

Report of the Directors

The directors present their annual report together with the audited consolidated financial statements of PCCW Limited (the “Company”) and its subsidiaries (the “Group”) for the year ended December 31, 2004.

PRINCIPAL ACTIVITIES

The principal activities of 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.

Details of segment information are set out in note 5 to the consolidated financial statements.

RESULTS AND APPROPRIATIONS

The results of the Group for the year ended December 31, 2004 are set out in the accompanying consolidated financial statements on page 65.

An interim dividend of 5.5 HK cents per ordinary share, totaling approximately HK\$295 million, was paid to shareholders of the Company in November 2004.

The board of directors (the “Board”) recommends the payment of a final dividend of 9.6 HK cents per ordinary share for the year ended December 31, 2004 to shareholders whose names appear on the Register of Members of the Company on May 23, 2005 and payable on or around May 31, 2005. The Register of Members will be closed from May 19, 2005 to May 23, 2005, both days inclusive.

FINANCIAL SUMMARY

A summary of the consolidated results and of the assets and liabilities of the Group for the last five financial years is set out on page 126.

SUBSIDIARIES, JOINTLY CONTROLLED COMPANIES AND ASSOCIATES

Particulars of the Company’s principal subsidiaries, jointly controlled companies and associates are set out in notes 21 to 23 to the consolidated financial statements.

FIXED ASSETS

Details of movements in the fixed assets of the Group during the year are set out in note 17 to the consolidated financial statements.

BORROWINGS AND CONVERTIBLE BONDS

Particulars of the Group’s and the Company’s borrowings and convertible bonds are set out in notes 25(g) and 26 to the consolidated financial statements.

SHARE CAPITAL

Details of the movements in the share capital of the Company during the year are set out in note 28 to the consolidated financial statements.

Pursuant to the ordinary resolution passed on March 16, 2005, the authorized share capital of the Company was increased to HK\$2.5 billion divided into 10 billion ordinary shares of HK\$0.25 each.

RESERVES

Details of the movements in reserves of the Group and the Company during the year are set out in note 31 to the consolidated financial statements.

MAJOR CUSTOMERS AND SUPPLIERS

For the year ended December 31, 2004, the aggregate amount of turnover attributable to the Group's five largest customers represented less than 30% of the Group's total turnover.

The largest supplier for the year ended December 31, 2004 represented 18% of the Group's total purchases (not including purchases of a capital nature), and the combined total of the five largest suppliers accounted for 37% of the Group's total purchases for the year. None of the directors, their associates or any shareholder of the Company, who to the knowledge of the directors, owns more than 5% of the Company's share capital, had any interests in these major suppliers.

DIRECTORS

The directors who held office during the year and up to the date of this report were:

Executive Directors

Li Tzar Kai, Richard *Chairman*

So Chak Kwong, Jack *Deputy Chairman and Group Managing Director*

Yuen Tin Fan, Francis *Deputy Chairman*

Peter Anthony Allen

Alexander Anthony Arena

Chung Cho Yee, Mico

Lee Chi Hong, Robert

Cheung Wing Lam, Linus *Deputy Chairman* (resigned on February 29, 2004)

Michael John Butcher (resigned on August 26, 2004)

Non-Executive Director

Sir David Ford, KBE, LVO

Independent Non-Executive Directors

Professor Chang Hsin-kang

Dr Fung Kwok King, Victor

Dr The Hon Li Kwok Po, David, GBS, JP

Sir Roger Lobo, CBE, LLD, JP

Aman Mehta (appointed on February 10, 2004)

The Hon Raymond George Hardenbergh Seitz (re-designated on February 1, 2005)

In accordance with Articles 101A, 101B and 101C of the Company's Articles of Association, Yuen Tin Fan, Francis, Professor Chang Hsin-kang, Dr Fung Kwok King, Victor and The Hon Raymond George Hardenbergh Seitz shall retire by rotation and, being eligible, offer themselves for re-election at the forthcoming annual general meeting.

INDEPENDENT NON-EXECUTIVE DIRECTORS

The Company has received from each of its independent non-executive directors an annual confirmation of his independence pursuant to Rule 3.13 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules") and considers the independent non-executive directors to be independent.

DIRECTORS' SERVICE CONTRACTS

So Chak Kwong, Jack entered into a service contract with the Company for a period of 3 years commencing on July 25, 2003. So Chak Kwong, Jack's service contract provides for a compensation payment from the Company for early termination by the Company during the term of the contract.

Save as disclosed above, no director proposed for re-election at the forthcoming annual general meeting has an unexpired service contract with the Group which is not determinable by the Group within one year without payment of compensation (other than statutory compensation).

DIRECTORS' AND CHIEF EXECUTIVE'S INTERESTS AND SHORT POSITIONS IN SHARES, UNDERLYING SHARES AND DEBENTURES OF THE COMPANY AND ITS ASSOCIATED CORPORATIONS

As at December 31, 2004, the directors and chief executive of the Company and their associates had the following interests and short positions in the shares, underlying shares and debentures of the Company and its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance (the "SFO")) as recorded in the register required to be kept under Section 352 of the SFO or as otherwise notified to the Company and The Stock Exchange of Hong Kong Limited (the "Stock Exchange") pursuant to the Model Code for Securities Transactions by Directors of Listed Companies (the "Model Code") of the Listing Rules:

1. The Company

(A) Interests in the Company

The table below sets out the aggregate long positions in the shares and underlying shares of each director and the chief executive of the Company.

Name of Directors/ Chief Executive	Personal interests	Number of ordinary shares			Number of underlying shares held under equity derivatives	Total	Percentage of issued share capital
		Family interests	Corporate interests	Other interests			
Li Tzar Kai, Richard	–	–	4,709,600 <i>(Note 1(a))</i>	1,746,122,668 <i>(Note 1(b))</i>	3,490,018 <i>(Note 1(c))</i>	1,754,322,286	32.64%
So Chak Kwong, Jack	2,161,000	–	–	–	16,322,000 <i>(Note 3)</i>	18,483,000	0.34%
Yuen Tin Fan, Francis	–	–	–	–	17,068,000 <i>(Note 2)</i>	17,068,000	0.32%
Peter Anthony Allen	253,200	–	–	–	2,629,200 <i>(Note 2)</i>	2,882,400	0.05%
Alexander Anthony Arena	760,000	–	–	–	12,800,200 <i>(Note 4)</i>	13,560,200	0.25%
Chung Cho Yee, Mico	1,176,260	18,455 <i>(Note 5)</i>	–	–	11,390,400 <i>(Note 2)</i>	12,585,115	0.23%
Lee Chi Hong, Robert	992,600 <i>(Note 6(a))</i>	511 <i>(Note 6(b))</i>	–	–	5,000,000 <i>(Note 2)</i>	5,993,111	0.11%
Sir David Ford	–	–	–	–	2,000,000 <i>(Note 2)</i>	2,000,000	0.04%
Prof Chang Hsin-kang	64,000	–	–	–	–	64,000	0.001%
Dr The Hon Li Kwok Po, David	600,000	–	–	–	–	600,000	0.01%

