newly-established subcontracting companies owned by individuals previously employed by the Group. Approximately 1,600 former employees joined these subcontracting companies in November 2002 and approximately 3,000 of the Group's employees joined a new wholly-owned subsidiary, Cascade Limited ("Cascade"), on January 1, 2003. In addition, the Group reset staff levels in 2002 involving approximately 1,400 employees. Restructuring costs of approximately HK$311 million in 2002 mainly represent the ex-gratia payments, curtailment losses on the related defined benefit retirement schemes, Cascade incentive bonuses on employment transfers and payments in lieu of notice for the above exercises.

10 Loss Before Taxation

Loss before taxation is stated after crediting and charging the following:

In HK$ million	The Group **2003**	2002
Crediting:		
Dividend income from		
– Listed other investments	**2**	–
– Unlisted investment securities	**8**	–
Realized gains on disposal of investments in jointly controlled companies and associates included in gains on investments, net	**8**	34
Realized gains on disposal of investment securities included in gains on investments, net	**87**	56
Realized gains on disposal of other investments included in gains on investments, net	**8**	–
Exchange gains, net	**7**	9
Gross rental income	**276**	332
Less: outgoings	**(21)**	(11)
Charging:		
Realized losses on disposal of other investments included in gains on investments, net	**–**	182
Provision for impairment of goodwill attributable to REACH	**315**	8,263
Provision for impairment of goodwill attributable to subsidiaries	**742**	309
Provision for impairment of goodwill attributable to another jointly controlled company	**122**	–
Provision for impairment of fixed assets	**1,167**	232
Provision for impairment of intangible assets	**351**	–
Write-off of intangible assets	**–**	8
Provision for inventory obsolescence	**70**	26
Depreciation	**2,674**	2,623
Amortization of intangible assets	**132**	112
Amortization of goodwill	**82**	85
Staff costs (excluding directors' emoluments (note 14) and retirement costs for other staff)	**2,813**	3,395
Retirement costs for other staff		
– contributions to defined contribution retirement scheme	**112**	47
– pension expense for defined benefit retirement schemes (note 30(a)(iii))	**103**	197
– curtailment loss for defined benefit retirement schemes included in restructuring costs (note 30(a)(iii))	**–**	108
Cost of inventories	**1,528**	1,431
Cost of properties sold	**3,951**	9
Loss on disposal of fixed assets	**145**	76
Auditors' remuneration		
– current year	**12**	10
– underprovision in previous year	**–**	2
Operating lease rental		
– land and buildings	**223**	261
– equipment	**99**	145

11 Finance Costs, Net

In HK$ million	The Group 2003	2002
Interest paid/payable for:		
Overdrafts and bank loans wholly repayable within 5 years	**501**	10
Bank loans not wholly repayable within 5 years	**4**	842
Other loans wholly repayable within 5 years	**908**	811
Other loans not wholly repayable within 5 years	**853**	531
	2,266	2,194
Interest capitalized in fixed assets	**(17)**	(33)
Finance costs	**2,249**	2,161
Interest income on bank deposits	**(132)**	(164)
Finance costs, net	**2,117**	1,997

Finance costs of HK$2,249 million (2002: HK$2,161 million) include arrangement fees expensed of approximately HK$217 million (2002: HK$241 million) incurred in respect of the bank loans and other long-term borrowings of the Group.

During the year, the capitalization rates used to determine the amount of interest eligible for capitalization ranged from 2.7 percent to 4.9 percent (2002: 3.0 percent to 3.5 percent).

12 Impairment Losses on Interests in Jointly Controlled Companies and Associates

In HK$ million	The Group 2003	2002
Impairment losses on interests in:		
REACH (note a)	**4,159**	8,263
Another jointly controlled company (note b)	**227**	–
Other associates	**78**	–
	4,464	8,263

a. On April 15, 2003, REACH and its bankers amended the terms of REACH's US$1,500 million syndicated term loan facility, which was subsequently reduced to US$1,200 million, with effect from April 25, 2003. The amendments to the term loan facility were intended to provide REACH with greater financial flexibility and an improved capital structure. REACH continues to operate in a difficult environment and the industry is expected to remain challenging for a period of time due to aggressive pricing and over supply of capacity.

The Group has performed an assessment of the fair value of its interest in REACH, including the related goodwill that had previously been eliminated against reserves, as at December 31, 2003. As a result, based on the estimated value in use of REACH determined using a discount rate of 10 percent (2002: 9 percent), the Group has made full provision for impairment of its previously unimpaired interest in REACH, recognizing an impairment loss of approximately HK$4,159 million (2002: HK$8,263 million) in the income statement for the year ended December 31, 2003. Accordingly, the Group's total interest in REACH has been written down to zero as at December 31, 2003 (2002: HK$3,930 million).

b. Due to continual losses sustained, the Group has performed an assessment of the carrying value of its interest in a jointly controlled company, which is engaged in the on-line game business, as at December 31, 2003. Based on the result of the assessment, the Group has made a full provision for impairment of its interest in this jointly controlled company of approximately HK$227 million in the income statement for the year ended December 31, 2003.

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13 Losses on Disposal of Interests in Joint Venture (Bermuda) No. 2 Limited ("RWC") and MobileOne Ltd ("MobileOne"), Net

In HK$ million	The Group 2002
Loss on disposal of interest in RWC (note a)	(1,771)
Profit on disposal of partial interest in MobileOne (note b)	338
	(1,433)

a. Loss on disposal of interest in RWC

On June 28, 2002, the Company and Telstra entered into, and completed, an agreement relating to the following:

i. the sale by the Company of its entire 40 percent equity interest in RWC to Telstra for a consideration of approximately US$614 million (approximately HK$4,792 million);

ii. the redemption by the Company of the outstanding principal amount of the US$750 million (approximately HK$5,850 million) variable coupon subordinated convertible bond due 2007 ("Telstra Bond due 2007") together with accrued interest of approximately US$54.38 million (approximately HK$424 million); and

iii. the issue by the Company of a US$190 million (approximately HK$1,482 million) 5 percent mandatory convertible note due 2005 ("Telstra Note due 2005") to Telstra.

A summary of the loss on disposal of interest in RWC is set out below:

In HK$ million	The Group 2002
Telstra Bond due 2007	5,850
Accrued interest on Telstra Bond due 2007	424
Less: Fair value of Telstra Note due 2005	(1,482)
Proceeds on disposal of interest in RWC	4,792
Less: Book carrying value of interest in RWC as at June 28, 2002	(2,482)
Surplus of proceeds on disposal of interest in RWC over its book carrying value	2,310
Less: Realization of related goodwill previously charged against reserves	(4,081)
Loss on disposal of interest in RWC	(1,771)

13 Losses on Disposal of Interests in Joint Venture (Bermuda) No. 2 Limited ("RWC") and MobileOne Ltd ("MobileOne"), Net *(continued)*

b. Profit on disposal of partial interest in MobileOne

In December 2002, MobileOne was listed on the Singapore Exchange Securities Trading Limited through the sale of existing shares. This resulted in a disposal of an equivalent of 8.4 percent stake in MobileOne by the Group. The consideration, net of transaction costs, for the disposal was approximately HK$497 million, which generated a profit of approximately HK$338 million. Following completion of the disposal, the Group's effective interest in MobileOne was reduced from 14.7 percent to 6.3 percent as at December 31, 2002. As at December 31, 2003, the Group's effective interest in MobileOne was 5.9 percent.

A summary of the profit on disposal of partial interest in MobileOne is set out below:

In HK$ million	The Group 2002
Proceeds on disposal of partial interest in MobileOne, net of transaction costs	497
Less: Share of the book carrying value of partial interest in MobileOne	(159)
Profit on disposal of partial interest in MobileOne	338

14 Directors' and Senior Executives' Emoluments

Details of directors' emoluments are set out below:

In HK$ million	The Group 2003	2002
Non-executive directors		
Fees	**4**	3
Executive directors		
Fees	**–**	–
Salaries, allowances and other allowances and benefits in kind	**62**	46
Pension scheme contributions	**4**	4
Bonuses paid and payable	**50**	38
Payments as compensation for loss of office	**–**	22
Further payment as compensation for loss of office to a past director	**2**	–
Payment to a director as inducement to join the Company	**–**	8
	118	118
Total	**122**	121

Pursuant to an agreement made between the Chairman and a director in 2002, 387,600 shares of the Company were transferred by the Chairman personally to that director in April 2003, being first of the three annual installments of a total of 1,162,800 shares the Chairman agreed to transfer to that director. No new shares were issued by the Company and the Company did not bear any portion of the cost of the shares transferred by the Chairman.

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14 Directors' and Senior Executives' Emoluments *(continued)*

The emoluments of the directors analyzed by the number of directors and emolument ranges are as follows:

	Number of directors The Group	
	2003	2002
Up to HK$1,000,000	**5**	7
HK$1,000,001 – HK$1,500,000	**–**	3
HK$1,500,001 – HK$2,000,000	**1**	–
HK$2,000,001 – HK$2,500,000	**3**	–
HK$4,000,001 – HK$4,500,000	**–**	1
HK$5,000,001 – HK$5,500,000	**1**	–
HK$5,500,001 – HK$6,000,000	**–**	1
HK$7,000,001 – HK$7,500,000	**2**	–
HK$8,000,001 – HK$8,500,000	**1**	1
HK$10,000,001 – HK$10,500,000	**1**	1
HK$10,500,001 – HK$11,000,000	**1**	2
HK$11,000,001 – HK$11,500,000	**–**	3
HK$13,500,001 – HK$14,000,000	**–**	1
HK$16,000,001 – HK$16,500,000	**–**	1
HK$16,500,001 – HK$17,000,000	**1**	–
HK$45,000,001 – HK$45,500,000	**1**	–
	17	21

No directors waived the right to receive emoluments during the year.

Of the five highest paid individuals in the Group, all (2002: all) are directors of the Company whose emoluments are included above.

15 Taxation

In March 2003, the Government of Hong Kong (the "Government") announced an increase in the profits tax rate applicable to the Group's operations in Hong Kong from 16 percent to 17.5 percent. Accordingly, Hong Kong profits tax has been provided at the rate of 17.5 percent (2002: 16 percent) on the estimated assessable profits for the year, except for certain subsidiaries as mentioned in note(a) below.

Overseas taxation has been calculated on the estimated assessable profits for the year at the rates prevailing in the respective jurisdictions.

