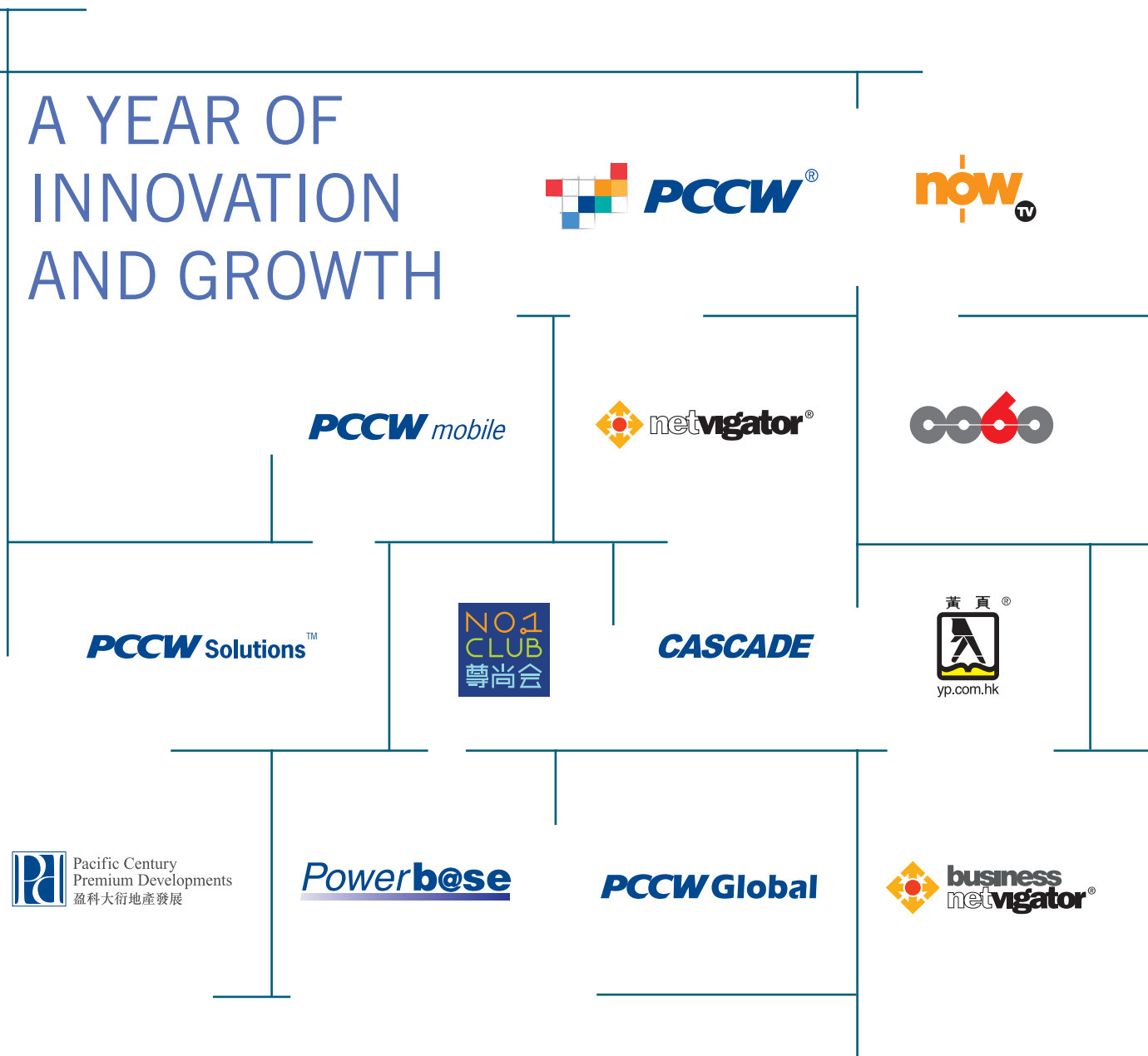


A YEAR OF INNOVATION AND GROWTH



PCCW made solid progress in 2005, building on foundations laid in previous years with some major achievements to set the scene for growth.

The PCCW brand was strengthened at home and overseas as the Group maintained a track record of innovation and service quality, while pursuing a strategy that positions PCCW as a fully-integrated provider of connectivity, mobility, information and entertainment.

A major development in 2005 was the acquisition of a majority stake in SUNDAY, heralding PCCW's return to Hong Kong's mobile communications scene and opening up a new vista of opportunity to explore synergies across the Group. This led to a ground-breaking "3G Trial" in early 2006 to help PCCW develop an exciting new 3G experience for Hong Kong.



Year 2005 also saw **now TV** rise to become the largest pay-TV operation of its kind in the world, with subscriber numbers reaching our 500,000 year-end target in November, before finally settling at 549,000 at the end of December.

Another milestone development last year was a major change in Hong Kong's regulatory regime – greatly assisted by our consultative and litigation efforts – granting far greater commercial freedom to the way we price our products and services (see page 21).

This new freedom, coupled with the move back into the mobile business, has enabled the Company to optimize its position as Hong Kong's most comprehensive service provider by creating imaginative marketing, cross-selling and pricing initiatives.

That has also empowered managers and their teams to maximize the integration of PCCW's products, services and content by exploring new possibilities and creating innovative solutions, packages and propositions.

Hong Kong's buoyant economy assisted growth in the fixed-line market in 2005, during which a gradual erosion in the overall number of fixed lines was reversed, helping to create a fertile sales and marketing environment for both PCCW's Consumer and Commercial Groups.

A major 2005 event was the announcement of a strategic alliance between PCCW and China Netcom Group to jointly develop businesses in mainland China and internationally. Terms of the alliance were approved by shareholders at an Extraordinary General Meeting on March 16, 2005, and three directors nominated by China Netcom Group joined the PCCW Board in April.

Like 2004, last year saw PCCW collect an array of accolades, including the highly-significant "Best International Leased Lines" and "Best International Frame Relay" titles in the international data services category of the Gartner DataQuest User Survey: International Telecom Services Asia Pacific 2005. The rankings were based on a survey of 400 network managers in multinational corporations in Asia Pacific and resulted in PCCW being placed at the top of a league-table of major telecoms operators.