DIRECTORS' AND CHIEF EXECUTIVE'S INTERESTS AND SHORT POSITIONS IN SHARES, UNDERLYING SHARES AND DEBENTURES OF THE COMPANY AND ITS ASSOCIATED CORPORATIONS (CONTINUED)

1. The Company (continued)

(A) Interests in the Company (continued)

Notes:

1. (a) These interests were held by Pacific Century Diversified Limited ("PCD"), a wholly-owned subsidiary of Chiltonlink Limited, which was 100% owned by Li Tzar Kai, Richard.
- (b) These interests represented:
 - (i) a deemed interest in 36,726,857 shares of the Company held by Yue Shun Limited, a subsidiary of Hutchison Whampoa Limited ("HWL"). Cheung Kong (Holdings) Limited ("Cheung Kong") through certain subsidiaries held more than one-third of the issued share capital of HWL. Li Tzar Kai, Richard was a beneficiary of certain discretionary trusts which held interests in Cheung Kong and HWL. Li Tzar Kai, Richard was also interested in one-third of the issued share capital of two companies, which owned all the shares in the trustee companies which acted as trustees of such discretionary trusts. Accordingly, Li Tzar Kai, Richard was deemed, under the SFO, to have an interest in the 36,726,857 shares of the Company held by Yue Shun Limited;
 - (ii) a deemed interest in 20,354,286 shares of the Company held by Pacific Century Group Holdings Limited ("PCGH"). Li Tzar Kai, Richard was the founder of certain trusts which held 100% interests in PCGH. Accordingly, Li Tzar Kai, Richard was deemed, under the SFO, to have an interest in the 20,354,286 shares of the Company;
 - (iii) a deemed interest in 1,526,094,301 shares of the Company held by Pacific Century Regional Developments Limited ("PCRD"), a company in which PCGH had, through certain wholly-owned subsidiaries including Anglang Investments Limited, Pacific Century Group (Cayman Islands) Limited, Pacific Century International Limited and Borsington Limited, an aggregate 75.33% interest. Li Tzar Kai, Richard was the founder of certain trusts which held 100% interests in PCGH. Accordingly, Li Tzar Kai, Richard was deemed, under the SFO, to have an interest in the 1,526,094,301 shares of the Company; and
 - (iv) a deemed interest in 162,947,224 shares of the Company held by a collective investment scheme in which PCD (a corporation 100% controlled by Li Tzar Kai, Richard – see above) was a holder.
- (c) This number represents interests under listed equity derivatives arising through corporations controlled by PCGH in which Li Tzar Kai, Richard was deemed interested as the founder of certain trusts which held 100% of PCGH and comprises:
 - (i) an interest in 679,000 underlying shares held by PCRD in the form of 67,900 American depositary receipts ("ADRs"), each representing 10 shares of the Company; and
 - (ii) an interest in respect of 2,811,018 underlying shares arising as a result of the holding of an aggregate of US\$14,000,000 of convertible bonds issued by a wholly-owned subsidiary of the Company which were held by PCGH and a wholly-owned subsidiary of Pacific Century Insurance Holdings Limited ("PCIHL") (a company in which PCRD had a 45.11% interest) and were convertible into 2,811,018 shares of the Company.
2. These interests represented the interests in underlying shares in respect of share options granted by the Company to these directors as beneficial owners, the details of which are set out in the section headed "SHARE OPTION SCHEMES" below.
3. These interests represented So Chak Kwong, Jack's beneficial interest in: (i) 4,322,000 underlying shares which will be transferred to him in two equal annual installments commencing from the second anniversary of his employment with the Company pursuant to an agreement made with PCD which constituted unlisted physically settled equity derivatives; and (ii) 12,000,000 underlying shares in respect of share options granted by the Company to So Chak Kwong, Jack as beneficial owner, the details of which are set out in the section headed "SHARE OPTION SCHEMES".
4. These interests represented Alexander Anthony Arena's beneficial interest in: (i) 200 underlying shares held in the form of 20 ADRs which constituted listed equity derivatives; and (ii) 12,800,000 underlying shares in respect of share options granted by the Company to Alexander Anthony Arena as beneficial owner, the details of which are set out in the section headed "SHARE OPTION SCHEMES" below.
5. These shares were held by the spouse of Chung Cho Yee, Mico.
6. (a) These shares were held jointly by Lee Chi Hong, Robert and his spouse.
- (b) These shares were held by the spouse of Lee Chi Hong, Robert.

(B) Short Positions in the Shares and Underlying Shares of the Company

Under the SFO, Li Tzar Kai, Richard was taken as at December 31, 2004 to have short positions held pursuant to equity derivatives in respect of an aggregate of 325,498,469 underlying shares, representing 6.06% of the total issued share capital of the Company, details of which are as follows:

- (a) a short position in respect of 91,764,705 underlying shares in the Company (such shares being beneficially held by PCRD) which arose under certain unlisted physically settled equity derivatives issued by PCRD pursuant to which the derivative holder has the right to call for the delivery of 91,764,705 shares in the Company. Li Tzar Kai, Richard's deemed short position arose as the founder of certain trusts which held 100% of PCGH of which PCRD is a controlled corporation under the SFO;

DIRECTORS' AND CHIEF EXECUTIVE'S INTERESTS AND SHORT POSITIONS IN SHARES, UNDERLYING SHARES AND DEBENTURES OF THE COMPANY AND ITS ASSOCIATED CORPORATIONS (CONTINUED)

1. The Company (continued)

(B) Short Positions in the Shares and Underlying Shares of the Company (continued)

- (b) a short position in respect of 229,411,764 underlying shares in the Company (such shares being beneficially held by PCR D) which arose under certain unlisted physically settled equity derivatives issued by PCR D pursuant to which the derivative holders have the right to call for the delivery of 229,411,764 shares in the Company. Li Tzar Kai, Richard's deemed short position arose as the founder of certain trusts which held 100% of PCGH of which PCR D is a controlled corporation under the SFO; and
- (c) through PCD (a corporation 100% controlled by Li Tzar Kai, Richard – see above) a short position in respect of 4,322,000 underlying shares in the Company which arose under an agreement entered into with So Chak Kwong, Jack, such interest constituted, for the purposes of the SFO, a short position of a corporation controlled by Li Tzar Kai, Richard under an unlisted physically settled equity derivative pursuant to which such shares in the Company will be transferred to So Chak Kwong, Jack in two equal annual installments commencing from the second anniversary of his employment with the Company.

2. Interests in Associated Corporations

(A) PCCW Capital Limited

PCGH and a subsidiary of PCIHL held, respectively, US\$4,000,000 and US\$10,000,000 of convertible bonds issued by PCCW Capital Limited, an associated corporation of the Company. Accordingly, Li Tzar Kai, Richard was deemed to have an aggregate interest in US\$14,000,000 of convertible bonds issued by PCCW Capital Limited by virtue of being the founder of certain trusts which held 100% of PCGH.

(B) Pacific Century Premium Developments Limited (“PCPD”)

The table below sets out the aggregate long positions in the shares and underlying shares of PCPD held by the directors and chief executive of the Company.