In HK$ million	The Group	
	2003	2002
The Company and subsidiaries:		
Hong Kong profits tax		
– Provision for current year	**1,300**	1,249
– Underprovision in respect of prior years	**57**	3
Overseas tax		
– Provision for current year	**10**	137
– Overprovision in respect of prior years	**(74)**	–
Recovery of deferred taxation (note 33(a))	**(145)**	(152)
	1,148	1,237
A jointly controlled company:		
Hong Kong profits tax		
– Provision for current year	**24**	175
Recovery of deferred taxation	**(8)**	(14)
Associates:		
Hong Kong profits tax		
– Provision for current year	**1**	36
Recovery of deferred taxation	**–**	(28)
Total	**1,165**	1,406

15 Taxation *(continued)*

Reconciliation between taxation charge and the Group's accounting loss at applicable tax rates is set out below:

In HK$ million	The Group 2003	2002
Loss before taxation	**(5,151)**	(6,482)
Calculated at applicable taxation rates (note a)	**(922)**	(1,037)
Income not subject to taxation	**(48)**	(193)
Expenses not deductible for taxation purposes	**1,340**	2,100
Tax losses not recognized	**453**	304
Underprovision in prior years	**57**	3
Income not subject to taxation and/or expenses not deductible for taxation purposes for jointly controlled companies and associates, net	**161**	36
(Recovery of)/Provision for deferred tax on revaluation surplus of properties	**(56)**	56
Tax provision of overseas operations	**10**	137
Effect on opening balance of deferred tax resulting from an increase in tax rate during the year	**170**	–
Taxation charge	**1,165**	1,406

a. For certain subsidiaries having accounting year end date of March 31, the applicable tax rate of 16 percent was used on the estimated assessable profits for the first three months of 2003 while 17.5 percent was used on the estimated assessable profits for the rest of the year.

16 Loss Attributable to Shareholders

Loss of HK$8,660 million (2002: HK$14,049 million) attributable to shareholders was dealt with in the financial statements of the Company.

17 Loss Per Share

The calculation of basic loss per share is based on the following data:

	2003	2002
Loss (in HK$ million)	**(6,100)**	(7,762)
Weighted average number of ordinary shares	**4,967,178,732**	4,605,653,512

The diluted loss per share for the year ended December 31, 2003 and 2002 is the same as the basic loss per share as all potential ordinary shares are anti-dilutive.

The weighted average number of ordinary shares in 2003 and 2002 for the purposes of calculating the basic and diluted loss per share has been retrospectively adjusted for the five-to-one share consolidation which took place in January 2003.

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18 Fixed Assets

In HK$ million	Investment properties	Land and buildings	Exchange equipment	Transmission plant	Other plant and equipment	Projects under construction	Total
THE GROUP							
Cost or valuation							
Beginning of year	5,635	3,445	6,883	7,722	4,542	1,146	29,373
Additions							
– through acquisition of subsidiaries	–	–	–	–	25	–	25
– others	–	–	143	242	528	1,045	1,958
Transfers	(54)	46	372	340	346	(1,050)	–
Elimination of accumulated depreciation on transfer to investment properties	–	(5)	–	–	(2)	–	(7)
Disposals	(6)	(147)	–	–	(72)	–	(225)
Exchange differences	–	26	–	–	7	–	33
Surplus on revaluation	305	–	–	–	–	–	305
End of year	5,880	3,365	7,398	8,304	5,374	1,141	31,462
Representing:							
At cost	–	3,365	7,398	8,304	5,374	1,141	25,582
At valuation	5,880	–	–	–	–	–	5,880
	5,880	3,365	7,398	8,304	5,374	1,141	31,462
Accumulated depreciation and impairment							
Beginning of year	–	192	1,880	1,392	2,629	–	6,093
Charge for the year	–	93	1,017	663	901	–	2,674
Provision for impairment in value	–	–	371	435	361	–	1,167
Elimination of accumulated depreciation on transfer to investment properties	–	(5)	–	–	(2)	–	(7)
Disposals	–	(4)	–	–	(19)	–	(23)
Exchange differences	–	2	–	–	16	–	18
End of year	–	278	3,268	2,490	3,886	–	9,922
Net book value							
End of year	5,880	3,087	4,130	5,814	1,488	1,141	21,540
Beginning of year	5,635	3,253	5,003	6,330	1,913	1,146	23,280

No land and buildings were pledged as security for bank borrowings of the Group as at December 31, 2003 (2002: HK$93 million).

18 Fixed Assets *(continued)*

The carrying amount of investment properties and land and buildings of the Group is analyzed as follows:

In HK$ million	Investment properties		Land and buildings	
	2003	2002	**2003**	2002
Held in Hong Kong				
On long lease (over 50 years)	**2,117**	1,869	**1,447**	1,483
On medium-term lease (10-50 years)	**4**	10	**1,559**	1,563
On short lease (less than 10 years)	**4**	5	**–**	–
Held outside Hong Kong				
Freehold	**–**	–	**44**	122
Leasehold				
On long lease (over 50 years)	**–**	–	**–**	46
On medium-term lease (10-50 years)	**3,755**	3,751	**37**	39
	5,880	5,635	**3,087**	3,253

Investment properties held in and outside Hong Kong were revalued as at December 31, 2003 by an independent valuer, CB Richard Ellis Limited. The basis of valuation for investment properties was open market value.

Approximately HK$3,737 million (2002: HK$3,830 million) of the investment properties were mortgaged as collateral for banking facilities of the Group.

19 Properties Held for/Under Development

In HK$ million	The Group	
	2003	2002
Leasehold land, at cost:		
Located in Hong Kong	**3**	3
Properties held for development	**3**	3
Properties under development (note b)	**4,068**	4,354
Less: Properties under development classified as current assets	**(297)**	–
	3,771	4,354
Total	**3,774**	4,357

a. No properties held for/under development were pledged as security for banking facilities as at December 31, 2003 (2002: Nil).

b. Pursuant to an agreement dated May 17, 2000 entered into with the Government ("Cyberport Project Agreement"), the Group was granted an exclusive right and obligation to design, develop, construct and market the Cyberport Project at Telegraph Bay on the Hong Kong Island. The Cyberport Project consists of commercial and residential portions. Pre-sales of residential portion of the Cyberport Project commenced in February 2003.

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20 Goodwill

In HK$ million	The Group 2003 Goodwill carried on consolidated balance sheet	The Group 2003 Goodwill carried in reserves
Cost		
Beginning of year	1,429	166,177
Additions	106	–
End of year	1,535	166,177
Accumulated amortization and impairment		
Beginning of year	125	128,039
Charge for the year	82	–
Provision for impairment	395	784
End of year	602	128,823
Carrying amount		
End of year	933	37,354
Beginning of year	1,304	38,138

21 Intangible Assets

In HK$ million	The Group 2003				
	Trademarks	Content Licence	Wireless Broadband Licence	Others	Total
Cost					
Beginning of year	1,518	375	–	61	1,954
Additions	–	–	93	2	95
End of year	1,518	375	93	63	2,049
Accumulated amortization and impairment					
Beginning of year	180	36	–	–	216
Charge for the year	76	38	11	7	132
Provision for impairment	–	301	–	50	351
End of year	256	375	11	57	699
Net book value					
End of year	1,262	–	82	6	1,350
Beginning of year	1,338	339	–	61	1,738

22 Investment in Subsidiaries

In HK$ million	The Company 2003	2002
Unlisted shares, at cost	**25,549**	24,599
Amounts due from subsidiaries	**203,323**	198,509
	228,872	223,108
Less: Provisions for impairment in value	**(148,179)**	(141,738)
	80,693	81,370
Amounts due to subsidiaries	**(56,639)**	(55,053)
	24,054	26,317

The provisions for impairment in value of HK$148,179 million (2002: HK$141,738 million) relate to certain subsidiaries of the Company which hold the Group's investments in subsidiaries, jointly controlled companies, associates, investment securities and other investments.

Certain subsidiaries had borrowings to or from the Company bearing interest at commercial rates throughout the terms of the borrowings. The interest bearing principal receivable from subsidiaries as at December 31, 2003 is HK$503 million (2002: HK$5,896 million) and the interest bearing principal payable to subsidiaries as at December 31, 2003 is HK$16,327 million (2002: HK$12,838 million). Other balances with subsidiaries are unsecured, non-interest bearing and have no fixed terms of repayment.

Dividends from the PRC joint ventures accounted for as subsidiaries will be declared based on the profits in the statutory financial statements of these PRC joint ventures. Such profits will be different from the amounts reported under HK GAAP.

As at December 31, 2003, the Group has financed the operations of certain of its PRC joint ventures accounted for as subsidiaries in the form of shareholder's loans amounting to approximately US$198 million (2002: US$191 million) which have not been registered with the State Administration of Foreign Exchange. As a result, remittances in foreign currency of these amounts outside the PRC may be restricted.

As at December 31, 2003, particulars of the principal subsidiaries of the Company are as follows:

Company name	Place of incorporation/ operations	Principal activities	Nominal value of issued capital/ registered capital	Equity interest attributable to the Group Directly	Indirectly
PCCW-HKT Limited	Hong Kong	Investment holding	HK$6,092,100,052	–	100%
PCCW-HKT Telephone Limited*	Hong Kong	Telecommunications services	HK$2,163,783,209	–	100%
PCCW-HKT Business Services Limited	Hong Kong	Provision of business customer premises equipment and ancillary business services	HK$2	–	100%
PCCW-HKT Consumer Services Limited	Hong Kong	Provision of consumer premises equipment, computer products and ancillary services	HK$2	–	100%
PCCW-HKT Network Services Limited	Hong Kong	Provision of retail international data and value-added services, and local value-added telecommunications services	HK$2	–	100%
PCCW-HKT Products & Services Limited*	Hong Kong	Management of customer loyalty programs "No.1 Club" and "**Partners**" for members of the programs	HK$8,437,500	–	100%
PCCW Teleservices (Hong Kong) Limited	Hong Kong	Provision of customer relationship management and customer contact management solutions and services	HK$2	–	100%

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22 Investment in Subsidiaries *(continued)*