LOCAL TELEPHONY

PCCW turned net line loss into line gain in 2005 – from a total net loss of 95,000 lines in the second half of 2004 to a net gain of 50,000 business and residential lines in the last six months of 2005.

After PCCW's obligation to seek the regulator's pre-approval for price adjustments was stripped away in January last year, the Company was able to capitalize on newfound flexibility by introducing creative pricing and cross-selling programs to offer customers greater choices and more benefits. The result was new customers, a higher "winback" rate in attracting subscribers back from competitors and greater loyalty among existing customers.

The strength of the PCCW brand and our reputation for high-quality products, tip-top customer service and value for money means the Company has been able to focus on profitability rather than market share, without being drawn into price wars.

Customers have enjoyed their third upgrade so far in New Generation Fixed Line (NGFL) SMS phones, with the latest cordless model for the home sporting a color screen and continued enrichment of functionality and features.

Constant enhancement of the infotainment downloads available on NGFL phones continues to differentiate our service from the rest of the market and reinforces PCCW as a premium service provider. Most NGFL content is free, while some services, such as downloadable ring and connecting tones and stock quotes, are competitively priced.

PCCW's reputation as a world leader in IP technology was reinforced last year by a number of high-profile projects, such as a contract to build a leading-edge, IP-based network for Hong Kong Exchanges and Clearing Limited (HKEx), which when finished in 2007 will result in the largest integrated, mission-critical, IP-enabled securities and derivatives network in Asia.

Another milestone development was a 10-year agreement under which PCCW joined with Hong Kong's new world-class AsiaWorld-Expo exhibition and event complex to provide next-generation ICT services to organizers, exhibitors and visitors from all over the world. As AsiaWorld-Expo's sole ICT provider, PCCW set out last year to build Asia's largest indoor wireless broadband network, plus an array of other leading-edge IP-based services.

PCCW's Commercial Group was also responsible for the Best in Business Award from the Metro Ethernet Forum, which is made up of some 70 organizations, including major telecoms service providers and network equipment and software manufacturers. Winning the award in the Asia Pacific Service Provider of the Year 2005 category, PCCW was said to have demonstrated outstanding ability and innovative skills in finding imaginative ways to integrate new service offerings with world-class business practices in the region.

That reputation for innovation was also reflected in enhanced versions of the PCCW Convergence service, which brings office communications together into one onscreen interface. The service continues to prove popular among Hong Kong's enterprise community, attracting 23,000 users by the end of 2005, compared with 10,000 the year before.

In fact, PCCW Convergence outperformed more than 40 other entries to win a Gold Award in the Enterprise Mobility Application category of the inaugural Hong Kong Wireless Technology Excellence Awards staged last year by the Hong Kong Wireless Technology Industry Association. In addition, the service topped the Intelligent Communications Service class of the IT Square Editor's Choice 2005 Awards organized by the *Sing Tao* newspaper.

TRANSITION TO AN ALL-IP NETWORK

Year 2005 saw careful planning of PCCW's transition to an all-IP network – or Next Generation Network (NGN) – to serve the Company's development as a provider of content, interactivity and transactional services, as well as connectivity.

During the year, the tender process was completed to select suitable vendors for access, core IP network and intelligent switching layers of the NGN, which will involve a number of vendors conforming to international NGN standards.

Running until 2014, our NGN program will result in one efficient, cost-effective IMS (IP-based Multimedia Services) platform carrying all traffic, whether voice, Internet, video, multimedia or applications on an all-IP "super-highway" network.

The first, or pilot stage will go live in 2006 and spearhead a network-wide upgrade based on a "just-in-time" planning model so that existing equipment is replaced at the end of its useful lifespan to prevent unnecessary expense and waste of resource. In fact, PCCW's NGN transition has been planned so that annual capital expenditure and eventual cost will be proportionate to the levels of investment traditionally required over time to keep legacy networks up to speed with demand.

The transition will also be executed seamlessly so that customers will not have to acclimatize to new tones or commands when using fixed-line phones, except that new and innovative services will be introduced in step with the upgrade.

Higher-speed bandwidth rollout to customers (beyond existing 8 Mbit/s services) is also planned to keep abreast of dynamic market demand, such as for interactive services from today's NOW TV, as well as an expected appetite for High Definition TV and more transactional functionality on fixed-line phones. Higher-speed bandwidth will also enable the development of "home networks" and Fixed Mobile Convergence, featuring suites of innovative lifestyle-enhancing applications.

INTERNATIONAL TELECOMS SERVICES

Although Hong Kong's International Direct Dial (IDD) market remained fiercely competitive in 2005, PCCW was able to generate double-digit growth in overall traffic minutes, make gains in total market share and keep price erosion at a lower level than the market average. The Company's return to the mobile communications business provides a potentially valuable opportunity to market our 0060 IDD service among mobile users at a time when the Hong Kong IDD market is showing continued signs of growth.

PCCW mobile

The acquisition of a controlling stake in SUNDAY in June last year signaled PCCW's return to the mobile communications scene and represented a major strategic milestone in the Company's development as a comprehensive service provider.

The move enabled PCCW to start work on a wider range of services for customers, progress plans for future Fixed Mobile Convergence and position the Company to be China Netcom Group's preferred mobile partner.

In January 2006, the Company hit the headlines when the new PCCW mobile division unveiled a ground-breaking "3G Trial" designed to offer customers an exciting new 3G experience and provide valuable feedback to help fine-tune the PCCW service before launch.

A major advertising campaign under the banner "PCCW wants you!" invited mobile users to join our "3G Trial" and drew over 330,000 applicants.

The six-month trial offer included use of a PCCW-branded handset, local airtime and inter-network video calls, MMS and





SMS. The offer also included local GPRS use for browsing the PCCW mobile 3G WAP portal, plus highlights, movie trailers, drama, news and music from **now TV** and TVB Channel.