Name of Directors/ Chief Executive	Personal interests	Number of ordinary shares			Number of underlying shares held under equity derivatives	Total	Percentage of issued share capital
		Family interests	Corporate interests	Other interests			
So Chak Kwong, Jack	–	–	–	–	5,000,000	5,000,000	0.27%
Chung Cho Yee, Mico	–	–	–	–	5,000,000	5,000,000	0.27%

The above interests represented the interests in underlying shares in respect of share options granted by PCPD to the directors and chief executive of the Company as beneficial owners pursuant to its share option scheme, the details of which are set out in the section headed “SHARE OPTION SCHEMES”.

Save as disclosed above, none of the directors or chief executive of the Company or their associates had any interests or short positions in any shares, underlying shares and debentures of the Company or any of its associated corporations (within the meaning of Part XV of the SFO) as recorded in the register required to be kept under Section 352 of the SFO or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code of the Listing Rules.

SHARE OPTION SCHEMES

The Company adopted a share option scheme on September 20, 1994 (the “1994 Scheme”) and unless otherwise canceled or amended, it is valid and effective for 10 years from that date. The 1994 Scheme was amended at an extraordinary general meeting of the Company held on May 23, 2002 in order to, amongst other things, comply with the requirements of Chapter 17 of the Listing Rules which came into effect on September 1, 2001. At the annual general meeting of the Company held on May 19, 2004, the shareholders of the Company approved the termination of the 1994 Scheme and adoption of a new share option scheme (the “2004 Scheme”). The 2004 Scheme will remain in force for 10 years from the date of its adoption, unless otherwise canceled or amended.

The Company operates share option schemes namely the 1994 Scheme and the 2004 Scheme (collectively the “Schemes”) under which the board of directors (the “Board”) may, at its discretion, grant share options to any eligible person to subscribe for shares in the Company subject to the terms and conditions stipulated therein. Following the termination of the 1994 Scheme during 2004, no further share options will be granted under such scheme, but in all other respects the provisions of such scheme will remain in full force and effect.

The Schemes provide an opportunity for eligible persons to acquire proprietary interests in the Company and to encourage eligible persons to work towards enhancing the value of the Company and its shares for the benefit of the Company and its shareholders as a whole. Eligible persons include, but are not limited to, any director, officer, employee, consultant, adviser, supplier, customer or sub-contractor of the Group or any member of it or any other person who has contributed to the development, growth or benefit of the Group as determined by the Board.

The maximum number of shares in respect of which options may be granted under the 2004 Scheme shall not in aggregate exceed 10% of the shares of the Company in issue as at the date of approval of such scheme. As at December 31, 2004, the total number of shares of the Company that may be issued upon exercise of all share options granted and yet to be exercised under the 1994 Scheme was 178,742,716, which represented 3.33% of the issued share capital of the Company as at that date. No share options have been granted under the 2004 Scheme during the year ended December 31, 2004 since its adoption, and no share options were outstanding at December 31, 2004 under such scheme. The maximum entitlement for any eligible person (other than a substantial shareholder or an independent non-executive director of the Company, or any of their respective associates) under the Schemes is that the total number of shares issued and to be issued upon exercise of all options granted and to be granted in any 12-month period up to and including the date of the latest grant does not exceed 1% of the shares of the Company in issue at the relevant time. Any further grant of share options in excess of this limit is subject to shareholders’ approval in general meeting.

The period within which an option may be exercised under each of the Schemes will be determined by the Board in its absolute discretion, save that no option may be exercised later than 10 years from the date of grant of the option.

Under each of the Schemes, 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 closing price of the shares as stated in the Stock Exchange’s daily quotations sheet on the date of grant of such option; (ii) the average closing price of the shares as stated in the Stock Exchange’s daily quotations sheets for the five trading days immediately preceding the date of grant of such option; and (iii) the nominal value of a share on the date of grant of such option.

Details of the share options which have been granted under the 1994 Scheme of the Company during the year ended December 31, 2004 are as follows:

1. Outstanding options at January 1, 2004 and at December 31, 2004

Name or category of participant	Date of grant (Notes 1 & 2)	Vesting period (Note 1)	Exercisable period (Note 1)	Exercise price HK\$	Number of options Outstanding at 01.01.2004	Number of options Outstanding at 12.31.2004
Directors/Chief Executive						
So Chak Kwong, Jack	07.25.2003	07.25.2004 to 07.25.2006	07.25.2004 to 07.23.2013	4.3500	12,000,000	12,000,000

SHARE OPTION SCHEMES (CONTINUED)

1. Outstanding options at January 1, 2004 and at December 31, 2004 (continued)

Name or category of participant	Date of grant (Notes 1 & 2)	Vesting period (Note 1)	Exercisable period (Note 1)	Exercise price HK\$	Number of options	
					Outstanding at 01.01.2004	Outstanding at 12.31.2004
Directors/Chief Executive (continued)						
Yuen Tin Fan, Francis	08.28.1999	08.17.2000 to 08.17.2004	08.17.2003 to 08.17.2009	11.7800	2,134,000	2,134,000
	08.26.2000	08.26.2001 to 08.26.2005	08.26.2001 to 08.26.2010	60.1200	3,200,000	3,200,000
	02.20.2001	08.26.2001 to 08.26.2005	08.26.2001 to 01.22.2011	16.8400	3,200,000	3,200,000
	07.25.2003	07.25.2004 to 07.25.2006	07.25.2004 to 07.23.2013	4.3500	8,534,000	8,534,000
Peter Anthony Allen	08.28.1999	08.17.2000 to 08.17.2002	08.17.2000 to 08.17.2009	11.7800	272,000	272,000
	08.26.2000	08.26.2001 to 08.26.2005	08.26.2001 to 08.26.2010	60.1200	178,600	178,600
	02.20.2001	08.26.2001 to 08.26.2005	08.26.2001 to 01.22.2011	16.8400	178,600	178,600
	07.25.2003	07.25.2004 to 07.25.2006	07.25.2004 to 07.23.2013	4.3500	2,000,000	2,000,000
Alexander Anthony Arena	08.28.1999	08.17.2000 to 08.17.2004	08.17.2000 to 08.17.2009	11.7800	3,200,000	3,200,000
	08.26.2000	08.26.2001 to 08.26.2005	08.26.2001 to 08.26.2010	60.1200	1,600,000	1,600,000
	02.20.2001	08.26.2001 to 08.26.2005	08.26.2001 to 01.22.2011	16.8400	1,600,000	1,600,000
	07.25.2003	07.25.2004 to 07.25.2006	07.25.2004 to 07.23.2013	4.3500	6,400,000	6,400,000
Chung Cho Yee, Mico	08.28.1999	08.17.2000 to 08.17.2004	08.17.2001 to 08.17.2009	11.7800	3,575,200	3,575,200
	08.26.2000	08.26.2001 to 08.26.2005	08.26.2001 to 08.26.2010	60.1200	1,060,000	1,060,000
	02.20.2001	08.26.2001 to 08.26.2005	08.26.2001 to 01.22.2011	16.8400	1,060,000	1,060,000
	07.25.2003	07.25.2004 to 07.25.2006	07.25.2004 to 07.23.2013	4.3500	5,695,200	5,695,200
Lee Chi Hong, Robert	07.25.2003	07.25.2004 to 07.25.2006	07.25.2004 to 07.23.2013	4.3500	5,000,000	5,000,000
Sir David Ford	07.25.2003	07.25.2004 to 07.25.2006	07.25.2004 to 07.23.2013	4.3500	2,000,000	2,000,000
Cheung Wing Lam, Linus	02.20.2001	08.26.2001 to 08.26.2005	08.26.2001 to 01.22.2011	16.8400	3,200,000	(Note 9)
Michael John Butcher	05.28.2002	04.29.2003 to 04.29.2007	04.29.2003 to 04.29.2012	9.9500	5,600,000	(Note 10)
	07.25.2003	07.25.2004 to 07.25.2006	07.25.2004 to 07.23.2013	4.3500	8,000,000	(Note 10)