Company name	Place of incorporation/ operations	Principal activities	Nominal value of issued capital/ registered capital	Equity interest attributable to the Group	
				Directly	Indirectly
PCCW Teleservices Operations (Hong Kong) Limited	Hong Kong	Provision of customer relationship management and customer contact management solutions and services	HK$2	–	100%
Cascade Limited	Hong Kong	Design, build and operate network infrastructures including technical consultancy and operation outsourcing	HK$10,000	–	100%
PCCW IMS Limited	Hong Kong	Retail broadband and narrowband Internet access services under the “NETVIGATOR” brandname, and the provision of interactive multimedia services and other support services	HK$2	–	100%
Pacific Century Systems Limited	Hong Kong	Customer premises equipment related business	HK$1,000,000	100%	–
Corporate Access Limited	Cayman Islands/ Asia Pacific	Transponder leasing	US$10	–	100%
BtN Access (HK) Limited	Hong Kong	Provision of satellite based telecommunication services to third parties and satellite transponder capacity to a fellow subsidiary	HK$10	–	100%
Beyond The Network Limited	Hong Kong	Global Internet Protocol based communication service	HK$2	–	100%
Beyond the Network America, Inc.	United States of America	Supply of broadband Internet access solutions and web services	US$18	–	100%
電訊盈科（北京）有限公司	The PRC	System integration, consulting and informatization project	US$6,750,000	–	100%
Omnilink Technology Limited	British Virgin Islands	Investment holding	US$14,850	–	76.43%
Unihub China Information Technology Company Limited 中盈優創資訊科技有限公司	The PRC	Selling of hardware and software and information system consulting services	RMB200,000,000	–	38.2%
Unihub Limited (formerly PCCW Business eSolutions (HK) Limited)	Hong Kong/ Asia Pacific	Computer services and provision of IP/IT related value-added services to business customers	HK$1,200	–	100%
PCCW Business eSolutions Limited	Hong Kong	Provision of IP/IT related, value-added services to business customers	HK$2	–	100%
廣州電盈企業網絡系統有限公司	The PRC	Systems integration and technology consultancy	HK$5,000,000	–	100%
PCCW Powerbase Data Center Services (HK) Limited	Hong Kong	Data center services	HK$2	–	100%
Power Logistics Limited	Hong Kong	Delivery services	HK$100,000	–	100%

22 Investment in Subsidiaries *(continued)*

Company name	Place of incorporation/ operations	Principal activities	Nominal value of issued capital/ registered capital	Equity interest attributable to the Group Directly	Indirectly
PCCW Directories Limited*	Hong Kong	Sale of advertising in the Business White Pages, Yellow Pages for businesses and Yellow Pages for customers, publication of directories, provision of Internet directory services and sale of on-line advertising	HK$10,000	–	100%
ChinaBiG Limited	Hong Kong	Production and distribution of trade directory	HK$359,189	–	62.31%
iLink Holdings Limited	Cayman Islands/ Hong Kong and the PRC	Provision of data center services, including Internet connectivity, server hosting and co-location services, other value-added services and sales of equipment and software	HK$50,463,000	–	100%
SecureNet Asia Limited	Hong Kong	Provision of Internet security audit and consultancy services as well as a full range of smart card, security products and solutions for e-Commerce transactions	HK$72,462,299	–	100%
Cyber-Port Limited	Hong Kong	Property development	HK$2	–	100%
Beijing Jing Wei House and Land Estate Development Co., Ltd.	The PRC	Property development	US$50,000,000	–	100%
Partner Link Investments Limited	British Virgin Islands/ Hong Kong	Property investment	US$1	–	100%
Ripley Investments Limited	Hong Kong	Property investment	HK$10	–	100%
PCCW Facilities Management Limited	Hong Kong	Property management services	HK$2	–	100%
JALECO LTD. (formerly Pacific Century CyberWorks Japan Co., Ltd.)	Japan	Software and game development, Internet content, e-commerce, broadband services and other businesses	Yen19,742,711,522	–	76.13%
Taiwan Telecommunication Network Services Co., Ltd.	Taiwan	Type II Telecommunications services provider	NT$1,087,000,000	–	56.56%
UK Broadband Limited (formerly Poundradio Limited)	United Kingdom	Public Fixed Wireless Access Licence Business	GBP1	–	100%

Certain subsidiaries which do not materially affect the results or financial position of the Group are not included.

* The subsidiary has accounting year end date of March 31. These subsidiaries prepare, for the purpose of consolidation, financial statements as at the same date as the Group.

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23 Interest in Jointly Controlled Companies

In HK$ million	The Group 2003	The Group 2002	The Company 2003	The Company 2002
Share of net assets of jointly controlled companies	**2,821**	3,806	**–**	–
Loans due from jointly controlled companies	**1,147**	93	**1,139**	–
Amounts due from jointly controlled companies	**27**	39	**–**	–
Amounts due to jointly controlled companies	**(1)**	(374)	**–**	–
	3,994	3,564	**1,139**	–
Provision for impairment	**(3,961)**	(59)	**(1,139)**	–
	33	3,505	**–**	–
Investments at cost, unlisted shares	**3,130**	3,581	**–**	–

Balances with the jointly controlled companies are unsecured, non-interest bearing and have no fixed terms of repayment except for the capacity prepayment made to REACH of HK$1,139 million (2002: Nil) (see note 3(c)) as included in "Loans due from jointly controlled companies" above.

As at December 31, 2003, particulars of the principal jointly controlled company of the Group are as follows:

Company name	Place of incorporation/ operations	Principal activities	Nominal value of issued capital/ registered capital	Equity interest attributable to the Group Directly	Equity interest attributable to the Group Indirectly
Reach Ltd.	Bermuda/Asia	Provision of international telecommunication services	US$5,000,000,000	–	50%

Summarized unaudited financial information of the significant jointly controlled company, REACH, is as follows:

In HK$ million	2003	2002
Condensed consolidated balance sheet information as at December 31		
Non-current assets	**23,800**	24,433
Current assets	**2,346**	3,982
Total assets	**26,146**	28,415
Non-current liabilities	**(13,710)**	(14,293)
Current liabilities	**(3,651)**	(3,854)
Minority interests	**(158)**	(159)
Net assets	**8,627**	10,109
Condensed consolidated income statement information for the year ended December 31		
Turnover	**7,036**	9,854
(Loss)/Profit after taxation	**(1,747)**	1,141

On April 15, 2003, REACH and its bankers amended the terms of REACH's US$1,500 million syndicated term loan facility, which was subsequently reduced to US$1,200 million, with effect from April 25, 2003. The amendments to the term loan facility were intended to provide REACH with greater financial flexibility and an improved capital structure. REACH continues to operate in a difficult environment and the industry is expected to remain challenging for a period of time due to aggressive pricing and over supply of capacity.

The Group has performed an assessment of the fair value of its interest in REACH, including the related goodwill that had previously been eliminated against reserves, as at December 31, 2003. As a result, based on the estimated value in use of REACH determined using a discount rate of 10 percent (2002: 9 percent), the Group has made full provision for impairment of its previously unimpaired interest in REACH, recognizing an impairment loss of approximately HK$4,159 million (2002: HK$8,263 million) in the income statement for the year ended December 31, 2003. Accordingly, the Group's total interest in REACH has been written down to zero as at December 31, 2003 (2002: HK$3,930 million).

23 Interest in Jointly Controlled Companies *(continued)*

An analysis of the Group's total interest in REACH as at December 31, 2003 is as follows:

In HK$ million	**2003**	2002
Share of net assets	**2,705**	3,615
Capacity prepayment to REACH (note 3(c))	**1,139**	–
Goodwill previously eliminated against reserves	**8,578**	8,578
Total interest in REACH before provision for impairment	**12,422**	12,193
Provision for impairment	**(12,422)**	(8,263)
Total interest in REACH after provision for impairment	**–**	3,930

24 Interest in Associates

In HK$ million	The Group	
	2003	2002
Share of net assets of associates	**547**	1,203
Loans due from an associate	**78**	–
Amounts due from associates	**34**	67
Amounts due to associates	**–**	(115)
	659	1,155
Provision for impairment	**(171)**	(28)
	488	1,127
Investment at cost:		
Unlisted shares	**991**	1,086
Shares listed in Hong Kong	**–**	72
	991	1,158
Market value of listed shares	**–**	68

Balances with associates are unsecured, non-interest bearing and have no fixed terms of repayment except for the loans due from an associate, which bear interest at commercial rates, are secured by part of its movable properties and have fixed terms of repayment ranging up to three years from the date of drawdown in 2000.

As at December 31, 2003, particulars of the principal associates of the Company are as follows:

Company name	Place of incorporation/ operations	Principal activities	Nominal value of issued capital/registered capital	Equity interest attributable to the Group	
				Directly	Indirectly
Great Eastern Telecommunications Limited*	Cayman Islands	Investment holding	US$43,112,715	–	49%
Abacus Distribution Systems (Hong Kong) Limited	Hong Kong	Provision of computer reservation systems and travel related services	HK$15,600,000	–	37.04%
Petro-CyberWorks Information Technology Company Limited	The PRC	Design and development of Enterprise Resource Planning systems, and customer relationship management systems	RMB50,000,000	–	45%

* The associate has accounting year end date of March 31. The associate prepares, for the purpose of consolidation, financial statements as at the same date as the Group.

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25 Investments

Investments are analyzed as follows:

In HK$ million	The Group 2003	2002
Held-to-maturity securities	**37**	42
Investment securities (note a)	**601**	866
	638	908

a. Investment securities

In HK$ million	The Group 2003	2002
Unlisted, at cost	**1,751**	1,764
Less: Provision for impairment in value	**(1,222)**	(1,027)
	529	737
Listed, at cost		
Hong Kong	**51**	72
Overseas	**63**	270
	114	342
Less: Provision for impairment in value	**(42)**	(213)
	72	129
Total investment securities	**601**	866
Quoted market value of listed investment securities as at December 31	**83**	81

During the year, a listed security was transferred from investment securities to other investments. This transfer was effected at fair value. The aggregate unrealized holding loss at the date of transfer which had not been previously recognized of approximately HK$1 million (2002: HK$28 million) was recognized in the income statement at the date of transfer.

Investment securities with an aggregate carrying value of approximately HK$20 million (2002: Nil) were pledged as security for certain bank borrowings of the Group.