The provision of **now TV** content on PCCW mobile 3G handsets is a prime example of new synergies that have been created across the Group by our return to the mobile communications business. Opportunities now exist for PCCW to produce imaginative and attractive packages for customers from a wider variety of products and services.

BROADBAND

Year 2005 saw PCCW following a strategy of differentiating our broadband offer in the market by leveraging the all-round strength of the **NETVIGATOR** brand and introducing new value-added services and customer benefits to enhance **NETVIGATOR**'s positioning as Hong Kong's premier broadband provider.

The number of residential customers rose to about 798,000 in 2005, from approximately 660,000 the previous year, while the number of retail business broadband lines – part of the Business eSolutions portfolio – increased to 88,000 by the end of 2005 from about 74,000 in 2004.

Consumers subscribing to **now TV** had the effect of boosting residential broadband take-up, while high satisfaction with the pay-TV service helped reduce churn among existing **NETVIGATOR** broadband Internet customers.

The business broadband market continues to grow, as PCCW creates more innovative applications to make broadband ever more useful to our commercial customers. Churn in the business sector has been kept to a minimum by the appeal of PCCW's many value-added services, such as security and storage features.

The broadband scene in Hong Kong is widely regarded as the most successful commercially-focused model in the world, with overall household penetration reaching 65.6% as of December 2005, according to OFTA. PCCW is able to serve all major business areas and 95% of all homes with broadband service.

now TV

Our pay-TV service became the largest of its kind in the world in 2005, with total subscriber numbers breaking through the 500,000 year-end target in November, reaching 549,000 by the end of December 2005. Building the customer-base will continue to be a primary focus in 2006.

Content improved steadily in terms of quantity, quality and variety over the year to reach more than 100 channels by 2006. In addition, special deals were struck to make **now TV** the exclusive Hong Kong provider of all STAR and HBO movie channels, as well as 2006 FA Cup coverage and the UEFA Champions League for three years beginning September 2006.

Upholding its image as the envy of the world's IPTV industry, **now TV** maintained a stream of innovation in 2005 that increased interactivity for subscribers and transformed the living-room TV set into a transactional tool.

A deal with the CityLine Internet and tele-ticketing company spawned the **now** Ticketing service, which enables customers to buy UA Cinema tickets and choose seats using the **now TV** remote control device. The service has proved to be a big hit among subscribers, who are able to watch trailers for the latest blockbuster movies on Channel 8, then buy cinema tickets from the comfort of their own armchairs. More interactivity and transactional e-commerce services are planned for 2006.

Another key development in 2005 was **now Select**, an on-demand service enabling subscribers to the STAR Chinese Movies and Mei Ah Drama and Movie Channels to enjoy access to libraries of movies and drama series at any time for just HK\$15 per month. The **now Select** service is expected to be extended to include content from other channels in 2006.

Movie fans also welcomed the launch of the **now MOVIE CLUB** last year, which offers subscribers the chance to attend special cinema preview screenings of blockbuster films in Hong Kong.

PCCW found that between 85% and 90% of all new **NETVIGATOR** broadband Internet-access customers became **now TV** subscribers, and a special "minipack" promotion continued to encourage viewers to subscribe to more channels by offering a "spend more, get more" deal.

A campaign was launched early last year to boost **now TV**'s local content and led to the addition of the Cantonese 24-hour ATV News channel, plus more Asian drama and Chinese movies. Other channels added in 2005 included **BLOOMBERG TELEVISION**, CNN Headline News, the Boomerang children's channel, EuroNews, EETV Asia Channel, EETV Asia News and the Asian Food Channel, as well as Asia's leading music service, made up of Channel [V] Mainland China, Channel [V] India and Channel [V] International.

Local content received another boost in early 2006 when PCCW announced an agreement for the **NOW TV** platform to carry Galaxy's TVB PAY VISION service of eight TVB-produced channels plus 12 others, bringing our pay-TV service line-up to more than 110 channels. A further development in early 2006 saw the launch of **NOW Business News Channel**, a self-produced, premium-quality, Cantonese-language, financial news channel.

An exciting new delivery medium opened up to our pay-TV service when PCCW announced a return to the mobile communications business and the 2006 launch of a six-month "3G Trial", enabling participants to watch **NOW TV** content and try a host of other exciting infotainment features on their unique PCCW-branded handsets.

In August last year, PROMAX and BDA, which represent more than 4,200 TV, radio and other electronic media players in 60 countries, named **NOW TV** winner of their World Gold and World Silver Awards at a special event in New York.

NETVIGATOR

The NETVIGATOR brand was further strengthened in 2005 by a string of awards, more value-added services and special brand-enhancing promotions such as the "Love Music" series of live concerts featuring popular Hong Kong stars.

The Internet Service Provider's (ISP) reputation for innovation received a boost in early 2006 when PCCW mobile's much-publicized "3G Trial" made it possible for participating customers to access their NETVIGATOR email accounts on their mobile phones.

Among NETVIGATOR's accolades for the year was the Top Service Award – Internet Service Provider Category in *Next Magazine's* Top Service Awards 2005 – making our ISP the winner for seven consecutive years. NETVIGATOR also won the Top Service Gold Award and an individual Silver Best Staff Award in *Next Magazine's* recognition scheme.

Other awards included Broadband Service Provider of the Year 2005 honors from consulting firm Frost & Sullivan's Asia Pacific Technology Awards 2005, and the PCM Best of IT Awards – Best of Broadband Internet Service Provider Award from *PC Market* magazine, following a readership poll.

Regional industry magazine *Telecom Asia* conferred its Best Broadband Carrier award on PCCW at the 2005 *Telecom Asia* Awards, and Business NETVIGATOR won the Business Internet Service category of the IT Square Editor's Choice 2005 Awards organized by the *Sing Tao* newspaper.

NETVIGATOR also won an Emotive Brand Award in the Mobile/Internet Service category of an awards scheme run by Yahoo!.

In addition, year 2005 saw NETVIGATOR become the first ISP in Asia to acquire BS 15000 certification, the latest worldwide standard for IT&T industry operation processes.

Wi-Fi services

NETVIGATOR customers are able to access the Internet wirelessly at more than 350 Wi-Fi hotspots, making our network of hotspots the most extensive in Hong Kong.

