New Business - HK Pay TV

Internal delivery trials of the five TVB-packaged channels for exTV, the pay TV platform operated by Galaxy Satellite Broadcasting Limited, commenced at the end of 2003. Since early 2004 five channels - TVBN, TVBE, TVBQ, TVB8 and Xing He, are being supplied to exTV. TVBN is a 24-hour news channel produced at the TVB News Centre. TVBE is an entertainment channel featuring acquired as well as TVB-produced dramas and non-drama programmes. By day, TVBQ delivers children's programming, and family informational and entertainment in the evenings. TVB8 and Xing He, broadcasting mainly in Putonghua, are presently produced by TVB Satellite Broadcasting Limited principally for international broadcast and distribution in the mainland and overseas.

FINANCIAL REVIEW

(a) Investments in Subsidiary Companies and Associates

On 19 February 2003, in compliance with conditions in the Domestic Free Television Programme Service Licence, the Company reduced to below 50% its interest in a wholly owned subsidiary company, Galaxy Satellite Broadcasting Limited ("GSBL"). GSBL holds a licence to operate Pay TV services in Hong Kong and is now reclassified as an associated company in these accounts submitted. The disposal has brought to the Group a profit of HK$5.2 million.

According to the Subscription & Shareholders Agreement entered into with Intelsat Hong Kong Limited, the cost of investment in Galaxy Satellite TV Holding Limited (which owns 100% in GSBL) is to be paid over a period of four years. In these accounts, the full cost of HK$520 million is stated as investment in an associated company and the amount of outstanding capital contribution of HK$382 million is shown as amounts due to an associate.

On 30 November 2001, MEASAT Broadcast Network System (BVI) Ltd. ("MBNS(BVI)") and Home Net N.V. ("HomeNet") were each issued 4,500,000 shares of TVB.COM Limited ("TVB.COM") unpaid at HK$8.60 per share. These shares, which did not carry voting and dividend rights until paid for, were to be paid for by four equal instalments. Two of these instalments were received by the end of February 2003, thus increasing MBSN(BVI)'s interest in TVB.COM to 18.42% and HomeNet's interest to 7.9%. This transaction is accounted for as a deemed disposal of the group's interest in TVB.COM resulting in a profit of HK$27.7 million. TVB.COM changed its name to TVB Publishing Holding Limited on 12 December 2001.

The Company has increased during the year its interest in a Taiwan associate, Interface Co. Ltd. ("Interface"), to a cumulative percentage of 64.76%. Interface is therefore reclassified as a subsidiary company in these accounts. There is goodwill of HK$8.9 million arising from the purchase which is to be amortised on a straight-line basis over 5 years.

To obtain complete control for long term business development in the European market, the Company, on 23 October 2003, acquired from the minority shareholders their entire 36% interest in The Chinese Channel (Holdings) Limited ("TCC"), for a consideration of HK$5 million, thus increasing the Company's interest in TCC group of companies to 100%. This has resulted in goodwill of HK$56 million which is to be amortised evenly over 10 years starting November 2003.

Apart from those reported above, there was no other material acquisition or disposal of subsidiaries and associated companies during the year.

(b) Capital Assets, Liquidity and Debts

The new TVB City Project has been completed and all capital expenditures incurred are reflected in the accounts for the year. As at 31 December 2003, fixed assets of the Group stood at HK$2,365 million, an increase over last year end by HK$198 million which is net of the effect of the de-consolidation of GSBL and its related fixed assets. The increase represents CAPEX for the TVB City Project and also for the Channel Supply Agreement entered into with GSBL on 4 September 2001 through an open bidding process for supply of five Pay TV programme channels.

Cash and bank balances as at 31 December 2003 stood at HK$362 million, comparable to the position of last year. It reflects the HK$138 million cash investment in the Pay TV Joint Venture paid on 20 February 2003 and the CAPEX paid during the year. About 40% of the cash balance was maintained in overseas subsidiaries for their daily operation and 30% in accounts for specially assigned purposes. To finance current working capital requirements, sufficient banking facilities have been arranged. Cash and cash equivalents held by the Group were principally in Hong Kong Dollars and US Dollars and were not related to debts.

Accounts receivable increased by 3% from the position at the end of the previous year, reflecting a higher level of billing for local advertising at year end. Adequate provision has been set up to allow for any anticipated recoverability issues. Accounts payable decreased over last year by 11%, reflecting a higher payout during year.

The Group recorded a gearing ratio of 18.7% as of 31 December 2003 (2002: 10.8%) which was measured by total debts of HK$618 million (December 2002: HK$356 million) against a shareholders' fund of HK$3,295 million (December 2002: HK$3,274 million). The increase was due to additional bank loans drawn mainly to finance the Pay TV Joint Venture and also the New TVB City Project.