26 Current Assets and Liabilities

a. Properties held for sale

In HK$ million	The Group 2003	2002
Properties held for sale:		
Located in Macau	–	2
	–	2

b. Sales proceeds held in stakeholders' accounts

The balance represents proceeds from sale of residential portion of the Cyberport Project retained in bank accounts opened and maintained by stakeholders which will be transferred to specific bank accounts, which are restricted in use as described in note (c) below, pursuant to certain conditions and procedures as stated in the Cyberport Project Agreement.

c. Restricted cash

Pursuant to the Cyberport Project Agreement, the Group has a restricted cash balance of approximately HK$2,701 million as at December 31, 2003 (2002: Nil) held in specific bank accounts. The uses of the funds are specified in the Cyberport Project Agreement. The restricted cash balance of approximately HK$720 million as at December 31, 2002 represented a bank fixed deposit placed by the Company as a security for a standby letter of credit facility granted to an indirectly wholly-owned subsidiary of the Company (see note 39).

d. Inventories

In HK$ million	The Group 2003	2002
Raw materials	–	10
Work-in-progress	**218**	235
Finished goods	**298**	218
Consumable inventories	**21**	18
	537	481

e. Other investments

In HK$ million	The Group 2003	2002
Unlisted		
Overseas	**73**	62
Listed, at quoted market value		
Hong Kong	**250**	269
Overseas	–	63
	250	332
	323	394

During 2002, the Group entered into certain derivative contracts, in the form of equity swap and equity option contracts, with a third party with the effect of entering into forward sales of a portion of certain quoted other investments plus written call options for the remaining portion of those quoted other investments. As at December 31, 2003, the underlying quoted other investments with aggregate carrying value of approximately HK$246 million (2002: HK$237 million) have been placed as collateral for the transaction. The equity swap and equity option contracts have terms of up to five years from the date of the contracts and will mature in 2007 (see note 36(a)). No new derivative contract of this nature was entered into by the Group in 2003.

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26 Current Assets and Liabilities *(continued)*

f. Accounts receivable, net

An aging analysis of trade receivables is set out below:

In HK$ million	The Group 2003	2002
0 – 30 days	**1,125**	1,280
31 – 60 days	**206**	299
61 – 90 days	**88**	87
91 – 120 days	**64**	66
Over 120 days	**276**	112
	1,759	1,844
Less: Provision for doubtful debts	**(188)**	(120)
	1,571	1,724

The normal credit period granted by the Group ranges from 18 days to 30 days from the date of the invoice.

g. Short-term borrowings

In HK$ million	The Group 2003	2002
Bank loans	**54**	75
Current portion of long-term borrowings	**106**	79
	160	154
Secured	**154**	145
Unsecured	**6**	9

Please refer to note 39 for details of the Group's banking facilities.

h. Accounts payable

An aging analysis of accounts payable is set out below:

In HK$ million	The Group 2003	2002
0 – 30 days	**886**	534
31 – 60 days	**130**	56
61 – 90 days	**88**	120
91 – 120 days	**44**	37
Over 120 days	**229**	413
	1,377	1,160

26 Current Assets and Liabilities *(continued)*

i. Gross amounts due to customers for contract work

In HK$ million	The Group 2003	The Group 2002
Contract costs incurred plus attributable profits less foreseeable losses	**809**	801
Less: estimated value of work performed	**(809)**	(811)
	–	(10)

The total amount of progress billings, included in the estimated value of work performed as at December 31, 2003, is approximately HK$776 million (2002: HK$753 million).

Included in non-current assets at December 31, 2003 is approximately HK$8 million (2002: HK$8 million) representing retentions receivable from customers in respect of construction contracts in progress.

27 Long-term Liabilities

In HK$ million	The Group 2003	The Group 2002	The Company 2003	The Company 2002
Long-term borrowings (note a)	**22,029**	27,757	**3,003**	–
Convertible note and bonds (note b)	**12,477**	13,609	**440**	1,519
	34,506	41,366	**3,443**	1,519

a. Long-term borrowings

In HK$ million	The Group 2003	The Group 2002	The Company 2003	The Company 2002
Repayable within a period				
– not exceeding one year	**106**	79	**–**	–
– over one year, but not exceeding two years	**133**	123	**–**	–
– over two years, but not exceeding five years	**4,704**	406	**3,003**	–
– over five years	**17,192**	27,228	**–**	–
	22,135	27,836	**3,003**	–
Less: Amounts repayable within one year included under current liabilities	**(106)**	(79)	**–**	–
	22,029	27,757	**3,003**	–
Representing:				
US$456 million guaranteed notes (note i)	**3,541**	–	**–**	–
HK$3,003 million 5-year term loan (note ii)	**3,003**	–	**3,003**	–
US$500 million guaranteed notes (note iii)	**3,900**	–	**–**	–
US$4,700 million term loan (note iv)	**–**	6,094	**–**	–
Yen 30,000 million guaranteed notes (note v)	**1,950**	1,950	**–**	–
US$1,000 million guaranteed notes (note vi)	**7,801**	7,799	**–**	–
HK$5,000 million 6-year term loan (note vii)	**–**	5,000	**–**	–
HK$5,000 million 7-year term loan (note viii)	**–**	5,000	**–**	–
Other bank loans	**1,834**	1,914	**–**	–
	22,029	27,757	**3,003**	–
Secured	**1,819**	1,908	**–**	–
Unsecured	**20,210**	25,849	**3,003**	–

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27 Long-term Liabilities *(continued)*

a. Long-term borrowings *(continued)*

Details of major long-term borrowings of HK$22,029 million of the Group are presented below:

i. US$456 million guaranteed notes

On January 24, 2003, PCCW Capital No. 3 Limited, an indirectly wholly-owned subsidiary of the Company, privately placed US$456 million 7.88 percent guaranteed notes due 2013 to raise funds for general corporate purposes. The notes are unconditionally and irrevocably guaranteed by the Company. The notes were subsequently listed on the Luxembourg Stock Exchange on August 21, 2003.

ii. HK$3,003 million 5-year term loan

On March 14, 2003, the Company entered into a five-year term loan facility for HK$3,003 million (approximately US$385 million) on an unsecured basis. The loan is repayable in 2008. The proceeds were used for general corporate purposes. Subsequent to the year end, this term loan has been fully prepaid.

iii. US$500 million guaranteed notes

On July 17, 2003, PCCW-HKT Capital No. 2 Limited, an indirect wholly-owned subsidiary of the Company, issued US$500 million (approximately HK$3,900 million) 6 percent guaranteed notes due 2013 which are listed on the Luxembourg Stock Exchange. The notes are irrevocable and unconditionally guaranteed by PCCW-HKT Telephone Limited ("HKTC"), an indirect wholly-owned subsidiary of the Company, and rank pari passu with all other outstanding unsecured and unsubordinated obligations of HKTC. The proceeds are used for general corporate purposes.

iv. US$4,700 million term loan

In February 2001, the Group arranged syndicated bank borrowings of US$4,700 million (approximately HK$36,660 million) through HKTC. It consisted of three tranches (A, B & C) which were repayable in three to seven years. Each tranche carried interest at rates ranging from London Interbank Offered rates ("LIBOR") plus 0.85 percent to LIBOR plus 1.45 percent for the US dollar portion and Hong Kong Interbank Offered rates ("HIBOR") plus 0.95 percent to HIBOR plus 1.55 percent for the Hong Kong dollar portion. This term loan has been fully prepaid as at December 31, 2003.

v. Yen 30,000 million guaranteed notes

On October 26, 2001, Profit Century Finance Limited ("PCF"), an indirect wholly-owned subsidiary of the Company, completed the placement of Yen 30,000 million (approximately HK$1,950 million) 3.65 percent guaranteed notes due 2031 (the "Yen Notes"). Interest is payable semi-annually in arrears. The Yen Notes are redeemable at the option of PCF on any interest payment date falling on or after October 27, 2006.

The Yen Notes are unconditionally and irrevocably guaranteed by HKTC and will rank pari passu with all other outstanding unsecured and unsubordinated obligations of HKTC.

vi. US$1,000 million guaranteed notes

In November 2001, PCCW-HKT Capital Limited, an indirect wholly-owned subsidiary of the Company, issued US$1,000 million (approximately HK$7,800 million) 7.75 percent guaranteed notes due 2011 (the "Notes due 2011"). Interest is payable semi-annually in arrears. The interest rate payable on the Notes due 2011 will be subject to adjustment from time to time if the relevant rating agencies downgrade the rating ascribed to the Notes due 2011 below a pre-agreed level. The interest rate payable on the Notes due 2011 has been adjusted to 8 percent based on the current ratings.

The Notes due 2011 are unconditionally and irrevocably guaranteed by HKTC and will rank pari passu with all other outstanding unsecured and unsubordinated obligations of HKTC.

vii. HK$5,000 million 6-year term loan

On March 7, 2002, HKTC entered into an agreement for a six-year HK$5,000 million (approximately US$641 million) term loan facility. This loan was denominated in Hong Kong dollars and was to mature in March 2008. Interest was payable at HIBOR plus 0.55 percent per annum. This term loan has been fully prepaid as at December 31, 2003.

27 Long-term Liabilities *(continued)*

a. Long-term borrowings *(continued)*

viii. HK$5,000 million 7-year term loan

On April 17, 2002, HKTC entered into an agreement for a seven-year HK$5,000 million (approximately US$641 million) term loan facility. This loan was denominated in Hong Kong dollars and was to mature in April 2009. Interest was payable at HIBOR plus 0.65 percent per annum. This term loan has been fully prepaid as at December 31, 2003.

