- Profit attributable to equity holders increased 2.5% to HK$1,595 million
- Final dividend of 12 HK cents per share
- Net fixed line gain of 50,000 in the second half of 2005
- now TV's subscription base reached 549,000

MANAGEMENT REVIEW

PCCW reported profit attributable to equity holders of the Company of HK$1,595 million for the year ended December 31, 2005, a 2.5% increase compared to 2004. The Board of Directors of PCCW (the "Board") has recommended the payment of a final dividend of 12 HK cents per share for the year ended December 31, 2005, subject to the approval of shareholders of the Company at the forthcoming annual general meeting.

2005 was a dynamic year for PCCW. The Group proved to be a successful turnaround telecoms operator amongst other incumbents around the world in a post-liberalization era. The new fixed carrier license granted at the beginning of 2005 to PCCW-HKT Telephone Limited ("HKTC"), an indirect wholly-owned subsidiary of PCCW, gave rise to a more level playing field and enabled HKTC to react to market changes more flexibly. The Group's effective customer win-back campaign and its premium quality of products and services continued to differentiate it from its competitors. On a net basis, the Group added 50,000 fixed lines in the second half of 2005, compared to a loss of 53,000 lines in the first half of 2005, and a loss of 212,000 lines in year 2004.

now TV continued to gain momentum, driving growth for the Group's broadband business. As at December 31, 2005, now TV's subscription base reached 549,000 and the Group's total broadband access lines grew by 20% year-on-year to 953,000. In addition to the long-term exclusive contracts secured with premier content providers, including ESPN, Satellite Television Asian Region Limited (STAR), HBO Pacific Partners (HBO) and Mei Ah Entertainment Group Limited, PCCW further enriched the local Chinese content by announcing a long-term carriage agreement with Galaxy Satellite Broadcasting Limited in February 2006 to distribute TVB PAY VISION service, including eight TVB-produced channels, on now TV's platform. Further, on March 20, 2006, now Business News Channel ("now BNC"), a self-produced premium quality Cantonese financial news channel, was launched.

Consolidated revenue for the year ended December 31, 2005, excluding Bel-Air, increased 1% compared to 2004, to HK$17,678 million. The Group's telecommunications services ("TSS") division, after consolidating the post-acquisition results for SUNDAY Communications Limited ("SUNDAY") in the second half of 2005, reported a 4% year-on-year growth in revenue, to HK$15,931 million.

The Group continued to exercise cautious cost control and saved 9% in total operating costs before depreciation and amortization by increasing corporate overhead efficiency and overall productivity level; and streamlining certain loss-making businesses.

As a result, group EBITDA margin improved to 30% while TSS EBITDA margin was diluted to 42.6% after including SUNDAY's results in the second half of 2005. Excluding SUNDAY's results, TSS EBITDA margin remained fairly stable at 44.1%.

The Group has changed certain of its accounting policies following its adoption of the new Hong Kong Financial Reporting Standards, Hong Kong Accounting Standards and Interpretations (collectively referred to as the "new HKFRSs"), which are effective for the accounting periods beginning on or after January 1, 2005. None of these changes affect the Group's underlying business operations or cashflow. Comparative figures in 2004 have been restated as required to conform with the new HKFRSs.

Under the new HKFRSs, the Group recorded HK$4,821 million of revenue from Bel-Air sales in 2005, a 11% decline compared to 2004. The new accounting policy delayed revenue recognition of Bel-Air units pre-sold on or after January 1, 2005 until when the properties would be completed. As a result, consolidated revenue for the year ended December 31, 2005, including Bel-Air, decreased 2% to HK$22,499 million.

In 2005, PCCW successfully re-entered the mobile market by acquiring an aggregate 79.35% stake in SUNDAY for a total cash consideration of HK$1,542 million. This transaction made PCCW a fully integrated operator with the ability to offer quadruple-play services including fixed line, broadband Internet, pay-TV and mobile services. It also enabled PCCW to progress its planning towards Fixed Mobile Convergence services in the future and strengthened its ability to be the preferred mobile partner in mainland China of China Network Communications Group Corporation ("China Netcom Group").

In January 2006, the Group introduced a six-month trial of its 3G services. This introductory trial has received a phenomenal response and about 110,000 users have been selected, most of whom are now connected to PCCW mobile's 3G services. It allows management to stress-test the 3G network and to better understand the market dynamics and customer behavior, hence minimizing the industry risk upon commercial launch.

