Management Discussion and Analysis

A. Review of 2003 Operating Results

The Group continued to grow its Pay TV and broadband subscriber base and improve its profitability in 2003, as growth momentum picked up in the second half of the year with the economic recovery after a challenging first half.

Consolidated turnover decreased slightly by HK$18 million to HK$2,143 million reflecting a HK$23 million increase in Pay TV turnover and a HK$41 million decline in Internet & Multimedia turnover.

Operating costs before depreciation decreased by 5% to HK$1,354 million due to significant programming cost savings this year as a result of stringent cost control and the non-recurring World Cup related costs incurred in 2002. Network and other operating costs increased marginally by 3% to HK$361 million due to increases in network operating and maintenance costs. Selling, general and administrative expenses remained relatively stable at HK$343 million.

Depreciation rose by 7% to HK$539 million due to further capital investments in digital set-top boxes, cable modems and related network equipment to cater for subscriber growth and services enhancement. Profit from operations rose by HK$24 million or 11% to HK$251 million.

The HK$47 million decline in finance costs and the HK$18 million reduction in interest income were mainly due to the early partial redemption of the fixed rate convertible bonds in October 2002. There was no impairment loss on investments during the year. Non-operating expenses of HK$10 million mainly represented loss on disposal of fixed assets.

Profit before taxation increased by 99% to HK$234 million. A HK$13 million non-recurring charge was made for additional profits tax payable on the Group's leveraged leasing transactions, following the increase in profits tax rate from 16% to 17.5% during the year.

Net profit attributable to shareholders for 2003 thus rose HK$103 million year-on-year to HK$220 million.

Basic earnings per share were 10.9 cents as compared to 5.8 cents in 2002.

B. Segmental Information

Pay Television

Subscribers grew by 50,000 to reach 656,000. The increase was the largest annual increase in the past 3 years. Benefiting from the economic rebound, subscriber growth momentum picked up in the second half of 2003 as net additions exceeded 30,000 notwithstanding the services launched by new competitors. ARPU declined by 6% year-on-year to HK$220 partly due to the absence of 2002 World Cup related revenue. Turnover increased by 1% to HK$1,734 million. Operating costs before depreciation declined by 8% to HK$1,001 million also due to the absence of World Cup while depreciation dropped by 3% as certain fixed assets became fully depreciated. As a result, EBITDA grew by 17% to HK$733 million and operating profit increased by 34% to HK$444 million.

Internet & Multimedia

Subscribers grew by 32,000 to surpass 258,000. Subscriber growth moderated as residential broadband market penetration has now surpassed 50%. ARPU declined 28% to HK$129 and turnover declined by HK$41 million to HK$409 million. However, both ARPU and revenue have started to recover in the second half of 2003. As a result of the drop in revenue, EBITDA declined by 24% to HK$159 million and an operating loss of HK$85 million was incurred on a full cost allocation basis. On an incremental basis, this business segment has continued to be profitable in 2003.

C. Liquidity and Financial Resources

The Group applied its surplus funds and cash generated from operations to fully redeem the fixed rate convertible bonds and repay its bank borrowings during the year. As of December 31, 2003, the Group was debt-free with surplus cash of HK$29 million.

The Group's cash and cash equivalents were denominated in Hong Kong dollars, and its other assets, liabilities, revenue and expenses were mainly denominated in Hong Kong dollars or U.S. dollars. The book value of consolidated net assets of the Group as at December 31, 2003 was HK$1,685 million, or HK$0.83 per share.

Capital expenditure for the year amounted to HK$437 million as compared to HK$559 million in the previous year. Major items included investments on digital set-top boxes and cable modems and related equipment, and further network upgrade and expansion expenditure. These items are expected to continue to be the major areas of the Group's capital expenditure in 2004.

The Group is comfortable with its present liquidity and financial positions. Cash to be generated from our operations and other external sources of funds are expected to be adequate to fund known upcoming capital expenditure and working capital requirements.

D. Contingent liabilities

At December 31, 2003, there were contingent liabilities in respect of guarantees, indemnities and letters of awareness given by the Company on behalf of subsidiaries relating to overdraft and guarantee facilities of banks up to HK$185 million, of which only HK$55 million was utilised by the subsidiaries.

The Group is in discussion with the Inland Revenue Department regarding the deductibility of certain interest payments claimed in previous years' tax computations with estimated maximum net exposure to the Group of HK$42 million at December 31, 2003. Good progress has been made in the discussion with the IRD and management is confident that there are ample grounds to support the deductibility of the interest expenses in dispute.

E. Human Resources

The Group had a total of 2,847 employees at the end of 2003. Total salaries and related costs incurred in the year under review amounted to HK$728 million.

Through a focused set of initiatives in the areas of human resources development, the work environment, strategic change and rewards programs, we are striving to build a strong, committed and engaged workforce.

Our pay-for-performance culture has been in place to incentivize and reward employee performance that will lead to a long-term enhancement of the overall calibre of the Group.