PCCW's wireless Internet-access expertise was further demonstrated when a new service was unveiled to enable passengers onboard Hong Kong's Central-Discovery Bay ferries to go online – the first such wireless broadband Internet-access service in Asia.

NETVIGATOR provides a Wi-Fi service throughout all public areas of Hong Kong International Airport, and many Cathay Pacific travelers are able to enjoy the NETVIGATOR Inflight service, which enables customers to send and receive email while in flight.

now.com.hk

NETVIGATOR provides a total experience in broadband home entertainment – *now.com.hk* for PC users and **NOW TV** for television viewers.

As well as the portal's multimedia platform offering current TV and radio programs, plus music videos and Asian drama, *now.com.hk* has expanded its range of attractions to include a greater variety of opportunities for subscribers to play online games on an e-commerce basis.

Year 2006 will see the *now.com.hk* team adding more attractive content and features, reinforcing the portal's image as Hong Kong's premier Internet-based local multimedia entertainment platform.

NETVIGATOR subscribers are the first in Hong Kong to use an "avatar" feature – co-branded with prominent names in fashion and sportswear – that enables *now.com.hk* users to build an online image from a choice of hairstyles and clothes.

These serve to encourage growth in NETVIGATOR's online community of young, Internet-savvy, broadband users.

PCCW CONSUMER SALES AND CHANNELS

PCCW runs one of the largest and most innovative sales operations in Hong Kong, via channels including retail shops, 24-hour call centers, a direct sales team and partnership sales.



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A chain of PCCW shops showcases the Company as an expert in ICT and offers shoppers total connectivity plus a full range of the latest telecoms, computer and digital products. All our 17 retail outlets have been upgraded to offer a bright, attractive and interactive shopping experience.

Last year, the PCCW chain of shops was named Service Category Leader in Electronic & Electrical Appliances/ Telecommunications by the Hong Kong Retail Management Association Mystery Shoppers Programme. In addition, readers of the *Guangzhou Daily* newspaper have awarded the PCCW shops chain the title, “Hong Kong Merchants of Integrity”, for three consecutive years, including 2006. Our retail outlets also won the newspaper’s My Favourite Top Ten Brands of Hong Kong Award.

For the second consecutive year, our 24-hour call center won a gold award from the Hong Kong Association of Customer Service Excellence, plus a best-in-class award from the Asia Pacific Customer Service Consortium.

PCCW products and services are also taken to consumers by Hong Kong’s largest mobile team of direct sales professionals, while more than 600 business agents act as retail outlets for PCCW phonecards, network services, computer hardware and accessories.

Our direct sales team is committed to upholding the highest professional standards and complies with OFTA’s nine “Best Practice Indicators” designed to provide customers with a positive sales experience.

In fact, the Development for Direct Sales program, run by PCCW Group Training, last year won a Certificate of Merit in the Awards for Excellence in Training recognition scheme

organized by the Hong Kong Management Association.

The increasingly popular and widely-circulated monthly lifestyle magazine, *i.shop*, supports PCCW’s integrated consumer sales channels by publicizing a wide variety of ICT products and services.

BRAND

As a corporate asset of significant value, the PCCW brand went from strength to strength in 2005, thanks to continued demonstration of innovation, quality, a strong customer service ethic and value for money.

Powerful branding is vital in Hong Kong – one of the world’s most competitive telecoms arenas – and regular surveys help us to understand market dynamics and influence purchase decisions.

The five core values behind the PCCW brand – innovation, knowledge, experience, trustworthiness and caring – are analyzed continually to keep in step with the evolving environment in which the Company operates.

For example, a December 2005 study by the TNS market information group, involving nearly 3,000 Cantonese speakers, revealed that PCCW was regarded as “reliable and trustworthy” when compared with bluechip companies of similar standing, and a leader in delivering “innovative products and services that enhance my lifestyle”. Nearly



three-quarters of those surveyed – compared with two-thirds last year – agreed that the latter attribute best described PCCW when ranked against other telecoms service providers.

The same survey identified PCCW as the preferred service provider when respondents were asked to rate five telecoms companies in terms of “has staff that are knowledgeable and helpful when making product and service selection”.

Similarly, 73% of respondents singled out PCCW when asked to rate the telecoms provider that “makes it worth my while to use two or more of its individual services at the same time”.

On the commercial side, the power of the PCCW “motherbrand” was harnessed by the new PCCW Solutions identity created for the Group’s IT services arm, Unihub. The new branding offers a more graphic description of how the division serves customers, while communicating the message that PCCW Solutions is able to call on a diverse wealth of skills, experience and expertise from across the entire PCCW Group.

Similarly, the “motherbrand” was the basis of the new identity for the PCCW Global business unit, formed last year when the international section of PCCW’s Commercial Group was merged with wholly-owned subsidiary BtN Access, Inc.

The same approach was used in early 2006 when the PCCW mobile division was formed to facilitate our return to Hong Kong’s mobile communications scene.

In 2005, the Superbrands Organization named PCCW “Leading Local Brand” and presented the Company with the Telecommunications Category Award for the third consecutive year. In 2004, PCCW was named “Best Local Brand” by Superbrands, an internationally-recognized arbiter of branding with a presence in more than 42 countries.

In addition, PCCW won the Platinum Telecom Company Award in the *Reader’s Digest* SuperBrands Asia 2005 scheme, based on a consumer survey in six Asian markets.

As a socially-responsible corporation on the *FTSE4Good Global Index*, PCCW is committed to contributing to the community, which is reflected by the Company’s “caring” brand attribute. PCCW and its people give practical and financial help to a wide range of charitable, community, cultural and environmental causes in Hong Kong.

CASCADE LIMITED

Energetic pursuit of revenue-generating opportunities with network-reliant organizations around the world resulted in a number of contracts and a significant increase in income last year for CASCADE Limited, PCCW’s technical services subsidiary.

A milestone in 2005 was a contract to provide an end-to-end IPTV solution for True Corporation, a leading telecoms operator in Thailand. The project will serve to reinforce CASCADE’s reputation as a world leader in IPTV technology.