Please refer to note 39 for details of the Group's banking facilities.

b. Convertible note and bonds

In HK$ million	The Group		The Company	
	2003	2002	**2003**	2002
Repayable within a period				
– over one year, but not exceeding two years	**8,983**	–	**–**	–
– over two years, but not exceeding five years	**3,494**	13,609	**440**	1,519
	12,477	13,609	**440**	1,519
Representing:				
US$450 million 1 percent guaranteed convertible bonds due 2007 (note i)	**3,494**	3,510	**–**	–
Telstra Note due 2005 (note ii)	**440**	1,521	**440**	1,519
US$1,100 million 3.5 percent guaranteed convertible bonds due 2005 (note iii)	**8,543**	8,578	**–**	–
	12,477	13,609	**440**	1,519
Secured	**440**	1,521	**440**	1,519
Unsecured	**12,037**	12,088	**–**	–

Details of convertible note and bonds of HK$12,477 million of the Group are presented below:

i. US$450 million 1 percent guaranteed convertible bonds due 2007

On January 29, 2002, PCCW Capital No. 2 Limited, an indirect wholly-owned subsidiary of the Company, issued US$450 million 1 percent guaranteed convertible bonds due 2007, which are unconditionally and irrevocably guaranteed on a joint and several basis by the Company and HKTC. The convertible bonds due 2007 are listed on the Luxembourg Stock Exchange. They are convertible, at the option of their holders, into ordinary shares of the Company at an initial conversion price of HK$13.5836 (approximately US$1.7415) per share at any time up to and including the close of business on January 15, 2007. The bonds bear interest at 1 percent per annum, payable semi-annually in arrears on January 29 and July 29 in each year and at maturity, commencing on July 29, 2002. Unless previously redeemed, converted or purchased and cancelled, these bonds will be redeemed in US dollars at 119.383 percent of their principal amount, plus accrued interest on January 29, 2007. The redemption premium is being accrued on a straight-line basis from the date of issuance to the final redemption date of January 29, 2007.

ii. Telstra Note due 2005

On June 28, 2002, the Company issued the Telstra Note due 2005 to Telstra as part of the disposal of the Group's 40 percent interest in RWC (see note 13(a)). Unless previously redeemed or converted or purchased and cancelled, the Telstra Note due 2005 will be convertible into ordinary shares of the Company on June 30, 2005 or the date which is 30 days after the holder of the Telstra Note due 2005 has given notice to the Company declaring that, amongst other things, an event of default or potential event of default has occurred under REACH's US$1,500 million syndicated term loan facility, which was subsequently reduced to US$1,200 million under the amendment of the terms made in April 2003, or any financing agreement entered into for the purpose of refinancing all or a significant part of such facility; the Company has ceased to have a controlling interest in HKTC; or if HKTC and its subsidiaries have ceased to carry on as their principal business the provision of fixed line telecommunications services in Hong Kong ("Repayment Date"). Interest is payable at 5 percent per annum compounded on a quarterly basis.

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27 Long-term Liabilities *(continued)*

b. Convertible note and bonds *(continued)*

ii. Telstra Note due 2005 *(continued)*

On the Repayment Date, the Telstra Note due 2005, plus accrued interest thereon, will be redeemed through its mandatory conversion into ordinary shares of the Company at a conversion price determined by reference to the volume weighted average price of the ordinary shares of the Company as quoted on the Stock Exchange for the 20 dealing days immediately preceding the Repayment Date. The Company is entitled to early redeem the Telstra Note due 2005 in full by giving notice in writing to Telstra. The redemption amount would be the outstanding principal balance together with any unpaid interest accrued at the date of redemption. The Telstra Note due 2005 may be redeemed at the request of Telstra, if a resolution is passed or an order is made that the Company be wound up or dissolved. The Company's obligations to Telstra as the initial holder of the Telstra Note due 2005 are secured by the Group's equity interest in REACH.

On April 15, 2003, the Company redeemed US$143 million (approximately HK$1,115 million) of the Telstra Note due 2005 and issued an amended note in the principal amount of approximately US$54 million (approximately HK$421 million) ("Amended Telstra Note due 2005") to Telstra. The principal amount of the Amended Telstra Note due 2005 is equal to US$190 million, being the initial principal amount of the Telstra Note due 2005, plus its accrued and capitalized interest until March 31, 2003 of approximately US$7 million less US$143 million. The terms of the Amended Telstra Note due 2005 are substantially the same as those of the Telstra Note due 2005.

iii. US$1,100 million 3.5 percent guaranteed convertible bonds due 2005

On December 5, 2000, guaranteed convertible bonds due 2005 with the principal amount of US$1,100 million were issued by PCCW Capital Limited, a wholly-owned subsidiary of the Company. These bonds are listed on the Luxembourg Stock Exchange. They are convertible into ordinary shares of the Company at US$4.9804 (approximately HK$38.8471) subject to adjustments, per share at any time on or after January 5, 2001 and up to the close of business on November 21, 2005 and bear interest at 3.5 percent per annum, payable annually in arrears. Unless previously cancelled, redeemed or converted, these bonds will be redeemed in US dollars at 120.12 percent of the principal amount together with accrued interest on December 5, 2005. If these bonds are fully converted, the Company will be required to issue approximately 221 million ordinary shares. The redemption premium is being accrued on a straight-line basis from the date of issuance to the final redemption date of December 5, 2005.

As at December 31, 2003, the redemption premiums for the convertible bonds described in (i) and (iii) above totaling HK$1,326 million (2002: HK$844 million) and have been included in "Other long-term liabilities" in the consolidated balance sheet.

As at December 31, 2003, none of the above-mentioned convertible bonds had been converted into ordinary shares of the Company.

28 Provisions

In HK$ million	The Group 2003 Payment to the Government (note a)	Others	Total
Beginning of year	–	70	70
Additional provisions made	–	123	123
Additional provisions included within properties under development	3,680	–	3,680
Provisions used during the year	–	(62)	(62)
End of year	3,680	131	3,811
Less: amount classified as current liabilities	(1,739)	(131)	(1,870)
	1,941	–	1,941

28 Provisions *(continued)*

a. Pursuant to the Cyberport Project Agreement, the Government shall be entitled to receive payments based on certain terms and conditions. Provision for payment to the Government is included within properties under development as the amount is considered as a part of the development costs for the Cyberport Project. The provision is based on estimated sales proceeds of residential portion and the estimated development costs of the Cyberport Project. The estimated amount to be paid to the Government during the forthcoming year is classified as current liabilities.

29 Share Capital

	2003 Number of shares	**2003** Nominal value HK$ million	2002 Number of shares	2002 Nominal value HK$ million
Authorized:				
Ordinary shares of HK$0.05 each				
Beginning of year	**32,000,000,000**	**1,600**	32,000,000,000	1,600
Ordinary shares of HK$0.25 each				
Effect of increase in nominal value of shares from HK$0.05 each to HK$0.25 each (note a)	**(25,600,000,000)**	**–**	–	–
End of year	**6,400,000,000**	**1,600**	32,000,000,000	1,600
Issued and fully paid:				
Ordinary shares of HK$0.05 each				
Beginning of year	**23,268,770,370**	**1,164**	22,693,349,346	1,135
Exercise of other share options (note c)	**–**	**–**	376,680,000	19
Issued for acquisition of a licence from a wholly-owned subsidiary of Trans World International, Inc.	**–**	**–**	175,000,000	9
Issued for cash under the employee share award scheme	**–**	**–**	23,741,024	1
	23,268,770,370	**1,164**	23,268,770,370	1,164
Ordinary shares of HK$0.25 each				
Effect of increase in nominal value of shares from HK$0.05 each to HK$0.25 each (note a)	**(18,615,016,296)**	**–**	–	–
	4,653,754,074	**1,164**	23,268,770,370	1,164
Issued for cash (note b)	**715,000,000**	**179**	–	–
End of year	**5,368,754,074**	**1,343**	23,268,770,370	1,164

a. Pursuant to an ordinary resolution passed at an extraordinary general meeting of the Company held on January 7, 2003, every five issued and unissued shares of HK$0.05 each were consolidated into one new share of HK$0.25 with effect from January 8, 2003. Following the share consolidation becoming effective on January 8, 2003, the authorized share capital of the Company is HK$1,600,000,000 divided into 6,400,000,000 shares of HK$0.25 each, of which 4,653,754,074 shares were in issue and fully paid. The shares after the share consolidation rank pari passu in all respects with each other.

b. On July 17, 2003, the Company and PCRD entered into a subscription agreement, pursuant to which PCRD conditionally agreed to subscribe for 715,000,000 new shares of HK$0.25 each at a price of HK$4.40 per share. The net proceeds from the subscription were approximately HK$3,068 million, of which HK$3,060 million was used for debt repayment purpose. The subscription was completed on July 25, 2003.

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29 Share Capital *(continued)*

c. In September 1999, as part of the acquisition of Pacific Convergence Corporation, Ltd. ("PCC"), the Company entered into an agreement, as subsequently amended, with the minority shareholder of PCC Holdings Ltd. ("PCCH"), under which the minority shareholder can exchange its effective 40 percent shareholding in PCCH, the holding company of PCC, for 1,003,070,000 new ordinary shares of the Company at no further consideration. The option is exercisable for 10 years. The Company has the right to require the minority shareholder to exercise the option at the end of the option period to the extent it has not already been exercised. During the year ended December 31, 2002, the minority shareholder exercised the remaining portion of the options and the Company had issued 376,680,000 ordinary shares of HK$0.05 each to the minority shareholder.

All new ordinary shares issued during the year rank pari passu in all respects with the existing shares.

30 Employee Retirement Benefits

a. Defined benefit retirement schemes

The Group operates defined benefit retirement schemes ("DB Schemes") that provide lump sum benefits for employees upon resignation and retirement. The DB Schemes are final salary defined benefit schemes. The scheme assets are administered by independent trustees and are maintained independently of the Group's finances.

The DB Schemes are funded by contributions from the Group and employees in accordance with qualified independent actuaries' recommendation from time to time on the basis of periodic valuations.

On July 1, 2003 ("the Transfer Date"), all former members of the DB Schemes were transferred to defined contribution schemes operated by the Group for future services to be rendered by them to the Group and the benefit in respect of services rendered before the Transfer Date remained unchanged. In other words, scheme service in determining the level of benefit was frozen as of June 30, 2003 whereas the scheme salary and multiple will continue to grow. This freezing of scheme services was considered as a curtailment event under SSAP 34 but did not result in any accounting impact on the Group's financial statements.

The latest independent actuarial valuation of the DB Schemes, in accordance with SSAP 34, was carried out on December 31, 2003 and was prepared by Mr Aaron Wong of Watson Wyatt Hong Kong Limited, fellow of the Canadian Institute of Actuaries and also fellow of the Society of Actuaries, USA, using the projected unit credit method. The actuary was of the opinion that the fair value of the scheme assets was sufficient to cover 90.6 percent (2002: 75.7 percent) of the present value of the defined benefit obligations as at December 31, 2003.

i. The net liability recognized in the balance sheet is as follows:

In HK$ million	The Group	
	2003	2002
Present value of the defined benefit obligations	**4,567**	4,578
Fair value of scheme assets	**(4,137)**	(3,466)
	430	1,112
Unrecognized actuarial gains/(losses)	**16**	(526)
Defined benefit liability in the balance sheet	**446**	586

As at December 31, 2003, the scheme assets include ordinary shares issued by the Company with a fair value of approximately HK$5 million (2002: HK$2 million).