A year after China Netcom Group acquired an approximately 20% stake of the Company, discussions between PCCW and China Netcom Group have progressed satisfactorily on business opportunities including broadband, property, directories and mobile businesses.

FINANCIAL REVIEW BY SEGMENTS

For the year ended December 31, HK$ million	2005 H1	2005 H2	2005 Full Year	2004 (Restated)[3] H1	2004 (Restated)[3] H2	2004 (Restated)[3] Full Year	Better/ (Worse) y-o-y
Revenue							
TSS	7,497	8,434	15,931	7,549	7,785	15,334	4%
Business eSolutions[1]	1,323	1,131	2,454	1,312	1,389	2,701	(9)%
Infrastructure	3,352	1,802	5,154	2,321	3,542	5,863	(12)%
Bel-Air	*3,179*	*1,642*	*4,821*	*2,096*	*3,319*	*5,415*	*(11)%*
Infrastructure (ex. Bel-Air)	*173*	*160*	*333*	*225*	*223*	*448*	*(26)%*
Others	160	152	312	194	178	372	(16)%
Elimination	(631)	(721)	(1,352)	(597)	(671)	(1,268)	(7)%
Total Revenue	11,701	10,798	22,499	10,779	12,223	23,002	(2)%
Cost of sales	(5,893)	(4,574)	(10,467)	(4,536)	(5,995)	(10,531)	1%
Operating costs before depreciation and amortization	(2,571)	(2,811)	(5,382)	(3,065)	(2,840)	(5,905)	9%
EBITDA[2]							
TSS[4]	3,335	3,445	6,780	3,347	3,491	6,838	(1)%
Business eSolutions[1]	27	4	31	72	16	88	(65)%
Infrastructure	322	376	698	358	416	774	(10)%
Bel-Air	*230*	*309*	*539*	*213*	*337*	*550*	*(2)%*
Infrastructure (ex. Bel-Air)	*92*	*67*	*159*	*145*	*79*	*224*	*(29)%*
Others	(447)	(412)	(859)	(599)	(535)	(1,134)	24%
Total EBITDA	3,237	3,413	6,650	3,178	3,388	6,566	1%
Group EBITDA Margin	28%	32%	30%	29%	28%	29%	1%
EBITDA Margin (ex. Bel-Air)	35%	34%	35%	34%	34%	34%	1%

OPERATING DRIVERS	2005 H1	2005 H2	2004 H1	2004 H2	Better/ (Worse) y-o-y
Exchange lines in service ('000)	**2,514**	**2,564**	2,662	2,567	0%
Business lines ('000)	**1,127**	**1,164**	1,175	1,144	2%
Residential lines ('000)	**1,387**	**1,400**	1,487	1,423	(2)%
Fixed line market share[5]	**67%**	**68%**	70%	68%	0%
Business lines	**68%**	**69%**	71%	69%	0%
Residential lines	**65%**	**66%**	70%	67%	(1)%
New Generation Fixed-Line ("NGFL") sign-ups ('000)	**972**	**994**	849	969	3%
now TV installed ('000)	**441**	**549**	269	361	52%
Total broadband access lines ('000)	**857**	**953**	753	796	20%
(Consumer, business and wholesale customers)					
Retail consumer broadband subscribers ('000)	**715**	**798**	558	660	21%
Retail business broadband subscribers ('000)	**80**	**88**	68	74	19%
Consumer narrowband subscribers ('000)	**139**	**132**	160	148	(11)%
Traditional data (Exit Gbps)	**262**	**294**	211	234	26%
Retail International Direct Dial ("IDD") minutes[6] ('M mins)	**741**	**786**	661	722	10%
International Private Leased Circuit ("IPLC") bandwidth (Exit Mbps)	**6,503**	**10,175**	4,822	6,020	69%

Note 1 *Business eSolutions included the Information and Communications Technologies ("ICT") services business provided under PCCW Solutions Limited ("PCCW Solutions") (formerly known as Unihub Limited ("Unihub")), retail business broadband and the Group's directories businesses.*