Working in partnership with telecoms equipment vendor Huawei, CASCADE embarked on IPTV projects as far afield as Serbia Montenegro, Ukraine and Morocco. Demand for CASCADE services from operators around the world planning IPTV projects is expected to grow in 2006.

Back in Asia, CASCADE won a contract with the Ministry of Finance of the Negara Brunei Darussalam Government to create network infrastructure interconnecting all government agencies in support of the Sultanate of Brunei's e-government strategy. Other projects were undertaken in Indonesia, Malaysia, Taiwan and Macau.

Closer to home, CASCADE was involved in a number of high-profile projects in Hong Kong and served major customers in mainland China, including PCCW's strategic alliance partner China Netcom Group.

In Hong Kong, CASCADE continues to meet its parent's increasingly complex technology needs and plays a major role in maintaining excellent service quality and developing the products and services that earn PCCW a reputation for innovation on the world stage.

As in previous years, CASCADE collected an array of awards in 2005. These included Gold Awards in all 14 categories of assessment of the Hong Kong Quality Assurance Association Business Performance Index (BPI) Awards scheme, which also conferred eight BPI "Outstanding" certificates on CASCADE. In addition, CASCADE received the Best Practice in Outsourcing Award from the Best Practice Management Group, the Customer Relationship Excellence Award from the Asia Pacific Customer Service Consortium, a Q-Mark Scheme Quality Services License from the Federation of Hong Kong Industries and the Best Vote-canvassing Award for a Quality Improvement Team from the Quality Improvement and Experience Sharing Convention.

CASCADE was also largely responsible for PCCW's "Best International Leased Lines" and "Best International Frame Relay" rankings in the Gartner DataQuest User Survey of all major carriers in Asia Pacific.

By the end of last year, CASCADE's people were holding more than 1,900 certifications, making the PCCW subsidiary one of the most highly-qualified technical services operators in the world. In 2005, CASCADE was also instrumental in NETVIGATOR's BS 15000 certification, which is the latest world standard for operation processes in the IT&T industry. Quality accreditations held by CASCADE include the telecoms-specific TL 9000 standard and BS 7799-2 certification for information security management.

CONTACT CENTERS

The PCCW Contact Center unit provides services and solutions that enable clients to maximize opportunities every time they have contact with their customers.

The unit runs one of Asia's largest and most sophisticated contact-center operations and is the biggest networked contact-center player of its kind in Greater China, with eight networked sites at locations including Beijing, Shanghai, Guangzhou, Shenzhen and Taipei, as well as Hong Kong.

The sites involve 4,000 positions and about 5,000 agents handling millions of inbound and outbound customer calls in 15 languages to serve PCCW's own customers and provide contact-center solutions for large organizations across Greater China.

Many top-tier multinational corporations, such as Nokia, Cathay Pacific and HSBC, are served by a PCCW Contact Centers portfolio that includes operational consultancy, build and design and outsourcing. Research in 2005 showed that the unit delivered between 10% and 30% in cost savings in running customer care programs, and exceeded telemarketing targets.

According to Frost & Sullivan, the compound average growth rate for the contact center outsourcing market in 2008 is set to reach 31.5% in mainland China, 18% in Taiwan and 13.4% in Hong Kong.

PCCW Contact Centers has attracted local and international acclaim for being highly skilled in all forms of customer contact and has won Hong Kong Call Centre Association (HKCCA) awards every year since 2001. In 2005, the unit won a Regional Call Centre Award from the Call Centre Council of Singapore, plus seven HKCCA accolades, including a Bronze Award for the Best Outsourced Call Centre of the Year.

Our contact center business also won a Customer Service Excellence Silver Award from the Hong Kong Association for Customer Service Excellence, and recognition for Best Customer Service in the Guangdong Province. In addition, the unit has been named one of the top-50 teleservices agencies in the world for three consecutive years by Customer Interaction Solutions, a US-based firm specializing in the global call-center industry. Based on 2005 findings, Customer Interaction Solutions ranked PCCW Contact Centers one of the global top-10 service providers in the Interactive Outbound category and one of the world's top-3 Interactive Inbound service providers.

A YEAR OF MAJOR PROGRESS

As well as being influenced by market forces, the Group's results are affected by policies established by the Hong Kong SAR Government and the two regulatory bodies that oversee the telecommunications and media sectors – the Office of the Telecommunications Authority (OFTA) and the Broadcasting Authority (BA).

Prime examples of such policies have been compulsory provision to competitors of our local-loop assets (phonelines into homes and businesses) and the regulation of PCCW as a dominant provider of residential and business-line services. Major progress was made on these, and other issues, in 2005.

Telecoms wholesale services

PCCW continued to provide network-to-network interconnection to other telecoms providers in 2005, with charges generally applied on a per-minute basis. Last year, major per-minute interconnection rates remained unchanged.

The Company also provides Fixed Telecommunications Network Services (FTNS) competitors with access to “last-mile” phonelines between exchanges and customers – a requirement known as “local-loop unbundling” – pursuant to OFTA-approved tariffs and contracts. Interconnection and unbundled local-loop services are provided to competitors on a non-discriminatory basis.

In July 2004, the Government announced that its policy of compulsory local-loop unbundling would be phased out, on a building-by-building basis, no later than June 30, 2008. In 2005, the Company negotiated new wholesale agreements with two major carrier customers, as we continued the

transition of these unbundling arrangements from regulated to commercial agreements. In addition, PCCW provides Internet Service Providers (ISPs) with bandwidth services, pursuant to OFTA-approved tariffs.

Telecoms retail pricing flexibility

In the second half of 2004, OFTA initiated a consultation with a view to changing the regulation of PCCW's pricing activities from ex-ante to ex-post.

OFTA adopted this new regulatory regime on January 13, 2005, with PCCW-HKT Telephone Limited (HKTC) accepting a new ex-post Fixed Carrier license on January 14, 2005. In the ex-post regime, OFTA's prior approval for tariff revisions (including discounts and promotions) is no longer required. Instead, HKTC notifies OFTA of any tariff revisions one day before they become effective.