SHARE OPTION SCHEMES (CONTINUED)**1. Outstanding options at January 1, 2004 and at December 31, 2004 (continued)**

Name or category of participant	Date of grant (Notes 1 & 2)	Vesting period (Note 1)	Exercisable period (Note 1)	Exercise price HK\$	Number of options	
					Outstanding at 01.01.2004	Outstanding at 12.31.2004
Employees						
In aggregate	08.17.1999 to 09.15.1999	(Note 3)	08.17.2000 to 08.17.2009	11.7800	10,343,988	9,691,190
	10.25.1999 to 11.23.1999	(Note 3)	10.25.2000 to 10.25.2009	22.7600	4,509,200	3,432,400
	02.08.2000 to 03.08.2000	02.08.2001 to 02.08.2003	02.08.2001 to 02.08.2010	75.2400	86,700	86,700
	08.26.2000 to 09.24.2000	(Note 4)	(Note 4)	60.1200	4,270,000	3,908,000
	10.27.2000 to 11.25.2000	(Note 5)	(Note 5)	24.3600	12,966,082	11,085,070
	01.22.2001 to 02.20.2001	(Note 6)	(Note 6)	16.8400	13,559,838	11,156,718
	02.20.2001	02.08.2002 to 02.08.2004	02.08.2002 to 02.08.2011	18.7600	86,700	86,700
	04.17.2001 to 05.16.2001	(Note 7)	(Note 7)	10.3000	3,542,960	1,324,360
	07.16.2001 to 09.15.2001	07.16.2002 to 07.16.2004	07.16.2002 to 07.16.2011	9.1600	689,760	648,600
	09.27.2001	09.27.2001 to 09.07.2003	09.27.2001 to 09.07.2011	6.8150	3,600,000	–
	10.15.2001 to 11.13.2001	10.15.2002 to 10.15.2004	10.15.2002 to 10.15.2011	8.6400	292,000	292,000
	05.10.2002	(Note 3)	04.11.2003 to 04.11.2012	7.9150	231,700	231,700
	06.19.2002	(Note 8)	(Note 8)	10.0900	279,000	179,000
	08.01.2002	08.01.2003 to 08.01.2005	08.01.2003 to 07.31.2012	8.0600	200,000	200,000
	11.13.2002	11.13.2003 to 11.13.2005	11.13.2003 to 11.12.2012	6.1500	7,040,000	6,860,000
	07.25.2003	07.25.2004 to 07.25.2006	07.25.2004 to 07.23.2013	4.3500	75,722,000	62,082,678
	09.16.2003	09.16.2004 to 09.15.2006	09.16.2004 to 09.14.2013	4.9000	1,190,000	1,190,000
Others	02.20.2001	Fully Vested on 01.22.2002	01.22.2002 to 01.31.2004	16.8400	480,000	–
	10.11.2002	Fully vested on 10.11.2002	10.11.2002 to 10.10.2007	8.6165	1,200,000	1,200,000
	07.25.2003	07.25.2004 to 07.25.2006	07.25.2004 to 07.23.2013	4.3500	2,200,000	2,200,000

SHARE OPTION SCHEMES (CONTINUED)**2. Options granted during the year ended December 31, 2004**

During the year under review, no share options were granted to any directors, chief executive, employees of the Group or other participants.

The share options granted are not recognized in the financial statements until they are exercised. The weighted average values per option granted in 2003 estimated at the date of grant using the trinomial option pricing model was HK\$2.68. The weighted average assumptions used were as follows:

	2004	2003
Risk-free interest rate	–	4.8%
Expected life (in years)	–	10
Volatility	–	0.44
Expected dividend per share	–	–

The trinomial option pricing model was developed for use in estimating the fair value of traded options that are fully transferable. Such an option pricing model requires input of highly subjective assumptions, including the expected stock price volatility. Because the Company's share options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, the trinomial option pricing model does not necessarily provide a reliable measure of the fair value of the share options.

3. Options exercised during the year ended December 31, 2004

Name or category of participant	Date of grant (Notes 1 & 2)	Vesting period (Note 1)	Exercisable period (Note 1)	Exercise Price HK\$	Number of shares acquired on exercise of options	Weighted average closing price of the shares immediately before the date(s) on which the options were exercised HK\$
Employees						
In aggregate	07.25.2003	07.25.2004 to 07.25.2006	07.25.2004 to 07.23.2013	4.3500	5,508,987	5.1407

During the year under review, no share options were exercised by any directors, chief executive, employees of the Group or other participants save as disclosed above.

4. Options canceled or lapsed during the year ended December 31, 2004

Name or category of participant	Exercise price HK\$	Number of options canceled	Number of options lapsed
Directors/Chief Executive			
Cheung Wing Lam, Linus (Note 9)	16.8400	–	3,200,000
Michael John Butcher (Note 10)	9.9500	–	5,600,000
	4.3500	–	8,000,000
Employees			
In aggregate	11.7800	–	652,798 (Note 11)
	22.7600	–	1,076,800
	60.1200	–	362,000
	24.3600	–	1,881,012
	16.8400	–	2,403,120
	10.3000	1,530,000	688,600
	9.1600	–	41,160
	6.8150	3,600,000	–
	10.0900	–	100,000
	6.1500	–	180,000
	4.3500	–	8,130,335
Others	16.8400	–	480,000

SHARE OPTION SCHEMES (CONTINUED)

PCPD, an indirect non-wholly owned subsidiary of the Company, adopted a new share option scheme on March 17, 2003 (the "2003 Scheme"), particulars of which are set out in note 30(d) to the financial statements.

Details of the share options which have been granted to the directors and chief executive of the Company and any other Participant (as defined in note 30(d) to the financial statements) under the 2003 Scheme of PCPD during the year ended December 31, 2004 are as follows:

1. Outstanding options at January 1, 2004 and at December 31, 2004

Name or category of participant	Date of grant (Note 1)	Vesting period (Note 1)	Exercisable period (Note 1)	Exercise price HK\$	Number of options Outstanding at 01.01.2004	Number of options Outstanding at 12.31.2004
Directors/Chief Executive of the Company						
So Chak Kwong, Jack	12.20.2004	Fully vested on 12.20.2004	12.20.2004 to 12.19.2014	2.375	-	5,000,000
Chung Cho Yee, Mico	12.20.2004	Fully vested on 12.20.2004	12.20.2004 to 12.19.2014	2.375	-	5,000,000

As at December 31, 2004, the total number of shares of PCPD that may be issued upon exercise of all share options granted and yet to be exercised under the 2003 Scheme was 10,000,000, which represented 0.53% of the issued share capital of PCPD as at that date.