30 Employee Retirement Benefits *(continued)*

a. Defined benefit retirement schemes *(continued)*

ii. Movements in the net liability recognized in the balance sheet are as follows:

In HK$ million	The Group 2003	2002
Balance as at January 1	**586**	–
Transitional liability recognized upon adoption of SSAP 34	**–**	521
Balance as at beginning of year	**586**	521
Contributions paid for the year	**(243)**	(240)
Expense recognized in the income statement for the year	**103**	305
Balance as at end of year	**446**	586

iii. Expense recognized in the consolidated income statement is as follows:

In HK$ million	The Group 2003	2002
Current service cost	**89**	235
Interest cost	**234**	401
Expected return on scheme assets	**(222)**	(428)
Net actuarial losses recognized	**2**	–
Loss on curtailment and settlement	**–**	97
	103	305
The expense is recognized in the following line items in the consolidated income statement:		
General and administrative expenses – retirement costs for other staff (note 10)	**103**	197
Restructuring costs (notes 9 &10)	**–**	108
	103	305
Actual return on scheme assets	**700**	(341)

iv. The principal actuarial assumptions used (expressed as weighted averages) are as follows:

	The Group 2003	2002
Discount rate	**5.25%**	5.50%
Expected rate of return on scheme assets	**5.75%**	6.50%
Future salary increases	**3.50%**	3.50%

b. Defined contribution retirement scheme

The Group also operates defined contribution schemes, including the Mandatory Provident Fund Scheme ("the MPF scheme") under the Hong Kong Mandatory Provident Fund Schemes Ordinance, for employees employed under the jurisdiction of the Hong Kong Employment Ordinance and not previously covered by the defined benefit retirement scheme. The schemes are administered by independent trustees.

Under the defined contribution scheme, the employer is required to make contributions to the scheme at rates specified under the rules of the scheme. Where employees leave the scheme prior to the full vesting of the employer's contributions, the amount of forfeited contributions is used to reduce the contributions payable by the Group.

Under the MPF scheme, the employer and its employees are each required to make contributions to the scheme at 5 percent of the employees' relevant income, subject to a cap of monthly relevant income of HK$20,000. Contributions to the scheme vest immediately upon the completion of the service in the relevant service period.

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31 Equity Compensation Benefits

a. Share option scheme

The Company has a share option scheme which was adopted in September 1994 and amended in May 2002 under which the board of directors (the "Board") of the Company may, at their discretion, invite employees of the Group, including directors of any company in the Group, and other eligible persons, to take up options to subscribe for shares of the Company. For options granted before May 23, 2002, the exercise price in relation to each option was determined by the Board in its absolute discretion, but in any event would not be less than the higher of the nominal value of the shares and 80 percent of the average of the closing prices of the shares on the Stock Exchange for the five trading days immediately preceding the relevant date of offer.

For options granted on or after May 23, 2002, the exercise price in relation to each option shall be determined by the Board in its absolute discretion, but in any event shall not be less than the highest of: (i) the nominal value of a share of the Company; (ii) the closing price of the shares of the Company as stated in the daily quotation sheet of the Stock Exchange on the date of grant; and (iii) the average closing price of the shares of the Company as stated in the daily quotation sheets of the Stock Exchange for the five trading days immediately preceding the date of grant.

The vesting period and exercisable period of the options are determined by the directors but in any case no options can be exercised later than ten years from the date of grant. Each option gives the holder the right to subscribe for one share.

i. Movements in share options

	Number of options		
	2003	2002 After the share consolidation	2002 Before the share consolidation
Beginning of year	**109,559,896**	119,242,866	596,214,416
Issued (note iii)	**132,856,200**	14,930,700	74,653,500
Cancelled/Lapsed (note iv)	**(20,238,568)**	(24,613,670)	(123,068,352)
End of year (note ii)	**222,177,528**	109,559,896	547,799,564
Options vested as at end of year	**66,869,490**	54,540,325	272,701,628

The number of share options for the movement in 2002 (after the share consolidation) has been retrospectively adjusted for the five-to-one share consolidation which took place in January 2003.

31 Equity Compensation Benefits *(continued)*

a. Share option scheme *(continued)*

ii. Terms of unexpired and unexercised share options at balance sheet date

		2003 After the share consolidation		2002 Before the share consolidation	
Date of grant	Exercise period	Exercise price HK$	Number of options	Exercise price HK$	Number of options
August 17, 1999 to September 15, 1999	August 17, 2000 to August 17, 2009	**11.7800**	**19,525,188**	2.3560	123,741,352
October 25, 1999 to November 23, 1999	August 17, 2000 to October 25, 2009	**22.7600**	**4,509,200**	4.5520	32,046,000
December 20, 1999 to January 18, 2000	December 20, 2000 to December 20, 2009	**33.5600**	**–**	6.7120	1,080,000
February 8, 2000 to March 8, 2000	February 8, 2001 to February 8, 2010	**75.2400**	**86,700**	15.0480	433,500
August 26, 2000 to September 24, 2000	May 26, 2001 to August 26, 2010	**60.1200**	**10,308,600**	12.0240	57,168,000
October 27, 2000 to November 25, 2000	March 15, 2001 to October 27, 2010	**24.3600**	**12,966,082**	4.8720	73,731,010
January 22, 2001 to February 20, 2001	January 22, 2001 to January 22, 2011	**16.8400**	**23,278,438**	3.3680	138,357,902
February 20, 2001	February 8, 2002 to February 8, 2011	**18.7600**	**86,700**	3.7520	433,500
April 17, 2001 to May 16, 2001	May 26, 2001 to April 17, 2011	**10.3000**	**3,542,960**	2.0600	18,971,000
July 16, 2001 to September 15, 2001	July 16, 2002 to July 16, 2011	**9.1600**	**689,760**	1.8320	3,723,800
August 3, 2001	March 31, 2002 to August 1, 2011	**16.8400**	**–**	3.3680	4,000,000
September 27, 2001	September 27, 2001 to September 7, 2011	**6.8150**	**3,600,000**	1.3630	18,000,000
October 15, 2001 to November 13, 2001	October 15, 2002 to October 15, 2011	**8.6400**	**292,000**	1.7280	1,460,000
May 10, 2002	April 11, 2003 to April 11, 2012	**7.9150**	**231,700**	1.5830	1,158,500
May 28, 2002	April 29, 2003 to April 29, 2012	**9.9500**	**5,600,000**	1.9900	28,000,000
June 19, 2002	June 19, 2002 to May 21, 2012	**10.0900**	**279,000**	2.0180	2,895,000
August 1, 2002	August 1, 2003 to July 31, 2012	**8.0600**	**200,000**	1.6120	1,000,000
October 11, 2002	October 11, 2002 to October 10, 2007	**8.6165**	**1,200,000**	1.7233	6,000,000
November 13, 2002	November 13, 2003 to November 12, 2012	**6.1500**	**7,040,000**	1.2300	35,600,000
July 25, 2003	July 25, 2004 to July 23, 2013	**4.3500**	**127,551,200**	–	–
September 16, 2003	September 16, 2004 to September 14, 2013	**4.9000**	**1,190,000**	–	–
			222,177,528		547,799,564

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31 Equity Compensation Benefits *(continued)*

a. Share option scheme *(continued)*

iii. Details of share options granted during the year

Exercise period	2003 After the share consolidation Exercise price HK$	Consideration received HK$	Number of options	2002 Before the share consolidation Exercise price HK$	Consideration received HK$	Number of Options
April 11, 2003 to April 11, 2012	**7.9150**	**–**	**–**	1.5830	2	1,158,500
April 29, 2003 to April 29, 2012	**9.9500**	**–**	**–**	1.9900	1	28,000,000
June 19, 2002 to May 21, 2012	**10.0900**	**–**	**–**	2.0180	5	2,895,000
August 1, 2003 to July 31, 2012	**8.0600**	**–**	**–**	1.6120	–	1,000,000
October 11, 2002 to October 10, 2007	**8.6165**	**–**	**–**	1.7233	–	6,000,000
November 13, 2003 to November 12, 2012	**6.1500**	**–**	**–**	1.2300	–	35,600,000
July 25, 2004 to July 23, 2013	**4.3500**	**–**	**131,666,200**	–	–	–
September 16, 2004 to September 14, 2013	**4.9000**	**–**	**1,190,000**	–	–	–
		–	**132,856,200**		8	74,653,500

iv. Details of share options cancelled or lapsed during the year

Exercise period	2003 After the share consolidation Exercise price HK$	Number of options	2002 Before the share consolidation Exercise price HK$	Number of options
August 17, 2000 to August 17, 2009	**11.7800**	**5,223,068**	2.3560	3,792,002
August 17, 2000 to October 25, 2009	**22.7600**	**1,900,000**	4.5520	4,757,000
December 20, 2000 to December 20, 2009	**33.5600**	**216,000**	6.7120	–
May 26, 2001 to August 26, 2010	**60.1200**	**1,125,000**	12.0240	1,930,000
March 15, 2001 to October 27, 2010	**24.3600**	**1,780,120**	4.8720	33,132,150
January 22, 2001 to January 22, 2011	**16.8400**	**4,393,140**	3.3680	65,017,800
May 26, 2001 to April 17, 2011	**10.3000**	**251,240**	2.0600	1,957,200
May 7, 2002 to May 7, 2011	**11.1600**	**–**	2.2320	12,000,000
July 16, 2002 to July 16, 2011	**9.1600**	**55,000**	1.8320	482,200
March 31, 2002 to August 1, 2011	**16.8400**	**800,000**	3.3680	–
June 19, 2002 to May 21, 2012	**10.0900**	**300,000**	2.0180	–
November 13, 2003 to November 12, 2012	**6.1500**	**80,000**	1.2300	–
July 25, 2004 to July 24, 2013	**4.3500**	**4,115,000**	–	–
		20,238,568		123,068,352

b. Share award schemes

In 2002, the Company established two employee share incentive award schemes under which awards of shares may be granted to employees of participating subsidiaries. Directors of the Company are not eligible to participate in either scheme. On June 10, 2002, the Company approved the establishment of a scheme (the “Purchase Scheme”) under which selected employees are awarded shares purchased in the market. On November 12, 2002, the Company approved the establishment of a scheme (the “Subscription Scheme”) under which selected employees are awarded newly issued shares. The purpose of both the Purchase Scheme and the Subscription Scheme is to recognize the contributions of certain employees of the Group, to retain them for the continued operation and development of the Group, and to attract suitable personnel for the further development of the Group. Under both schemes, following the making of an award to an employee, the relevant shares are held on trust for that employee and then vest over a period of time provided that the employee remains an employee of the Group at the relevant time and satisfies any other conditions specified at the time the award is made. The maximum aggregate number of shares that can be awarded under the two schemes is limited to one percent of the issued share capital of the Company (excluding shares that have already been transferred to employees on vesting).