This modification represents a significant change in OFTA's regulatory approach and has allowed PCCW to compete on a more level playing field. During 2005, the Company launched a variety of promotions and loyalty programs to address competition, with ex-post tariff revisions being employed to enhance operations, introduce new services and support network investment. The significant change in the churn rate in 2005 is, in part, due to the transition from ex-ante to ex-post regulation.

The ex-post regime has also permitted us to de-tariff some services and to increase rates for other services. In addition, no presumption as to the Company's dominance in any market can be drawn from this new license.

Broadband Wireless Access (BWA) services

OFTA launched a public consultation in December 2004 on the licensing framework for deployment of BWA as an alternative to the delivery of both fixed and mobile telecommunications services in Hong Kong. Consultation submissions were filed in mid-March 2005. After considering responses received, OFTA formulated a set of proposals and issued a second consultation paper in August 2005 seeking comments from the industry on the proposals.

PCCW joined 12 other operators in filing a joint submission in November 2005. The filers considered it was premature to discuss details surrounding the implementation of BWA services when the overall Spectrum Policy review (SPR) – which would define BWA spectrum, cover interference management and stipulate rights attached to the spectrum used by BWA and other services – had not yet been conducted. The SPR was recognized as necessary and timely by the Government in 2004. PCCW and the 12 other operators suggested it would be more appropriate for spectrum and convergence policy issues to be decided first in the SPR and in the Fixed Mobile Convergence consultation (*see below*) before detailed matters relating to the use of specific spectrum, such as BWA, were decided. At the time of compiling this report, the SPR had not been commenced and the BWA consultations were still pending.

Fixed Mobile Convergence (FMC)

In anticipation of increasing convergence between fixed-line and wireless services, and the fact that these services are currently being offered under separate licenses, OFTA considered it appropriate to conduct a consultation to examine whether there was a need to revise the existing regulatory regime to cater for converged fixed-mobile services. A consultation paper was issued by OFTA in September 2005. This focused on the terms and conditions associated with a proposed new unified carrier license for converged fixed-mobile services, leaving the more substantive FMC issues to be dealt with under a later consultation. In the joint

submission made by PCCW and 12 other operators in November 2005, the operators argued that it was inappropriate for the terms of the unified carrier license to be discussed before the more substantive FMC issues were resolved. OFTA has now commenced a study on the set of substantive FMC issues.

Voice over Internet Protocol (VoIP)

Year 2005 saw an increasing number of service providers offering VoIP services in the market. A primary use of these services is to enable users to make IDD calls using the public Internet. Another primary use is for the provision of local services. The need to formulate a framework to regulate VoIP services was recognized by OFTA in 2004 when it issued a consultation paper soliciting views from the industry. After considering responses, OFTA issued a statement detailing the regulatory framework for VoIP services in June 2005. Under the statement, VoIP services were permitted to be offered by facilities-based licensees (Class I) or services-based licensees (Class II), each with their own rights and obligations. VoIP services offered by Class I licensees were, however, to possess the same functionality as traditional fixed-line voice services.

Merger and Acquisition Provisions

In 2005, OFTA approved the acquisition of SUNDAY by PCCW and the acquisition of PEOPLES by China Mobile under these provisions. The application from CSL and New World PCS to merge their companies has more recently been approved by OFTA.

Broadcasting services

PCCW's domestic pay-TV service continued to grow in 2005, during which PCCW engaged the Broadcasting Authority on a number of licensing and competition questions with the purpose of requiring competitors to comply with the licensing regime and their specific licenses.

A VISION TO BE GREATER CHINA'S IT SERVICES OPERATOR OF CHOICE

PCCW SOLUTIONS

Operating as PCCW's IT services arm, this division plays a central role in building Hong Kong's image as a world-class digital city.

After helping Hong Kong's leading-edge Smart ID Card become the envy of governments all over the world, PCCW Solutions won a 10-year contract for the total design, provision and on-going maintenance of an e-Passport System for the HKSAR Government's Immigration Department.

In early 2006, the division announced a multi-million-dollar contract with the Treasury of the HKSAR Government for the supply, implementation and maintenance of a highly-sophisticated Government Financial Management Information System (GFMS), plus provision of on-going support and related services. The new system will support all accounting and financial management processes and replace the Ledger Accounting and Financial Information System (LAFIS), and other legacy systems, that have been in use for more than 20 years. The new web-based GFMS will connect about 5,400 users across all government bureaus and departments.

With this and a number of other high-profile projects under way, PCCW Solutions has adopted the vision to become one of the top fully-integrated IT players in Greater China, offering the fullest range of technology-neutral IT services.

A significant development early this year was the change of brand from Unihub to PCCW Solutions – an identity that offers a graphic description of how PCCW's IT flagship serves customers by integrating information, communications and technology to create practical solutions.

The new branding also underscores the message that PCCW Solutions is able to call on a diverse wealth of skills, experience and expertise across the PCCW Group.

The division won business with a number of HKSAR Government departments last year and continues to take on projects to support large Hong Kong manufacturers and retailers in their expansion into mainland China. PCCW Solutions provides state-of-the-art systems that enable clients to run multiple production and retail operations in mainland China from a base in Hong Kong.

Another high-profile deal in 2005 was a three-year contract making PCCW Solutions the preferred IT partner to Dragonair, following highly-successful projects to provide the airline with an iProcurement system, plus financial and HR systems.

In mainland China, PCCW Solutions followed a massive 31-province China Mobile ERP (Enterprise Resource Planning) project with contracts to provide similar solutions for China Netcom Group.

Also in mainland China, the PCCW Solutions Outsource Development Center in Guangzhou is now supporting a number of projects by bringing technologies from all over the world and turning them into practical solutions for customer organizations in Greater China.

In addition, the division's Internet Data Center (IDC) sub-division made significant progress in 2005 to become one of the largest operations of its kind in Hong Kong and mainland China. This valuable element of the PCCW Solutions portfolio has flourished into a design-and-build, as well as a hosting service, and serves customers such as The Bank of East Asia, Amway (China) Co Ltd and ZTE Corporation, one of China's largest providers of telecoms equipment.