Note 2 *EBITDA represents earnings before interest income, finance costs, income tax, depreciation, amortization, gain/loss on disposal of property, plant and equipment, investment properties and interests in leasehold land held for own use under operating leases, net other gains, provisions for impairment losses, restructuring costs, impairment losses on interests in jointly controlled companies and associates and the Group's share of results of jointly controlled companies and associates. While EBITDA is commonly used in the telecommunications industry worldwide as an indicator of operating performance, leverage and liquidity, it is not presented as a measure of operating performance in accordance with the new HKFRSs and should not be considered as representing net cash flows from operating activities. The computation of the Group's EBITDA may not be comparable to similarly titled measures of other companies.*

Note 3 *2004 figures were restated in accordance with the new HKFRSs effective January 1, 2005.*

Note 4 *2005 second half TSS EBITDA included SUNDAY's EBITDA of HK$25 million.*

Note 5 *Year-on-year percentage change was based on absolute percentage change.*

Note 6 *Year-on-year percentage change was based on total IDD minutes for the year.*

Note 7 *Gross debt refers to the principal amount of short-term borrowings and long-term liabilities. Net debt refers to the principal amount of short-term borrowings and long-term liabilities minus cash and cash equivalents.*

TSS

TSS, leveraging on the new fixed carrier license granted by OFTA in January 2005, continued to actively manage its business and operations in response to the challenging operating, competitive and regulatory environment in Hong Kong's telecommunications market. PCCW's innovative NGFL services, and now TV, continued to bring enhanced features to its customers and the quality of service is seen as a key differentiator against competitors.

TSS revenue for the year ended December 31, 2005 increased 4% to HK$15,931 million after consolidating the post-acquisition results of SUNDAY in the second half of 2005. Excluding SUNDAY's results, TSS revenue maintained solid at HK$15,333 million.

For the year ended December 31, HK$ million	2005 H1	2005 H2	2005 Full Year	2004 (Restated)[3] H1	2004 (Restated)[3] H2	2004 (Restated)[3] Full Year	Better/ (Worse) y-o-y
Local Telephony Services	2,462	2,400	4,862	2,739	2,671	5,410	(10)%
Local Data Services	2,219	2,275	4,494	2,164	2,222	4,386	2%
International Telecommunications Services	1,167	1,166	2,333	1,176	1,209	2,385	(2)%
Other Services	1,649	2,593	4,242	1,470	1,683	3,153	35%
TSS Revenue	7,497	8,434	15,931	7,549	7,785	15,334	4%
Cost of sales	(2,175)	(2,757)	(4,932)	(2,006)	(2,268)	(4,274)	(15)%
Operating costs before depreciation and amortization	(1,987)	(2,232)	(4,219)	(2,196)	(2,026)	(4,222)	0%
TSS EBITDA[4]	3,335	3,445	6,780	3,347	3,491	6,838	(1)%
TSS EBITDA Margin	44%	41%	42.6%	44%	45%	44.6%	(2)%
TSS EBITDA Margin (ex. SUNDAY)	44%	44%	44.1%	44%	45%	44.6%	(0.5)%

Local Telephony Services. In January 2005, OFTA issued a new fixed carrier license to HKTC, moving it from ex-ante to ex-post regulation. The Group is no longer required to obtain prior approval of tariff revisions, but merely notifies the regulator one day before the changes become effective. Various targeted marketing programmes were launched to retain and win-back fixed line customers. As a result, the Group gained 50,000 fixed lines in the second half of 2005 on a net basis, compared to a net loss of 53,000 fixed lines in the first half of 2005 and a net loss of 212,000 fixed lines in 2004.

The Hong Kong fixed line market is highly saturated and due to the economic downturn in previous years, the total number of direct exchange lines declined by around 1-2% per annum since 2001. For the year of 2005, according to industry statistics provided by OFTA and the Group's estimate, the total number of direct exchange lines increased marginally by 0.3% compared to the 1% contraction in 2004. At the end of 2005, PCCW operated a total of 2,564,000 direct exchange lines compared to 2,567,000 lines in 2004, with an overall market share maintained at 68% year-on-year but improved from 67% in June 2005.

Revenue from local telephony services for the year ended December 31, 2005 decreased 10% year-on-year to HK$4,862 million. The lower revenue was partly due to the 8% net line loss in 2004 as a result of the competition from other network operators, and substitution by broadband access lines and wireless telecommunications services.

After the Government announced in July 2004 that the Type II interconnection policy for local fixed-line telecommunications services would be phased out in stages by June 30, 2008, at which time interconnection terms between operators would be subject to commercial negotiation, certain network operators leased fewer local access lines from the Group, resulting in a further decline in local telephony services revenue.

