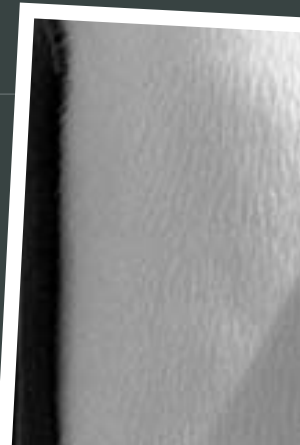




we have a clear corporate mission





competition

WINNER

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Dear Fellow Shareholders,

City Telecom (HK) Limited (CTI) was established in 1992, such that we now possess a history of 13 years. During our first 12 years, we recorded satisfactory results that delivered substantial returns to shareholders. Riding on the income from our operations, the Group evolved into new business lines during these first 12 years, i.e. the cash flow from our early IDD callback and resale businesses funded our investment in international submarine cables and since 2000, the building of Hong Kong's largest alternative end-to-end telecom network. Starting from zero, we have established our "Little Kingdom", and some people would even consider our story to be a "Legend".

FY05 marks our first ever full year loss, suggesting the fall of the Legend. However the net loss is within our strategic tolerance, and is in line with the trends set out in our interim results announcement.



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A key reason for inaugural net loss of HK\$206.4 million is our depreciation expenses of HK\$237.7 million, which is a function of our heavy investment in our Metro Ethernet network since 2000. In addition, this is the second year of operation for the Group's IP-TV business, which requires tremendous investment to bring to fruition.

Some investors, who do not fully understand our long term development strategy, are likely to be disappointed by our financial results. However, as a major shareholder and Chairman of the Group, I should be more concerned on the development of the Group, compared to other shareholders. During the year, we received several awards and words of praises that confirmed our Metro Ethernet platform is the top choice for Hong Kong. I believe that you need great long term foresight for investment in infrastructure.

Whilst the road ahead for establishing infrastructure is challenging, we are committed to expanding our own end-to-end network with the objective of total independence from other operators. As other operators are, at the end, our direct competitors, we must ride on our own network as market competition intensifies, in order to attain victory.

From internal customer surveys of focus groups and a report from an external customer service consultant, we observed that the quality of our services and customer care has improved significantly over the past 12 months. Our mission is to become the best operator in Hong Kong, and we set in motion a tactical plan to surpass the incumbent operator in terms of quality of services and customer care. The component that we are now lacking is an established brand name. Having

reached a high level in quality of service and customer care, we will now complete the package by large scale brand building campaigns, as we strive to become the best triple-play (voice, broadband and IP-TV) service provider in Hong Kong.

In January 2005, we secured long term funding with a 10-year US\$125 million senior notes issue. The proceeds are being used to strengthen and expand our Metro Ethernet network, from the existing 1.2 million homes pass to 1.8 million homes pass, targeting 80% of the total number of households in Hong Kong. In addition, as we anticipate that competition in telecom market will become even more intense and that extended price wars are inevitable, we must prepare sufficient resources to counterattack in the coming three to four years.

Rightly, shareholders may be concerned about the strategic direction of our IP-TV business. Based on our experiences from investing in the broadband and voice businesses, IP-TV is an infrastructure intensive business which will require time to mature, and as such, we are committed to investing in IP-TV for the benefit of the Group overall.

In my view, there will be drastic changes in the local pay-TV market. In the past from the early 1990's to 2004, the local pay-TV market was dominated by a single operator. The formation of PCCW's NOW Broadband TV and HKBN Digital TV will lead to significant changes in the market place, such that it is questionable whether the incumbent pay-TV operator can sustain its market share of taking a majority of the pay-TV customers. Following the attack by PCCW's NOW Broadband TV in taking away most of the exclusive pay-TV contents from the incumbent pay-TV operator at

high cost, the market share of the incumbent operator is under serious threat. In short, there are now four pay-TV operators in the local market, which will help to propel the development of the local pay-TV market. In future, I expect that the majority of households will subscribe to pay-TV services, in addition to the terrestrial free-to-air television services. As not all households can afford service of monthly tariff at HK\$180 level or above, this creates a large market gap for our services. With our extensive fixed telecom network services customer base, we can generate substantial income even if only half of them subscribe to our IP-TV service.

Finally, on behalf of the Board of Directors, I wish to sincerely thank our Finance Director, Ms Corinna Sio for her invaluable contributions to the Group. Ms Sio joined the Group in 1993, staying with us for more than 12 years. She had fully devoted herself to the Group, and her intelligence, integrity and candor is particularly valuable, especially at her position as Finance Director. Ms Sio has contributed a significant role in several major milestones of the Group, such as listing on Stock Exchange of Hong Kong Limited and Nasdaq National Market in the US, as well as current development of the Group. Ms Sio will leave the Group at the end of this year to pursue personal interests. Once again, I would like to thank her sincerely for all she has done for us.

Wong Wai Kay, Ricky
Chairman
21st November 2005