PCCW DIRECTORIES

After doubling Internet-related revenues over the last three years, PCCW Directories is now seen as a major player in Hong Kong's Internet advertising industry.

Attracting 23 million page views per month, Internet Yellow Pages (IYP) is one of the most popular portals in Hong Kong and offers customers maximum advertising exposure on the Web. Our IYP customers enjoy one of the best Internet advertising returns on investment the industry has to offer.

The unit also has relationships with other portals in Hong Kong, so is able to provide a one-stop shop to advertisers to help them achieve maximum impact in reaching customers.

For example, regular tracking surveys show that as many as 82% of end customers find what they want when searching PCCW Directories' optimized online advertising set-up in Hong Kong. Of that proportion, about 98% are known to contact advertisers involved and approximately half end up making a transaction.

IYP was relaunched in early 2006 with significantly enhanced search and user interface capabilities, which were positively received by the Internet community and are expected to lead to even better return on advertising investment for our customers.

In 2005, a partnership with Yahoo! Hong Kong continued to flourish, while similar arrangements with Internet giant Google are slated for 2006.

Approximately one million directories and supplements, including the English and Chinese-language versions of both Consumer and Business Yellow Pages publications, were printed in 2005. For the second year running, our Yellow Pages Consumer publication won the Directories category of the US Gold Ink Award, while the Business edition achieved a gold-standard Superb Printing Award, organized by the International Association of Printing House Craftsmen in the US.

With more than 80,000 registered users, the in-house-developed YP Card continues to make Yellow Pages advertisers more visible and attractive to affluent consumers by offering special deals and discounts from more than 2,000 merchant outlets.



A GROWING PRESENCE AROUND THE WORLD



PCCW GLOBAL

In October 2005, the merging of the international section of PCCW's Commercial Group and wholly-owned subsidiary BtN Access, Inc. (see following section) resulted in PCCW Global – a new worldwide business unit positioned to optimize synergies between the two businesses.

As well as expanding the Company's share of the international business market and reinforcing PCCW's image as an industry leader in Asia, the new unit plays a key role in capturing emerging opportunities in high-growth markets overseas.

PCCW Global enables organizations to bring their business to Asia, run operations across the region and take Asian business to the rest of the world. The unit is particularly well placed to assist multinational corporations and enterprises to enter Greater China, thanks to long-standing relationships with a diversity of major mainland China-based carriers.

Able to reach virtually any part of the world, PCCW Global addresses markets in North America, Europe, the Middle East and Africa, as well as in Asia. In addition, the unit has signed Internet connectivity contracts to serve major telecoms carriers in Egypt, Ukraine, Kuwait, Brazil and Mexico, and also supports top US-based Internet content providers with hosting services.

PCCW Global offers a wide portfolio of products and services based on leading-edge technology in international data and voice solutions and cost-effective value-added and managed services, as well as a range of network monitoring services. An example of a growing enterprise market opportunity for PCCW Global in the US and Europe is a hosted PBX (Private Branch Exchange) solution that replaces a company's traditional PBX and supports highly cost-effective Voice-over-Internet Protocol (VoIP) services. Another growing part of PCCW Global's business is the provision of wholesale voice services using VoIP.

The unit's IP-VPN solution, built over Asia's largest backbone, and a technology-independent MPLS (Multi-Protocol Label Switching) network, are able to provide state-of-the-art reach to more than 700 cities in more than 70 countries.

Growth was recorded in VPN (Virtual Private Network) and GIA (Global Internet Access) business in 2005, while traditional International Private Leased Circuits (IPLC) sales continued to perform well.

PCCW Global's industry credibility was reinforced in 2005 by the "Best International Leased Lines" and "Best International Frame Relay" titles from Gartner's User Survey of international data services. This was the second consecutive year that the "Best International Leased Lines" title had been awarded to PCCW.

BtNAccess

Prior to the launch of PCCW Global (see preceding section) in October 2005, BtNAccess, Inc. served customers in various parts of the world as a market leader in IP communications after being created in 2003 by the amalgamation of PCCW's Beyond the Network and Corporate Access units.

Headquartered in the US and Hong Kong, and operating across North America, the Middle East, Europe, Africa and Asia, BtNAccess offered solutions including a hosted PBX service, an international MPLS network, wholesale VoIP and dedicated Internet access and hosting for enterprises.

BtNAccess also provided VSAT (Very Small Aperture Terminal) satellite solutions for voice and data communications in remote areas of the world not served by conventional fixed or wireless networks.

PCCW Global was formed when BtNAccess was merged with the international section of PCCW's Commercial Group.

REACH

A 50:50 joint venture between PCCW and Australia's Telstra Corporation Limited (Telstra), REACH supports the international service offerings of the two parents by operating the most extensive international connectivity network in Asia. REACH is the region's premier provider of international voice,

data and satellite services and one of the world's largest carriers of international voice traffic, according to Telegeography, a research and analysis company.

In April, REACH became an outsourcer of network services for the joint-venture partners and ceased to pursue data service sales to third parties. Such services have since been retailed directly by PCCW and Telstra, with REACH continuing to provide voice and satellite services to the parents, as well as to third parties.

In September 2005, and for the fifth consecutive year, independent research firm Gartner ranked REACH top IP backbone operator in Asia, in terms of intra-Asia connectivity. In addition, the REACH IP network was last year's highest-ranked Asian carrier in a performance league-table compiled by the Netconfigs network management resource.

REACH also played a major role in PCCW's award of "Best International Leased Lines" and "Best International Frame Relay" titles by Gartner's DataQuest User Survey: International Telecom Services Asia Pacific 2005 scheme.

Dr Beng Yeoh was appointed Chief Executive Officer by the REACH Board of Directors, with effect from September 1, 2005. Dr Yeoh was previously Vice President of Network Services and Applications for Motorola Networks, Asia Pacific.



UK BROADBAND

A phased rollout of a pioneering wireless broadband Internet service into various areas of London and a new and well-received brand were two highlights of the year for UK Broadband Limited, a wholly-owned PCCW subsidiary.