In December 2005, the Group has entered into long-term service supply agreements with two of the major network operators where interconnection arrangements are set at agreed commercial terms. This follows a similar agreement reached in 2004 with the third major network operator.

Local Data Services. Local data services revenue for the year ended December 31, 2005 increased 2% year-on-year to HK$4,494 million. Demand for broadband products and services continued to be strong and churn rate remained low as subscription of now TV increased customer loyalty. Total broadband access lines grew by 20% to 953,000 as at December 31, 2005 while now TV subscription base increased by 52% to 549,000. Increase in broadband and now TV revenue was partially offset by the decline in revenue due to severe pricing pressure in the provision of local area and wide area (LAN and WAN) corporate networks, and high-speed, high-volume data transmissions from mobile telephone operators and Internet service providers.

International Telecommunications Services. International telecommunications services revenue for the year ended December 31, 2005 decreased 2% year-on-year to HK$2,333 million. This market continued to be competitive driving down retail prices while traffic volume rose strongly. IPLC bandwidth sold increased by 69% while retail outgoing IDD minutes traffic increased 10% year-on-year. Unit prices of IPLC, IDD and other international data products were lower than those in 2004, in line with the global market trend.

In October 2005, the Group restructured its international businesses to form a new business unit, PCCW Global. Leveraging on PCCW's brand name, the new division will focus on maintaining PCCW's competitive position in Asia, improving its global marketing effort as well as capturing emerging opportunities in targeted high growth markets overseas.

Other Services. Other services revenue, including the post-acquisition results of SUNDAY in the second half of 2005, increased 35% to HK$4,242 million. Excluding SUNDAY, other services revenue increased 16% primarily due to an increase in customer premise equipment ("CPE") sales during the year and increase in revenue from certain international connectivity businesses.

For more information about the performance of SUNDAY, please refer to its 2005 annual results released on March 29, 2006.

Business eSolutions[1]

Business eSolutions included PCCW Solutions (formerly known as Unihub), the Group's ICT business in Hong Kong and mainland China provisioned under one new brand name; retail business broadband; the business undertaken by Unihub China Information Technology Company Limited, the Company's subsidiary co-owned with China Telecommunications Corporation; and the Group's directories business in Hong Kong and mainland China. Business eSolutions revenue for the year ended December 31, 2005 decreased 9% to HK$2,454 million. A lower revenue contribution from PCCW Solutions, due mainly to delays in award of certain major contracts, was partially offset by an increase in revenue from retail business broadband.

Infrastructure

Infrastructure revenue primarily represented the contribution from Pacific Century Premium Developments Limited ("PCPD"), the Company's majority-owned property subsidiary. Bel-Air sales continued to be strong, riding on the buoyant economy and the renewed interest in the luxury residential sector in Hong Kong.

Revenue for the year ended December 31, 2005 decreased 12% to HK$5,154 million mainly due to the change in accounting policy on revenue recognition of Bel-Air sales from percentage of completion basis to full completion basis in accordance with the new HKFRSs. Revenue from Infrastructure, excluding Bel-Air, dropped 26% as a result of the disposal of PCCW Tower in February 2005.

The Company converted Tranche A of the Convertible Notes (as defined in the shareholder circular of the Company dated March 26, 2004) issued by PCPD on May 10, 2004 with the principal amount of HK$1,170 million effective March 1, 2005. The stake of the Group in PCPD was approximately 61.66% as of December 31, 2005.

For more information about the performance of PCPD, please refer to its 2005 annual results released on March 29, 2006.

Others and Elimination

Other revenue primarily included revenue from the Group's businesses in Taiwan and Japan. The Group continued to streamline certain non-core businesses including JALECO Ltd. ("JALECO"), the Group's gaming business in Japan. On August 19, 2005, the Group disposed of its 79.72% interest in JALECO for a consideration of approximately US$48 million or HK$375 million, at a gain of approximately HK$159 million. Thus, other revenue decreased 16% to HK$312 million.

Elimination of HK$1,352 million predominantly relates to internal charges for communications services consumed, IT support and computer system network charges, customer support services and facilities management services between the Group's business units.

COSTS

Total cost of sales for the year ended December 31, 2005 decreased slightly to HK$10,467 million. The lower cost of the Cyberport project recognized under the new HKFRSs was partially offset by the higher cost of sales in relation to now TV, higher CPE sales and increased revenue from certain international connectivity businesses. TSS costs of sales included post-acquisition cost of sales for SUNDAY in the second half of 2005.