31 Equity Compensation Benefits *(continued)*

b. Share award schemes *(continued)*

A summary of movements in shares held under the share award schemes during the year is as follows:

	Number of shares 2003	2002
Beginning of year	**7,935,205**	–
Issue of the Company's shares under the share award scheme at par value of HK$0.25 per share	**–**	4,748,205
Purchases from the market by the trustee at average market price of HK$4.35 (2002: HK$8.24) per share	**834,800**	3,187,000
Awards of vested shares to employees during the year	**(2,999,005)**	–
End of year	**5,771,000**	7,935,205

The number of shares for the movement in 2002 has been retrospectively adjusted for the five-to-one share consolidation which took place in January 2003.

In HK$ million	2003	2002
Fair value of shares held as at December 31	**29**	49
Fair value, on issuance, of shares issued during the year	**–**	34
Fair value, on date of purchase, of shares purchased from the market	**4**	26
Fair value of shares awarded to employees during the year	**16**	–
Amounts recognized in the consolidated balance sheet as prepaid expenses	**17**	25
Amounts recognized in the consolidated income statement as staff costs	**12**	3

c. Employees' rights to invest in shares of JALECO

In August 2000, the Group established an incentive scheme under which certain employees of the Group are granted options to acquire equity interests in JALECO. The exercise price of the options to the employees was set at a price not less than the fair value of the shares at the time of issue. Shares of JALECO have been trading below the cost of the options since the first exercise date, and up to December 31, 2003. A total number of 4,021,000 (2002: 4,021,000) shares of JALECO were held by the incentive scheme which is operated under a limited partnership arrangement. As at December 31, 2003, no options have been exercised by the employees (2002: Nil).

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32 Reserves/(Deficit)

In HK$ million	2003 Share premium	2003 Property revaluation reserve	2003 Currency translation reserve	2003 Deficit	2003 Total
THE GROUP					
Beginning of year	**170,571**	**–**	**(117)**	**(177,534)**	**(7,080)**
Issue of ordinary shares, net of issuing expenses	**2,889**	**–**	**–**	**–**	**2,889**
Surplus on revaluation of investment properties	**–**	**305**	**–**	**–**	**305**
Translation exchange differences	**–**	**–**	**20**	**–**	**20**
Provision for impairment of goodwill attributable to REACH	**–**	**–**	**–**	**315**	**315**
Provision for impairment of goodwill attributable to subsidiaries	**–**	**–**	**–**	**469**	**469**
Loss for the year	**–**	**–**	**–**	**(6,100)**	**(6,100)**
End of year	**173,460**	**305**	**(97)**	**(182,850)**	**(9,182)**
Attributable to:					
– The Company and subsidiaries	**173,460**	**305**	**(97)**	**(183,004)**	**(9,336)**
– Jointly controlled companies	**–**	**–**	**–**	**57**	**57**
– Associates	**–**	**–**	**–**	**97**	**97**
End of year	**173,460**	**305**	**(97)**	**(182,850)**	**(9,182)**
THE COMPANY					
Beginning of year	**170,571**	**–**	**–**	**(143,306)**	**27,265**
Issue of ordinary shares, net of issuing expenses	**2,889**	**–**	**–**	**–**	**2,889**
Loss for the year	**–**	**–**	**–**	**(8,660)**	**(8,660)**
End of year	**173,460**	**–**	**–**	**(151,966)**	**21,494**

In HK$ million	2002 Share premium	2002 Property revaluation reserve	2002 Currency translation reserve	2002 Deficit	2002 Total
THE GROUP					
Beginning of year	169,635	–	(224)	(182,310)	(12,899)
Issue of ordinary shares and exercise of options, net of issuing expenses	936	–	–	–	936
Realization of goodwill on disposal of RWC	–	–	–	4,081	4,081
Translation exchange differences	–	–	107	–	107
Provision for impairment of goodwill attributable to REACH	–	–	–	8,263	8,263
Provision for impairment of goodwill attributable to a subsidiary	–	–	–	194	194
Loss for the year	–	–	–	(7,762)	(7,762)
End of year	170,571	–	(117)	(177,534)	(7,080)
Attributable to:					
– The Company and subsidiaries	170,571	–	(117)	(178,531)	(8,077)
– Jointly controlled companies	–	–	–	964	964
– Associates	–	–	–	33	33
End of year	170,571	–	(117)	(177,534)	(7,080)
THE COMPANY					
Beginning of year	169,635	–	–	(129,257)	40,378
Issue of ordinary shares and exercise of options, net of issuing expenses	936	–	–	–	936
Loss for the year	–	–	–	(14,049)	(14,049)
End of year	170,571	–	–	(143,306)	27,265

33 Deferred Taxation

a. Movement in deferred tax liabilities during the year is as follows:

In HK$ million	2003					
	Accelerated tax depreciation	Valuation adjustment resulting from acquisition of subsidiaries	Leasing partnership	Revaluation of properties	Others	Total
THE GROUP						
Beginning of year	**1,840**	**485**	**467**	**451**	**(78)**	**3,165**
Deferred taxation (credited)/charged to income statement during the year (note 15)	**(115)**	**5**	**2**	**20**	**(57)**	**(145)**
Exchange differences	**–**	**–**	**–**	**–**	**6**	**6**
End of year	**1,725**	**490**	**469**	**471**	**(129)**	**3,026**

In HK$ million	2002					
	Accelerated tax depreciation	Valuation adjustment resulting from acquisition of subsidiaries	Leasing partnership	Revaluation of properties	Others	Total
THE GROUP						
Beginning of year	2,036	506	520	395	(137)	3,320
Deferred taxation (credited)/charged to income statement during the year (note 15)	(196)	(21)	(53)	56	62	(152)
Exchange differences	–	–	–	–	(3)	(3)
End of year	1,840	485	467	451	(78)	3,165

b. Deferred income tax assets are recognized for tax loss carry forwards to the extent that realization of the related tax benefit through utilization against future taxable profits is probable. The Group has unutilized estimated tax losses of HK$13,766 million (2002: HK$12,176 million) to carry forward for deduction against future taxable income. Estimated tax losses of HK$1,818 million (2002: HK$1,205 million) will expire within 1-5 years from December 31, 2003. The remaining portion of the tax losses, mainly relating to Hong Kong companies, can be carried forward indefinitely.

Notes to the Financial Statements

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(Amount expressed in Hong Kong dollars unless otherwise stated)

34 Notes to the Consolidated Cash Flow Statement

a. Reconciliation of loss before taxation to net cash inflow from operating activities

In HK$ million	The Group	
	2003	2002
Loss before taxation	**(5,151)**	(6,482)
Adjustment for:		
Losses on disposal of interests in RWC and MobileOne, net	**–**	1,433
Impairment loss on interest in REACH	**4,159**	8,263
Impairment loss on interest in another jointly controlled company	**227**	–
Impairment loss on interest in other associates	**78**	–
Provision for inventory obsolescence	**70**	26
Write-off of intangible assets	**–**	8
Interest income	**(132)**	(164)
Interest expense	**2,020**	1,948
Finance charges	**217**	226
Depreciation	**2,674**	2,623
Net unrealized holding (gains)/losses on other investments	**(8)**	142
Realized (gains)/losses on disposal of other investments	**(8)**	182
Realized gains on disposal of investments in jointly controlled companies and associates	**(8)**	(34)
Realized gains on disposal of investment securities	**(87)**	(56)
Provision for impairment of investments	**258**	581
Provision for impairment of fixed assets	**1,167**	232
Provision for impairment of multimedia business related assets	**301**	309
Provision for impairment of game business related assets	**893**	–
Provision for impairment of other non-current assets	**91**	–
Release of provision for an onerous contract	**–**	(464)
Loss on disposal of fixed assets	**145**	76
Provision for doubtful debts	**115**	148
Amortization of intangible assets	**132**	112
Amortization of goodwill	**82**	85
Amortization of business development costs	**–**	12
Amortization of premium received from equity options	**(12)**	(32)
Share of results of jointly controlled companies and associates	**826**	(831)
Gain on termination and amendment of the terms of cross currency swap contracts	**(532)**	(332)
OPERATING PROFIT BEFORE CHANGES IN WORKING CAPITAL	**7,517**	8,011
Decrease/(Increase) in operating assets:		
– properties under development	**286**	(2,204)
– inventories	**(123)**	(135)
– accounts receivable	**54**	(32)
– prepayments, deposits and other current assets	**(245)**	54
– sales proceeds held in stakeholders' accounts	**(2,402)**	–
– restricted cash	**(2,701)**	–
– amounts due from related companies	**(25)**	204
Increase/(Decrease) in operating liabilities:		
– accruals, accounts payable, provisions, other payables and deferred income	**3,448**	159
– amount due to minority shareholders of subsidiaries	**–**	5
– gross amounts due to customers for contract work	**(10)**	(38)
– amounts due to related companies	**(322)**	(446)
– advances from customers	**(63)**	(277)
CASH GENERATED FROM OPERATIONS	**5,414**	5,301
Interest paid	**(294)**	(221)
Interest received	**93**	82
Tax paid		
– Hong Kong profits tax paid	**(1,371)**	(1,243)
– Overseas tax paid	**(26)**	(2)
NET CASH INFLOW FROM OPERATING ACTIVITIES	**3,816**	3,917

34 Notes to the Consolidated Cash Flow Statement *(continued)*

b. Acquisition of subsidiaries

In HK$ million	The Group 2003	2002
Net assets acquired:		
Fixed assets	**25**	–
Inventories	**3**	–
Accounts receivable, prepayments, deposits and other assets	**161**	–
Cash and bank balances	**304**	–
Accounts payable, accruals and other payables	**(135)**	–
Minority interests	**4**	–
	362	–
Goodwill arising on acquisition	**55**	–
	417	–
Satisfied by:		
Interest in jointly controlled companies	**130**	–
Interest in associates	**112**	–
Setting off shareholder's loan	**23**	–
Cash from internal resources	**152**	–
	417	–
Analysis of the net inflow of cash and cash equivalents in respect of the acquisition of subsidiaries:		
Cash	**(152)**	–
Cash and bank balances acquired	**304**	–
Net cash inflow in respect of acquisition of subsidiaries	**152**	–

c. Analysis of cash and cash equivalents

In HK$ million	The Group 2003	2002
Cash and bank balances	**8,248**	8,638
Bank loans and overdrafts	**(12)**	(37)
Restricted cash	**(2,701)**	(720)
Cash and cash equivalents as at December 31	**5,535**	7,881

35 Net Lease Payments Receivable

A company within the Group is a limited partner in a number of limited partnerships, which own and lease assets to third parties.