The innovative plug-and-play service – branded **NOW** (www.now.com) – continues to draw positive results in user surveys of a steadily-increasing customer-base and has proved competitive with fixed-line broadband service in the UK. Studies in the Thames Valley, west of London, found that nearly 90% of users were either satisfied or very satisfied.

NOW provides wireless broadband to the home and office without the need of a fixed telephone line and offers download speeds of 256 Kbps, 512Kbps or 1Mbps.

As a world leader in wireless broadband, the **NOW** team made significant progress last year to establish the optimum solution for an industry-challenging technology, while continuing to build value around PCCW's radio spectrum rights in the UK.

Year 2005 also saw UK Broadband increase coverage area fourfold and double customer numbers at the same time as testing a new **NOW** wireless data card for laptops to allow greater portability in the home or outdoors.

Holding licenses to provide a nationwide wireless broadband network service in the UK, PCCW is generating valuable expertise that could be applied in other parts of the world such as mainland China and elsewhere in Asia.

INFRASTRUCTURE

PACIFIC CENTURY PREMIUM DEVELOPMENTS

Majority owned by PCCW, Pacific Century Premium Developments Limited (PCPD) is principally engaged in the development and management of premium property and infrastructure projects, as well as investment in premium-grade buildings in Asia.



AIMING FOR EXCELLENCE IN TRAINING

PCCW continues to place great emphasis on training and developing all employees to ensure our customers enjoy leading-edge and innovative services with best-in-class quality. In 2005, more than 34,000 “man-days” of training were provided, an increase of 30% compared with 2004.

Employee development to enable growth

Every PCCW manager is aware of the importance of fostering employee development and growth. For example, a senior management team led a number of People Development Forum events for reviews of executive leadership development in 2005. At business and functional unit level, more than 400 managers’ abilities and development plans to take up different roles or new assignments were discussed. Tailor-made development programs, particularly those relating to business leadership, were organized in various business units to ensure that the Group has enough managers in the pipeline to maintain growth.

Nine senior managers attended executive development programs organized by the INSEAD global business school and Hong Kong University of Science and Technology in pursuit of excellence in managerial and business practices.

The Challenge21 Leadership Development Program was organized as part of the Group’s continued efforts to prepare high-performing young leaders to succeed in bigger roles. In 2005, the program helped produce 36 high-performing middle managers.

In 2005, e-curriculum was launched to help line managers and employees take advantage of training and learning opportunities through online enrollment of programs designed for individual business units. Apart from tutor-led programs, employees all over the world made use of online training programs from the Group’s in-house Aladdin Learning Portal, which provided IT&T, business and management training in English and Putonghua. Employees benefited from some 2,200 online training programs.

More than 140 young employees took part in trainee schemes to help the Company maintain a flow of talent and future leaders to meet the capability requirements of business units. These fast-track schemes included structured training programs, job rotation, mentoring and development meetings with senior managers, and attracted young graduates with career aspirations in professional engineering, IT, sales and management.

Business and management training – at the leading edge

More than 16,000 “man-days” of business and management training were provided across the Group to develop skills in sales, marketing, consultancy, service and management.

1. Sales excellence

The Company continued to channel effort into enhancing the power of sales teams. More than 180 sales-related training programs were made available to sales forces, involving more than 3,600 professionals within the Group.

Programs focused on sales skills relating to call centers, major strategic accounts, territories and roadshows to support business development in commercial and consumer markets.

In addition, the Development for Direct Sales program won a Certificate of Merit as part of the Awards for Excellence in Training 2005 recognition scheme, organized by the Hong Kong Management Association.

2. Management practices

People management training programs designed to cultivate a performance-driven culture in PCCW were organized for more than 520 newly-promoted or recruited supervisors/managers from Commercial Group, Consumer Group, CASCADE, Contact Center Business and PCCW Solutions.

To promote and develop a systematic approach to innovation, the world-class *Six Thinking Hats* training program was organized for managers from various business units.

A structured mentoring program dubbed *Little Moments, Big Magic* saw 28 senior managers in Commercial Group taking on the role of mentor to coach more than 100 up-and-coming managers to give them developmental support and help them broaden perspectives.

A Team Leadership Training Program under the title *Building a Competitive Team* was provided to 850 supervisors and managers in CASCADE to help encourage effective team leadership practices, with upward feedback helping to bring about improvements in managerial practices.

Keeping the Company at the forefront of ICT

In 2005, more than 18,000 "man-days" of technology and product training were provided, covering fields such as Enterprise Application Interface (EAI), wireless and IP networking.

1. Technology training (IT)

To ensure our PCCW Solutions colleagues are equipped with knowledge of the latest enterprise IT-solution technologies, the Company provides training in different software applications, such as the BEA system and TIBCO, as well as applications relating to billing and order management systems.

Implementation of best practice is another primary focus, especially in enterprise software applications support and management. In 2005, we certified more than 50 staff, based on the PCCW Solutions IT Infrastructure Library (ITIL), following training programs.

2. Technology training (communications technology)

Technology training ensures our technical professionals are up to speed on the latest developments in areas such as mobile communications and broadband. Specific mobile cell-site planning workshops, initiatives on new broadband equipment and VoIP equipment training were arranged for more than 500 of our technicians.

To support PCCW's return to the mobile market, internal seminars on mobile technology, future trends in Fixed Mobile Convergence (FMC) and the Next Generation Network (NGN) were organized by Sales and Solutions consultants in Commercial Group and CASCADE.

3. Company and professional/practitioner accreditation

The Company helped individuals attain more than 2,000 industrial certificates, including qualifications in relation to Foundation Certification in IT-service Management, IT Infrastructure Library (ITIL) Manager Certification, BEA 8.1 Certified Administrator, Check Point Certified Security Administrator, Certified Oracle Database Administrator, Certified Information System Auditor, Microsoft Certified System Engineer and Certified Project Management Professional and Certified Security Professional, plus PRINCE2 Practitioner and Sun certification.

By the end of 2005, 95 staff members had attained Professional/Chartered Engineer status.