For the year ended December 31, HK$ million	2005	2004 (Restated)[3]	Better/ (Worse) y-o-y
Staff costs	**2,677**	2,996	11%
Repair and maintenance	**369**	358	(3)%
Other operating costs	**2,336**	2,551	8%
Total operating costs before depreciation and amortization	**5,382**	5,905	9%
Depreciation and amortization	**2,694**	2,535	(6)%
Gain on disposal of property, plant and equipment, investment properties and interests in leasehold land held for own use under operating leases	**(24)**	(56)	(57)%
General and administrative expenses	**8,052**	8,384	4%

The Group achieved 9% savings in total operating costs before depreciation and amortization. Corporate overhead efficiency was further improved and certain non-core businesses including the gaming business in Japan were streamlined. TSS operating costs also included post-acquisition operating costs from SUNDAY in the second half of 2005.

EBITDA[2]

Group EBITDA for the year ended December 31, 2005 increased 1% year-on-year to HK$6,650 million and Group EBITDA margin increased slightly to 30%.

TSS EBITDA[4] for the year ended December 31, 2005 decreased 1% to HK$6,780 million while TSS EBITDA margin was slightly diluted to 42.6% after consolidating the post-acquisition results for SUNDAY in the second half of 2005. Excluding SUNDAY's results, TSS EBITDA remained fairly stable at 44.1%.

OTHER GAINS, NET

Net other gains of HK$626 million for the year ended December 31, 2005 primarily included net realized and unrealized gains on cross currency swap contracts and on certain investments of the Group; and gain on disposal of the Group's interests in JALECO; net of provision made for rental guarantee (note 8(a) of the financial statements).

INTEREST INCOME AND FINANCE COSTS

Interest income increased eight times to HK$533 million for the year ended December 31, 2005 mainly due to the higher average cash balance maintained by the Group. Finance costs increased 11% to HK$2,234 million for the year ended December 31, 2005 primarily due to the interest and premium paid for the early repurchase of the Yen 30,000 million 3.65% guaranteed notes due 2031; and the finance costs incurred by SUNDAY included in the second half of the year. Average cost of debt for 2005 was 6.7%.

SHARE OF RESULTS OF ASSOCIATES

Share of results of associates of HK$120 million for the year ended December 31, 2005 primarily represented the Group's share of associate's realized and unrealized gain on its investment in MobileOne Ltd ("MobileOne"). On October 28, 2005, the Group disposed of its entire indirect interest in MobileOne at a disposal gain of approximately HK$52 million.

TAXATION

Taxation expenses for the year ended December 31, 2005 increased 10% to HK$1,103 million primarily due to the increase in profit before taxation. The Group's effective tax rate for the year ended December 31, 2005 was 37% (2004: 39%). This rate is higher than the statutory tax rate of 17.5% mainly due to the fact that losses of some companies cannot be offset against profits of other companies for Hong Kong tax purposes and the disallowance of financing costs relating to the financing of non-income-producing assets. Excluding these factors, the Group would have an effective tax rate around the statutory tax rate of 17.5%.

MINORITY INTERESTS

Minority interests of HK$272 million primarily represented the net profit attributable to the minority shareholders of PCPD. The minority interests of HK$20 million in 2004 was net of the share of loss from the Group's Japan and Taiwan businesses.

LIQUIDITY AND CAPITAL RESOURCES

Net cash inflow from operating activities decreased to HK$4,639 million for the year ended December 31, 2005 from HK$5,103 million in 2004. This was primarily due to an increase in restricted cash balance (note 27(b) of the financial statements) and tax paid for the year.

The Group continued to deleverage and reduced gross debt[7] to HK$29,165 million as at December 31, 2005. Cash and cash equivalents increased to HK$9,679 million. HKTC had a total of HK$10,800 million committed medium-term revolving credit facilities, of which HK$4,300 million remained undrawn at year end 2005. The Group's net debt[7] reduced by 26% year-on-year to HK$19,486 million as at December 31, 2005.

In February 2005, PCCW Tower, the Group's headquarters in Hong Kong, was disposed of at a cash consideration of HK$2,808 million.