2. Options granted during the year ended December 31, 2004

Name or category of participant	Date of grant (Note 1)	Vesting period (Note 1)	Exercisable period (Note 1)	Exercise price HK\$	Number of options granted	Closing price of the shares immediately before the date on which the options were granted HK\$
Directors/Chief Executive of the Company						
So Chak Kwong, Jack	12.20.2004	Fully vested on 12.20.2004	12.20.2004 to 12.19.2014	2.375	5,000,000	2.325
Chung Cho Yee, Mico	12.20.2004	Fully vested on 12.20.2004	12.20.2004 to 12.19.2014	2.375	5,000,000	2.325

The share options granted are not recognized in the financial statements until they are exercised. The weighted average values per option granted in 2004 estimated at the date of grant using the trinomial option pricing model was HK\$1.29. The weighted average assumptions used are as follows:

	2004	2003
Risk-free interest rate	3.95%	-
Expected life (in years)	10	-
Volatility	0.50	-
Expected dividend per share	-	-

SHARE OPTION SCHEMES (CONTINUED)**2. Options granted during the year ended December 31, 2004** *(continued)*

The trinomial option pricing model was developed for use in estimating the fair value of traded options that are fully transferable. Such an option pricing model requires input of highly subjective assumptions, including the expected stock price volatility. Because PCPD's share options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, the trinomial option pricing model does not necessarily provide a reliable measure of the fair value of the share options.

3. Options exercised during the year ended December 31, 2004

During the year under review, no share options were exercised by any directors or chief executive of the Company.

4. Options canceled or lapsed during the year ended December 31, 2004

During the year under review, no share options were canceled or lapsed.

Notes:

1. All dates are shown month/day/year.
2. Due to the large number of employees participating in the Scheme, certain information such as the date of grant can only be shown within a reasonable range in this report. For options granted to employees, the options were granted, where applicable, during the underlying periods for acceptance of the offer of such options by the employees concerned.
3. These options vest in installments during a period starting from the first anniversary of the offer date of such options (the "Offer Date") and ending on either the third or fifth anniversary of the Offer Date inclusive.
4. These options vest in installments during a period starting from: (i) May 26, 2001 and ending on May 26, 2003 inclusive; (ii) the first anniversary of the Offer Date and ending on the third anniversary of the Offer Date inclusive; or (iii) the first anniversary of the Offer Date and ending on the fifth anniversary of the Offer Date inclusive. All these options are exercisable in installments from the commencement of the relevant vesting period until the tenth anniversary of the Offer Date.
5. These options vest in installments during a period starting from: (i) March 15, 2001 and ending on March 15, 2005 inclusive; or (ii) the first anniversary of the Offer Date and ending on the third anniversary of the Offer Date inclusive. All these options are exercisable in installments from the commencement of the relevant vesting period until the tenth anniversary of the Offer Date.
6. These options vest in installments during a period starting from: (i) dates ranging between the date of grant to August 26, 2001 and ending on dates ranging between December 7, 2002 to August 26, 2005 inclusive; (ii) the first anniversary of the Offer Date and ending on the third anniversary of the Offer Date inclusive; or (iii) the first anniversary of the Offer Date and ending on the fifth anniversary of the Offer Date inclusive. All these options are exercisable in installments from the commencement of the relevant vesting period until the tenth anniversary of the Offer Date.
7. These options vest in installments during a period starting from: (i) May 26, 2001 and ending on May 26, 2005 inclusive; (ii) the first anniversary of the Offer Date and ending on the third anniversary of the Offer Date inclusive; or (iii) the first anniversary of the Offer Date and ending on the fifth anniversary of the Offer Date inclusive. All these options are exercisable in installments from the commencement of the relevant vesting period until the tenth anniversary of the Offer Date.
8. These options vest in installments during a period starting from: (i) the date of grant and ending on either May 26, 2003 or October 27, 2003 inclusive; or (ii) May 21, 2003 and ending on May 21, 2005 inclusive. All these options are exercisable in installments from the commencement of the relevant vesting period until the tenth anniversary of the Offer Date.
9. Cheung Wing Lam, Linus resigned as a director of the Company on February 29, 2004. His outstanding 3,200,000 options at an exercise price of HK\$16.8400 per share lapsed on March 1, 2004.
10. Michael John Butcher resigned as a director of the Company on August 26, 2004. His outstanding 5,600,000 options and 8,000,000 options at an exercise price of HK\$9.9500 and HK\$4.3500 per share respectively lapsed on November 1, 2004.
11. The number of share options lapsed was adjusted as a result of the discrepancies caused by the share consolidation of the Company on January 8, 2003.

Save as disclosed above, at no time during the year was the Company or any of its subsidiaries, holding companies or fellow subsidiaries a party to any arrangement to enable the directors of the Company to acquire benefits by means of the acquisition of shares in, or debentures of, the Company or any other body corporate and none of the directors or chief executive of the Company or their spouses or children under 18 years of age had any right to subscribe for equity or debt securities of the Company or any of its associated corporations or had exercised any such right during the year.

INTERESTS AND SHORT POSITIONS OF SUBSTANTIAL SHAREHOLDERS

As at December 31, 2004, the following persons (other than directors or chief executive of the Company) were substantial shareholders of the Company (as defined in the Listing Rules) and had interests or short positions in the shares and underlying shares of the Company as recorded in the register required to be kept under Section 336 of the SFO:

(A) Interests and Short Positions of Substantial Shareholders

Name of shareholder	Note	Number of shares/underlying shares held	Percentage of issued share capital
Interests			
PCRD	1	1,528,781,171	28.45%
PCGH	2	1,549,938,605	28.84%
Star Ocean Ultimate Limited	3	1,549,938,605	28.84%
The Ocean Trust	3	1,549,938,605	28.84%
The Starlite Trust	3	1,549,938,605	28.84%
OS Holdings Limited	3	1,549,938,605	28.84%
Ocean Star Management Limited	3	1,549,938,605	28.84%
The Ocean Unit Trust	3	1,549,938,605	28.84%
The Starlite Unit Trust	3	1,549,938,605	28.84%
Short Positions			
PCRD	4	321,176,469	5.98%
PCGH	4	321,176,469	5.98%
Star Ocean Ultimate Limited	4	321,176,469	5.98%
The Ocean Trust	4	321,176,469	5.98%
The Starlite Trust	4	321,176,469	5.98%
OS Holdings Limited	4	321,176,469	5.98%
Ocean Star Management Limited	4	321,176,469	5.98%
The Ocean Unit Trust	4	321,176,469	5.98%
The Starlite Unit Trust	4	321,176,469	5.98%

Notes:

- These interests represented (i) PCRD's beneficial interests in 1,526,094,301 shares and 679,000 underlying shares held in the form of 67,900 ADRs which constituted listed equity derivatives; and (ii) PCRD's interests through its 45.11% owned subsidiary, Pacific Century Insurance Holdings Limited ("PCIHL"), in 2,007,870 underlying shares in respect of US\$10,000,000 convertible bonds which constituted listed physically settled equity derivatives convertible into shares of the Company.
- These interests represented (i) PCGH's beneficial interests in 20,354,286 shares and 803,148 underlying shares in respect of US\$4,000,000 convertible bonds held by it which constituted listed physically settled equity derivatives convertible into shares of the Company; and (ii) PCGH's interests through its controlled corporations (being its wholly-owned subsidiaries, Borsington Limited, Pacific Century International Limited, Pacific Century Group (Cayman Islands) Limited and Anglang Investments Limited, which together controlled 75.33% of PCRD) in shares and underlying shares of the Company held by PCRD (as described in Note 1 above).
- On April 18, 2004, Li Tzar Kai, Richard transferred the entire issued share capital of PCGH to Ocean Star Management Limited as trustee of The Ocean Unit Trust and The Starlite Unit Trust. The entire issued share capital of Ocean Star Management Limited was held by OS Holdings Limited. The Ocean Trust and The Starlite Trust held all units of The Ocean Unit Trust and The Starlite Unit Trust respectively. Star Ocean Ultimate Limited was the discretionary trustee of The Ocean Trust and The Starlite Trust.
- PCGH, Star Ocean Ultimate Limited, The Ocean Trust, The Starlite Trust, OS Holdings Limited, Ocean Star Management Limited, The Ocean Unit Trust and The Starlite Unit Trust were deemed to have short positions in the same underlying shares held by PCRD, under the SFO pursuant to the arrangements as described in the paragraph (1)(B) under the sub-section headed "Short Positions in the Shares and Underlying Shares of the Company".

INTERESTS AND SHORT POSITIONS OF SUBSTANTIAL SHAREHOLDERS (CONTINUED)**(B) Interests and Short Positions of Other Persons Required to be Disclosed under the SFO**

As at December 31, 2004, the following persons (not being directors, the chief executive or substantial shareholders of the Company) had interests or short positions in the shares and underlying shares of the Company as recorded in the register required to be kept under Section 336 of the SFO:

Name of shareholder		Number of shares/underlying shares held	Percentage of issued share capital
Interests			
Ocean Star Investment Management Limited	Note	1,549,938,605	28.84%
Lehman Brothers Holdings Inc.		434,546,309	8.09%
Short Positions			
Ocean Star Investment Management Limited	Note	321,176,469	5.98%
Lehman Brothers Holdings Inc.		554,387,107	10.32%

Note: Ocean Star Investment Management Limited was deemed interested and to have short positions under the SFO in the shares and underlying shares of the Company by virtue of it being the investment manager of The Ocean Unit Trust and The Starlite Unit Trust which together held 100% of PCGH (see above).

Save as disclosed above in this section and the previous section headed "INTERESTS AND SHORT POSITIONS OF SUBSTANTIAL SHAREHOLDERS", the Company had not been notified of any other person (other than directors or chief executive of the Company) who had an interest or a short position in the shares and underlying shares of the Company as recorded in the register required to be kept by the Company pursuant to Section 336 of the SFO as at December 31, 2004.

DIRECTORS' INTERESTS IN CONTRACTS OF SIGNIFICANCE

No contract of significance in relation to the Group's business (as defined in the Listing Rules) to which the Company, its subsidiaries, its holding companies or any of its fellow subsidiaries was a party and in which a director of the Company had a material interest, whether directly or indirectly, subsisted at the end of the year or at any time during the year. However, during the year, Li Tzar Kai, Richard had an interest, through his associates including Pacific Century Group Japan Y.K. (formerly known as Pacific Century Group Japan Co., Ltd.) ("PCGJ"), Pacific Century Matrix (HK) Limited ("PC Matrix"), Pacific Century Insurance Company Limited ("PCI") and PCRD, in certain transactions which constituted "connected transactions" of the Company under the Listing Rules. Particulars of these transactions are set out in the section headed "CONNECTED TRANSACTIONS" in this report.

DIRECTORS' INTERESTS IN COMPETING BUSINESS

The interests of the directors of the Company in competing business as at December 31, 2004 required to be disclosed pursuant to Rule 8.10 of the Listing Rules were as follows:

Name of Directors	Names of companies	Nature of business	Nature of interests
Li Tzar Kai, Richard	Cheung Kong and its subsidiaries ("Cheung Kong Group")	Property development and investment, hotel and serviced suite operation, property and project management and investment in securities	Deemed interests in Cheung Kong (Note 1)
	HWL and its subsidiaries ("Hutchison Group")	Ports and related services, telecommunications, property and hotels, retail and manufacturing and energy and infrastructure	Certain personal and deemed interests in HWL (Note 2)
Yuen Tin Fan, Francis	Kee Shing (Holdings) Limited ("KSH") and its subsidiaries	Sale of chemicals and metals, property and securities investment	Non-executive director and deemed interests of 22.84% of KSH through a controlled corporation and as founder of a trust
Chung Cho Yee, Mico (Note 3)	Capital Strategic Investment Limited ("CSI") and its subsidiaries	Property holding, leasing of property, investment holding and sale of securities	Non-executive director and beneficial owner of 40.90% of CSI

Notes:

1. Certain business of the Cheung Kong Group may compete with certain aspects of the business of the Group. Li Tzar Kai, Richard is one of the discretionary beneficiaries of certain discretionary trusts which hold units in unit trusts which in turn are interested in certain shares of Cheung Kong. Li Tzar Kai, Richard holds one-third of the issued share capitals of two companies, which own all the shares in the trustee companies which act as trustees of such discretionary trusts and unit trusts. These trustee companies perform their functions as trustees independently without any reference to Li Tzar Kai, Richard. Notwithstanding the above, his being a discretionary beneficiary and that the trustee companies act independently of him, the Company considers that Li Tzar Kai, Richard is not able to exert control or influence over the Cheung Kong Group.
2. Li Tzar Kai, Richard was a director of HWL and certain of its subsidiaries until August 16, 2000, the day before the acquisition of Cable & Wireless HKT Limited (now known as PCCW-HKT Limited) became effective. Certain businesses of the Hutchison Group compete with certain aspects of the business of the Group. Li Tzar Kai, Richard has a personal interest in 110,000 shares in HWL, and is one of the discretionary beneficiaries of certain discretionary trusts which hold units in unit trusts which in turn are interested in certain shares of HWL. Li Tzar Kai, Richard holds one-third of the issued share capitals of two companies, which own all the shares in the trustee companies which act as trustees of such discretionary trusts and unit trusts. These trustee companies perform their functions as trustees independently without any reference to Li Tzar Kai, Richard. Notwithstanding the above, and in view of his small personal shareholding, his being a discretionary beneficiary and that the trustee companies act independently of him, the Company considers that Li Tzar Kai, Richard is not able to exert control or influence over the Hutchison Group.
3. Chung Cho Yee, Mico holds direct personal interest in a private company, which engages in property investment or development in Repulse Bay, Hong Kong.