In HK$ million	The Group 2003	2002
The net investment in relation to these finance leases comprises:		
Net lease payments receivable	**454**	475
Less: Current portion of net lease payments receivable (included in "Prepayments, deposits and other current assets" on consolidated balance sheet)	**(77)**	–
	377	475

Non-recourse finance of HK$2,302 million (2002: HK$2,600 million) has been offset against net rentals receivable in arriving at the above net investment in finance leases.

36 Financial Instruments

a. Equity options

In 2002, the Group entered into certain derivative contracts, in the form of equity swap and equity option contracts, with a third party with the effect of entering into forward sales of a portion of certain quoted other investments plus written call options for the remaining portion of those quoted other investments. The deemed forward sales effectively eliminated the Group's exposure to market price fluctuation and accordingly, the underlying quoted other investments were carried at the deemed forward price as at December 31, 2002. An advance receipt of approximately HK$187 million for the deemed forward sales was received in 2002. The amount was included in other long-term liabilities in the consolidated balance sheet and is interest bearing at commercial rate. The Group recognized a gain of approximately HK$10 million for marking the quoted other investments to the deemed forward price and the gain was reflected in net gains on investments in the income statement for the year ended December 31, 2002. The Group also received premiums of approximately HK$25 million for the written call options with notional amount of approximately HK$71 million. The premiums received were recorded as deferred income and are being amortized into income on a straight-line basis over the life of the call options. The underlying quoted other investments are carried at market value at each balance sheet date and any unrealized holding gains or losses are recognized in the income statement in the period as it arises. The underlying quoted other investments for both the deemed forward sale and written call options have been placed as collateral for the above equity swap and equity option transactions (note 26(e)). No new derivative contract of this nature was entered into by the Group in 2003.

Apart from the above, as at December 31, 2003, the Group had no other outstanding written equity call options (2002: with a total notional amount of approximately HK$157 million). Other than the equity options as mentioned in the previous paragraph, the Group did not receive premiums on writing new equity options in 2003 and 2002.

The notional amounts of the outstanding equity option contracts indicate the volume of transactions outstanding at the balance sheet date and do not represent amounts at risk.

b. Interest rate options

The Group enters into interest rate options to manage its interest rate risk. As at December 31, 2003, the total notional amount of such instruments was HK$68 million (2002: HK$150 million).

The notional amounts of the outstanding interest rate options indicate the volume of transactions outstanding at the balance sheet date and do not represent amounts at risk.

c. Swaps

As at December 31, 2003, the Group had outstanding cross currency swap contracts of US$2,756 million and Yen 30,000 million (2002: US$2,990 million and Yen 30,000 million) at various rates totaling approximately HK$21,497 million and HK$1,950 million (2002: HK$23,322 million and HK$1,950 million), respectively, to manage the Group's exposure to foreign currencies and interest rate fluctuations. In addition, the Group had outstanding swap contracts to receive HK$7,800 million at monthly floating rate and to pay HK$7,800 million at daily floating rate to manage the Group's exposure to interest rate fluctuation as at December 31, 2002.

During the year ended December 31, 2003, the Group has recognized a gain of approximately HK$532 million (2002: HK$332 million) from the termination of certain cross currency swap contracts and the amendment of the terms of another cross currency swap contract. The gain is reflected under "Net gains on investments" in the consolidated income statement (see note 7).

37 Commitments

a. Capital

In HK$ million	The Group 2003	2002
Authorized and contracted for	**3,025**	4,155
Authorized but not contracted for	**3,480**	7,436
	6,505	11,591

An analysis of the above capital commitments by nature is as follows:

In HK$ million	The Group 2003	2002
Investments	**274**	137
Investment properties	**82**	–
Property development (note i)	**5,637**	11,080
Development of Internet business	**–**	101
Construction contracts	**–**	24
Acquisition of fixed assets	**512**	247
Others	**–**	2
	6,505	11,591

i. The capital commitment as disclosed above represented management's best estimate of total construction costs for the Cyberport Project, which has been revised from the total construction costs since the Cyberport Project Agreement was entered into on May 17, 2000.

b. Operating leases

As at December 31, 2003, the total future minimum lease payments under non-cancellable operating leases are payable as follows:

Land and buildings

In HK$ million	The Group 2003	2002
Within 1 year	**148**	188
After 1 year but within 5 years	**259**	288
After 5 years	**198**	123
	605	599

Equipment

In HK$ million	The Group 2003	2002
Within 1 year	**44**	35
After 1 year but within 5 years	**–**	29
	44	64

c. Others

As at December 31, 2003, the Group had outstanding forward foreign exchange contracts to buy US$750 million (2002: buy US$160 million and sell S$110 million) at various rates totaling approximately HK$5,860 million (2002: HK$1,245 million and US$63 million).

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38 Contingent Liabilities

In HK$ million	The Group 2003	2002	The Company 2003	2002
Performance guarantee	**130**	74	**–**	1
Tender guarantee	**2**	10	**–**	–
Advance payment guarantee	**9**	14	**–**	–
Guarantees given to banks in respect of credit facilities granted to				
– subsidiaries	**–**	–	**17,632**	14,112
– an associate	**85**	–	**–**	–
Guarantee in lieu of cash deposit	**16**	20	**–**	–
Staff mortgage loan guarantee	**1**	5	**–**	–
Guarantee indemnity	**12**	11	**–**	–
	255	134	**17,632**	14,113

On April 23, 2002, a writ of summons was issued against PCCW-HKT Limited ("HKT"), an indirect wholly-owned subsidiary of the Company, by New Century Infocomm Tech Co., Ltd. for HKT's failure to purchase 6,522,000 shares of Taiwan Telecommunication Network Services Co., Ltd. ("TTNS"), an indirect subsidiary of the Company, pursuant to an option agreement entered into on July 24, 2000. The total claim against HKT amounted to approximately HK$96 million (NT$418 million), being the purchase price of shares in TTNS, contractual interest for the period from January 1, 2001 to January 2, 2002 at 6.725 percent per annum and interest on the due amount pursuant to Sections 48 and 49 of the High Court Ordinance, Cap. 4. However, this figure should be reduced by the current market value of the shares in TTNS which would be transferred to HKT in the event that the claimants are successful in their claim. A defence was filed by HKT on May 29, 2002 and proceedings are ongoing. Based on legal advice received, the directors consider that HKT has valid defences and therefore no provision has been made.

On August 23, 2003, a summons was issued against the Company upon the application of Wharf T&T Limited ("Wharf"). The summons relates to an application to a Magistrate for an order declaring that the Company shall not obstruct or prevent Wharf from entering PCCW Tower for the purposes of exercising its rights under Section 14(1) of the Telecommunications Ordinance to install telephone lines amongst other things. Based on facts available and legal advice received, the application would not result in any award, damages or monetary penalty against the Company. Accordingly, no provision has been made.

The Company is subject to certain parent company guarantee obligations to guarantee performance of its wholly-owned subsidiaries in the normal course of their businesses. The amount of liabilities arising from such obligations, if any, cannot be ascertained but the Directors are of the opinion that any resulting liability would not materially affect the financial position of the Company.

39 Banking Facilities

Aggregate banking facilities as at December 31, 2003 were HK$17,714 million (2002: HK$21,660 million) of which the unused facilities amounted to HK$12,745 million (2002: HK$3,521 million).

A summary of major loan agreement terms is set out in note 27(a).

Security pledged for certain banking facilities includes:

In HK$ million	The Group 2003	2002
Investment properties	**3,737**	3,830
Land and buildings	**–**	93
Interest in a subsidiary	**312**	312
Fixed deposit	**119**	122
Investment securities	**20**	–
	4,188	4,357

39 Banking Facilities *(continued)*

As at December 31, 2002, Cyber-Port Limited, an indirect wholly-owned subsidiary of the Company, had been granted a standby letter of credit facility amounting to approximately HK$722 million from a bank for the purpose of providing a cashflow guarantee covering an amount equal to the 6-month forecast net cashflow requirements of the Cyberport Project, defined in and pursuant to the terms of the Cyberport Project Agreement. Such facility was secured by a bank fixed deposit of approximately HK$720 million placed by the Company. This amount was included in "Restricted cash" on consolidated balance sheet (see note 26(c)) as at December 31, 2002. There was no such standby letter of credit facility as at December 31, 2003.

40 Post Balance Sheet Events

The following events occurred subsequent to December 31, 2003 up to the date of approval of these financial statements by the Board of Directors:

a. On January 19, 2004, the Company prepaid in full a HK$750 million term loan.

b. On February 17, 2004, HKTC drew down HK$600 million under a five-year HK$6,000 million revolving loan facility entered into in December 2003.

c. On February 19, 2004, HKTC drew down HK$2,800 million under a seven-year HK$2,800 million revolving credit and term loan facility entered into in August 2003. This facility was amended to become a 100 percent revolving loan facility in October 2003.

d. On February 19, 2004, a sale and purchase agreement was signed to dispose of The Broadway, the office building located in the Wan Chai district in Hong Kong, at a profit of approximately HK$40 million and the completion date will be on or before March 16, 2004.

e. On February 26, 2004, the Company prepaid in full the HK$3,003 million five-year term loan.

f. On March 1, 2004, Beijing Jing Wei House and Land Estate Development Co., Ltd., an indirectly wholly-owned subsidiary of the Company, prepaid the outstanding principal amount of RMB1,220 million under the RMB1,300 million loan facility.

g. The Company and Dong Fang Gas Holdings Limited ("DFG"), a company incorporated in Bermuda and whose shares are listed on the Stock Exchange, entered into an agreement on March 5, 2004 (the "Sale and Purchase Agreement"). Pursuant to the Sale and Purchase Agreement, DFG has conditionally agreed to purchase the Company's interest in certain investment properties, the Cyberport Project and related property and facilities management companies for an aggregate consideration of HK$6,557 million. Approximately HK$2,967 million of the aggregate consideration will be satisfied by the allotment and issue of new shares of DFG. The remaining HK$3,590 million is to be satisfied by the issuance of convertible notes by DFG to the Company entitling the holder to convert the principal amount into new shares of DFG. DFG will become a subsidiary of the Company immediately after completion of the Sale and Purchase Agreement. The Group is in the process of evaluating the financial impact of this transaction which will be reflected in the Group's 2004 financial statements.