- Debts increased over last year by HK$262 million due to the aforesaid additional short-term loans.

- Debts consisted of short and long-term bank loans and bank overdrafts taken out for purchase of properties, equipment and studio facilities in Taiwan and the new TVB City Project, etc. Loans totalling HK$85 million (December 2002: HK$162 million) were secured by assets of subsidiary companies.

- All debts are subject to floating rates of interest at an agreed percentage above the prevailing lending rates of the banks.

- The debt maturity profile as at 31 December 2003 was as follows: within one year HK$561 million (91%); in the second year HK$9 million (1%); in the third to fifth years HK$17 million (3%) and after the fifth year HK$31 million (5%).

- Debts were denominated mainly in Hong Kong Dollars (73%), New Taiwan Dollars (25%), British Pounds (1%) and other currencies, such as US and Australian Dollars.

- The Group had no committed borrowing facilities during the year.

Capital commitments of the Group, excluding the Group's share of commitments for jointly controlled entities, decreased by 60% to HK$243 million (December 2002: HK$606 million).

(c) Major Provisions and Write-off

The Group has a contractual commitment for transponder capacity (36 MHz) on AMC4 (beaming over the USA, including Hawaii) provided by SES Americom for a period of 10 years to 30 September 2012. Following the migration of our satellite platform to DirecTV in USA, this transponder capacity became redundant. Memorandums of Understanding have been signed with channel operators and operators of broadcasting platforms which we anticipate will lead to the signing of subleases, at prevailing market rates, covering the full original transponder capacity. These sublease rates are expected to be lower than the rates in our original transponder lease. Accordingly, a provision of HK$54 million has been set up in these accounts to cover the shortfall between our original lease obligation and the anticipated revenue from subleases through to the end of the original contract term.

Likewise, there was about 9 MHz of redundant capacity on a 54 MHz PAS-8 C Band transponder provided by PanAmSat, beaming over Asia, the west coast of the USA and northern Australia. A provision of HK$9 million was set up to address outstanding contractual liabilities to 31 March 2006.

The Company vacated premises at Shaw House (Clear Water Bay) when it moved to the new TVB City at Tseung Kwan O. However, the relevant tenancy leases for these Shaw House premises will end only as of 30 June 2005. Accordingly, we have provided a sum of HK$32 million in the accounts to cover these lease obligations from 1 January 2004 to 30 June 2005, less amounts receivables from subleases.

On 30 September 2003, Hsin Chi Broadcast Co. Ltd. ("Hsin Chi") ceased business. Instead of putting the company into liquidation, it was decided that the capital of the company should be reduced after selling assets and paying off liabilities. The company is now posted for sale as a shell company holding just the DTH licence for the Taiwan market. Hsin Chi is owned 57.14% by Liann Yee Production Co. Ltd. ("LYP"), a 70% owned subsidiary of the Company. A loss of NT$208 million has been taken up in the accounts of LYP and impact to the Group is reduced to about HK$20 million, after tax.

(d) Contingent Liabilities

There were guarantees to the extent of HK$1.1 million (December 2002: HK$89.6 million) provided to bankers for banking facilities. The HK$88 million bank guarantee for the performance bond issued to the HKSAR Government has been uplifted and replaced by security provided by the new holding company of GSBL. The Company now owns only 49% of GSBL.

(e) Exposure to Fluctuation in Exchange Rates and Related Hedges

As of 31 December 2003, exchange contracts, entered into with bankers to sell forward certain foreign currencies in order to hedge against fluctuation for trade receipts from overseas customers, amounted to HK$15.5 million. There was a potential loss on these contracts of HK$0.8 million which has not been recognised in the accounts.

HUMAN RESOURCES

As of 31 December 2003, the Group employed, excluding directors and freelance workers but including contract artistes and staff in overseas subsidiary companies, a total of 5,242 (December 2002: 5,039) full-time employees. The increase was due to additional manpower required for production of programmes for GSBL. About 26% of these were employed in overseas subsidiaries and were paid on a scale and system relevant to their localities and local legislation. For local employment, different pay schemes are operated for contract artistes, sales and non-sales employees. Contract artistes are paid either on a per-show basis or by a package of shows. Sales personnel are remunerated based on on-target-earning packages comprised of salary and sales commission. Non-sales personnel are offered a monthly salary. The year end bonus equivalent to one month's salary was withdrawn from 1 January 2002. There was no share option scheme adopted by the Group during the year. From time to time, the Group organises, either in house or with vocational institutions, seminars, courses and workshops on subjects of technical interest, industry safety, management skills and related studies, apart from sponsorship of training programmes that employees may enroll on their own initiatives.