In addition, Li Tzar Kai, Richard, Yuen Tin Fan, Francis, Peter Anthony Allen, Alexander Anthony Arena and Lee Chi Hong, Robert are directors of certain private companies (the "Private Companies"), which are engaged in property development and investment in Hong Kong (a development called Gough Hill) and/or Japan (investment in certain residential properties and a commercial building).

Further, Li Tzar Kai, Richard, Peter Anthony Allen and Alexander Anthony Arena are directors of PCRDC. PCRDC acts as an investment holding company of, among others, interests in the Company and certain property development interests in Singapore and India.

DIRECTORS' INTERESTS IN COMPETING BUSINESS (CONTINUED)

The business interests of the Private Companies in Hong Kong are not significant when compared to the business of the Group and it is unlikely that such businesses will compete with the property business of the Group. The businesses in Japan, Singapore and India, are also unlikely to compete with the existing investment and development property portfolio of the Group.

Li Tzar Kai, Richard has a controlling interest in some of the Private Companies. Further, he is or may be regarded as interested in PCRD and PCGH due to the interests as disclosed in the above paragraph under the section headed "Directors' and Chief Executive's Interests and Short Positions in Shares, Underlying Shares and Debentures of the Company and its Associated Corporations" in this report.

As those companies disclosed above, which might have competing businesses with the Group, are involved in the development and/or investment of properties of different types and/or in different locations, the Group has been operating independently of, and at arms length from, the businesses of those companies.

Furthermore, the Group holds minority equity interests in a number of Internet-related companies in which the Group is entitled to appoint, and has appointed, one or more directors to the board of these companies to represent the interests of the Group. Some or all of these companies may compete directly or indirectly, with certain aspects of the Group's business.

Other than as disclosed above, none of the directors is interested in any business apart from the Group's businesses, which competes or is likely to compete, either directly or indirectly, with the Group's businesses.

CHARITABLE DONATIONS

During the year, the Group made no donation (2003: HK\$1.2 million).

POST BALANCE SHEET EVENTS

Details of the significant post balance sheet events are set out in note 39 to the consolidated financial statements.

PURCHASE, SALE OR REDEMPTION OF LISTED SECURITIES

During the year, there was no purchase, sale or redemption by the Company, or any of its subsidiaries, of the listed securities of the Company.

CONNECTED TRANSACTIONS

In the period since the publication of the Company's 2003 Annual Report, members of the Group entered into (or continued to be party to) certain transactions which were "connected transactions" as defined by the Listing Rules and which are subject to disclosure obligations under Chapter 14A of the Listing Rules. Details of such transactions are as follows:

1. On November 19, 2001 (as disclosed in the Company's 2003 Annual Report), PCCW Communications (Japan) K.K. ("PCCW Communications"), an indirect wholly-owned subsidiary of the Company, entered into a five-year lease agreement (the "Lease") with PCGJ regarding the lease of certain office space in Pacific Century Place Marunouchi, Tokyo, Japan (the "Building") owned by PCGJ at a monthly rent of approximately Yen 7.4 million (approximately HK\$0.5 million) plus other monthly management expenses and a sub-lease agreement (the "Sub-Lease") regarding the sub-lease of office space in the Building to PCGJ at a monthly rent of approximately Yen 3.1 million (approximately HK\$0.2 million) plus other monthly management expenses and renovation costs in order to meet office space requirements. The Sub-Lease has a term of approximately four years and ten months. PCCW Communications also entered into a five-year lease agreement (the "Display Lease") with The Pacific Century Place Marunouchi Owners Union ("PCPMOU") regarding the lease of space for display of the Company's logo outside the Building at a monthly rent of Yen 0.95 million (approximately HK\$0.07 million). A change was made to the arrangements described above when, on December 2, 2002, PCCW Communications entered into an agreement (the "Novation") with PCGJ and New PCGJ Co., Ltd. The Novation was required in connection with certain financing arrangements PCGJ entered into with a third party and does not impact on the substance of the arrangements. Its effect was to transfer PCGJ's rights and obligations under the Sub-Lease to New PCGJ Co., Ltd. In the calendar year 2004, PCCW Communications paid approximately HK\$8 million and approximately HK\$0.9 million under the Lease and Display Lease respectively and received approximately HK\$3.7 million under the Sub-Lease.

Li Tzar Kai, Richard indirectly holds a 55% interest in the issued share capital of PCGJ and New PCGJ Co., Ltd. PCGJ is able to exercise 94% of the voting rights of PCPMOU. As PCGJ, New PCGJ Co., Ltd. and PCPMOU are each associates of Li Tzar Kai, Richard, they are therefore connected persons of the Company.

CONNECTED TRANSACTIONS (CONTINUED)

2. During the year ended December 31, 2004, PCCW Services Limited (“PCCW Services”), a wholly-owned subsidiary of the Company, provided certain staff, administrative and support services to PC Matrix. The services were provided by PCCW Services on normal commercial terms and were within the ordinary course of business of PCCW Services. PC Matrix is a leading provider of satellite-based broadband network solutions for broadcasters, Internet services providers, corporations and content providers across the Asian region. Its headquarters are in Hong Kong. PCCW Services provides various management, administrative, office and support services to subsidiaries of the Company and certain third parties and as such, agreed to provide these services to PC Matrix. For the year ended December 31, 2004, the total charges for such services provided to PC Matrix amounted to approximately HK\$6.3 million. The charges were negotiated on arm’s length basis with the charges based on a cost plus arrangement. PCCW Services is continuing to provide services of a similar scope, and on the same terms as those referred to above, to PC Matrix.

PC Matrix is indirectly wholly-owned by Li Tzar Kai, Richard. As PC Matrix is an associate of Li Tzar Kai, Richard, it is a connected person of the Company.

3. The Group have maintained annually renewable group life and medical policies with PCI which include life, clinical and hospitalization coverage for the benefit of employees of the Group. PCI is principally engaged in individual life insurance, medical and disability insurance, retirement scheme, administration, group insurance and life personal accidental insurance. During the year ended December 31, 2004, the Group paid to PCI insurance premiums in cash amounting to approximately HK\$4.4 million in respect of group life and medical insurance coverage for employees of the Group. PCI is continuing to provide group life and medical insurance to the Group. The policies are within the ordinary course of business of PCI, were negotiated on an arm’s length basis and are on normal commercial terms. The policies are provided for life, clinical and hospitalization coverage to employees of the Group in the ordinary course of the Group’s business and are on substantially the same terms and conditions that are offered by PCI to other PCI policyholders.

PCI is a wholly-owned subsidiary of PCIHL, of which PCRD held approximately 45% as at December 31, 2004. PCRD is a substantial shareholder of the Company.

4. PCRD, a substantial shareholder of the Company, has provided a rental guarantee on each of Towers A and B and the 6-storey commercial podium of Pacific Century Place, Beijing, the PRC. The two-year rental guarantees on Tower A and Tower B expired in 2001 and 2002 respectively. The two-year rental guarantee of not less than US\$12,028,526 (approximately HK\$93 million) in respect of the podium commenced in July 2002.

Details of this guarantee have been previously disclosed by the Company in a shareholders’ circular dated July 7, 1999 and were approved by the shareholders of the Company at an extraordinary general meeting held on July 29, 1999.

The Board, including the independent non-executive directors of the Company, has reviewed the rental guarantee and confirmed that such rental guarantee has been provided to the Company as stated in the Acquisition Agreement as amended by the Acquisition Supplemental Agreement (each as defined in the shareholders’ circular dated July 7, 1999).

5. The Group from time to time enters into transactions (“CTC Transactions”) with China Telecommunications Corporation (“China Telecom” or “CTC”) and its subsidiaries and associates (“China Telecom Group”) relating to the services provided and to be provided by the Group relating to solutions and system integration services, project management, advisory, training, application development, design, maintenance and implementation services, equipment and equipment installation products and services that support a variety of telecommunications products and services within the PRC, voice and data communication products and services (including without limitation to bandwidth service), and the acquisition or sale or delivery of international and associated domestic connectivity products and services and/or telephone traffic minutes of use (“Services”).

Unihub China Information Technology Company Limited (“UCIT”) is a 50%:50% equity joint venture established in the PRC by Unihub Global Network Technology (China) Limited, an indirect non wholly-owned subsidiary of the Company, and China Huaxin Post and Telecommunications Economy Development Centre (“China Huaxin”), a wholly-owned subsidiary of China Telecom. UCIT is an indirect non wholly-owned subsidiary of the Company because the Company indirectly controls the composition of a majority of the board of directors of UCIT. A major part of UCIT’s business plan is the development, production and sale of information technology, systems and products that support the provision of a variety of telecommunications services within the PRC.

CONNECTED TRANSACTIONS (CONTINUED)

China Telecom is regarded as a connected person of the Company because: (i) China Huaxin, a wholly-owned subsidiary of China Telecom, is a substantial shareholder of UCIT, a non wholly-owned subsidiary of the Company; and (ii) China Telecom is an associate of China Huaxin. Accordingly, members of the China Telecom Group are connected persons (as defined in the Listing Rules) of the Company and transactions between the Group and the China Telecom Group will constitute connected transactions for the Company under the Listing Rules.

The consideration for each of the CTC Transactions will be a fixed sum set out in the relevant agreements between the relevant parties for a fixed term of not more than 3 years, settled by way of cash and determined by arm's length negotiations between the relevant parties with reference to (i) the estimated costs of the provision of the relevant Services to the China Telecom Group; and (ii) if applicable, the estimated costs of the relevant hardware equipment and the resources to be incurred by the Group for installing the same.

As it is anticipated that the Services to be provided by the Group to the China Telecom Group will be on a regular basis, the Company applied and the Stock Exchange granted a waiver to the Company in February 2004 of strictly compliance with the requirements under the then Listing Rules in respect of the continuing connected transactions for the period ending December 31, 2006. Details of the CTC Transactions have been disclosed in the Company's announcement dated February 9, 2004.

Following the amendment of the Listing Rules effective March 31, 2004, the CTC Transactions constitute connected transactions under Rule 14A.34 of the Listing Rules which will only be subject to the reporting and announcement requirements set out in Rules 14A.45 to 14A.47 of the Listing Rules and no shareholders' approval will be required if the aggregate value of the CTC Transactions on an annual basis does not exceed 2.5% of each of the percentage ratios (other than profits ratio) under Rule 14.07 of the Listing Rules. Details of the said arrangement of the CTC Transactions have been disclosed in the Company's announcement dated August 27, 2004 ("August Announcement") and this report.

As explained in August Announcement, the relevant amount calculated pursuant to Rule 14.07 would be approximately HK\$563,000,000 ("Annual Cap") which represents an amount less than 2.5% of the Company's revenue for the financial year ended December 31, 2003. The Annual Cap has been determined by reference to the nature and value of the CTC Transactions for the financial year ended December 31, 2003 and during the period from January 1, 2004 to August 1, 2004, and the existing scale and operation of the Group's business within the PRC. The Company will comply with the requirements under Rule 14A.36 of the Listing Rules if the aggregate value of the CTC Transactions during each of the three financial years ending December 31, 2006 exceeds the amount of HK\$563,000,000, or such other amount as calculated pursuant to Rule 14.07 based on the financial information for the relevant year.

The aggregate value for the CTC Transactions between the Group and China Telecom Group for the period from February 10, 2004 to December 31, 2004 was approximately HK\$559 million.

The Board, including the independent non-executive directors of the Company, has reviewed and confirmed that the CTC Transactions for the period from February 10, 2004 to December 31, 2004 were entered into:

- (i) in the ordinary and usual course of the business of the Group;
- (ii) either on normal commercial terms or on terms no less favourable to the Group than terms available to or from independent third parties; and
- (iii) in accordance with the relevant agreements governing them on terms that are fair and reasonable and in the interests of the shareholders of the Company as a whole.

In addition, the Auditors of the Company confirmed to the Board in writing in respect of the CTC Transactions for the period from February 10, 2004 to December 31, 2004 that the CTC Transactions:

- (i) were approved by the Board;
- (ii) were in accordance with the pricing policies of the Group if the CTC Transactions involve provision of goods or services by the Group;
- (iii) were entered into in accordance with the relevant agreements governing the CTC Transactions; and
- (iv) did not exceed the Annual Cap disclosed in August Announcement.

PUBLIC FLOAT

As at the date of this report, the Company has maintained the prescribed public float under the Listing Rules, based on the information that is publicly available to the Company and within the knowledge of the Company's directors.

MODEL CODE FOR SECURITIES TRANSACTIONS BY DIRECTORS

The Company has established its own code of conduct regarding securities transactions by Directors and senior management namely PCCW Code of Conduct for Securities Transactions by Directors and Senior Management (the "PCCW Code") on terms no less exacting than the required standard set out in the Model Code. Having made specific enquiry of all directors of the Company, they have confirmed that they complied with the required standard set out in the PCCW Code and the Model Code throughout the year.

CODE OF BEST PRACTICE

Throughout the year, the Company complied fully with the Code of Best Practice as set out in Appendix 14 to the Listing Rules in force prior to January 1, 2005 save that the non-executive directors are not appointed for a specific term of office. Following the amendments to the Company's Articles of Association with effect from January 7, 2003, the directors (including non-executive directors) are subject to retirement by rotation and shall be eligible for re-election at each annual general meeting.

AUDITORS

Arthur Andersen & Co acted as the Auditors of the Company in respect of the financial year ended December 31, 2001. The financial statements for the financial years ended December 31, 2002, 2003 and 2004 have been audited by PricewaterhouseCoopers who will retire upon the conclusion of the forthcoming annual general meeting. A resolution for the re-appointment of PricewaterhouseCoopers as Auditors of the Company is to be proposed at the forthcoming annual general meeting.

On behalf of the Board

Hubert Chak

Company Secretary

Hong Kong,

March 30, 2005