In March 2005, the shareholders of PCCW approved the strategic alliance transaction between the Company and China Netcom Group whereby China Netcom Group paid approximately HK$7,927 million in cash for an approximately 20% stake of the Company.

Subsequent to the first distribution of the net surplus proceeds of the Cyberport project between the Government and the Group in August 2004, the Group received further distributions in June and September 2005 for an aggregate amount of HK$727 million, thus increasing the Group's balance of cash and cash equivalents.

On June 22, 2005, the Group acquired approximately 59.87% of SUNDAY at a cash consideration of HK$1,164 million. Under the requirements of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules") and the Hong Kong Code on Takeovers and Mergers, a mandatory unconditional cash offer was triggered. Upon the closing of the offer on September 9, 2005, the Group's shareholding in SUNDAY was increased to approximately 79.35% at an additional cash investment of approximately HK$378 million.

In July 2005, the Group also provided financial resources to SUNDAY and its subsidiaries (the "SUNDAY Group") to repay the loans and to refinance the performance bonds outstanding under the facilities previously arranged with Huawei Tech. Investment Co., Limited (the "Huawei Facilities"). The Group and SUNDAY Group entered into long-term inter-company loan facilities whereby the SUNDAY Group was provided with the required funding aggregating approximately HK$874 million for full repayment and cancellation of the Huawei Facilities. Management of the Company believes that the Huawei facilities were relatively cost ineffective to the Group.

The Group continued to prudently manage its debt profile and the following financing activities took place in 2005:

- Redemption of US$54 million 5% mandatory convertible note due to Telstra Corporation Limited ("Telstra Note") on June 30, 2005.
- Repurchase and cancellation of the Japanese Yen 30,000 million 3.65% guaranteed notes on June 30, 2005.
- Issuance of US$500 million 5.25% guaranteed notes due 2015 on July 20, 2005.
- Redemption of US$1,100 million 3.5% guaranteed convertible bonds due 2005 on December 5, 2005, plus redemption premium.

As at December 31, 2005, the Group's gross debt[7] to total assets was 54.7%.

CREDIT RATINGS OF HKTC

As of December 31, 2005, HKTC had investment grade ratings from Standard & Poor's Ratings Services (BBB/Positive), Moody's Investors Service (Baa2/Stable) and Fitch Ratings (BBB+/Negative).

CAPITAL EXPENDITURE

Consolidated capital expenditure for the year ended December 31, 2005 was HK$2,441 million (2004: HK$1,972 million), including SUNDAY's capital expenditure of HK$210 million in the second half of 2005 but excluding the indefeasible rights to use the international undersea cable capacity and other related equipment acquired from REACH Ltd. ("REACH") of HK$1,627 million. The majority of capital expenditure was spent on meeting demand of new products and services, such as now TV, and on new initiatives including the Group's IP Network, UK Broadband project, NGFL services and broadband network expansion.

PCCW has made significant investment in its communications network in previous years. This included the upgrade and expansion of network coverage, and building a platform for broadband and fast developing IP initiatives. Besides on-going core network expansion, the capital expenditure in 2006 will include development of the full IP Network, mobile network services and other new products and services. PCCW will continue to invest prudently, using assessment criteria including internal rate of return, net present value and payback period.

HEDGING

Market risk arises from foreign currency exposure and interest rate exposure related to cash investments and borrowings. As a matter of policy, the Group continues to manage the market risk directly relating to its operations and financing and does not undertake any speculative derivative trading activities. The Finance and Management Committee, a sub-committee of the Executive Committee of the Board, determines appropriate risk management activities undertaken with the aim of managing prudently the market risk associated with transactions undertaken in the normal course of the Group's business. All treasury risk management activities are carried out in accordance with policies and guidelines approved by the Finance and Management Committee and the Executive Committee of the Board, which are reviewed on a regular basis.

In the normal course of business, the Group enters into forward contracts and other derivative contracts in order to limit its exposure to adverse fluctuations in foreign currency exchange rates and interest rates. These instruments are executed with creditworthy financial institutions, and all contracts are denominated in currencies of major industrial countries. Gains and losses on these contracts serve as hedges in that they offset fluctuations that would otherwise impact the Group's financial results. Costs associated with entering into such contracts are not material to the Group's financial results.

CHARGE ON ASSETS

As at December 31, 2005, certain assets of the Group with an aggregate carrying value of HK$62 million (2004: HK$67 million) were pledged to secure loan and borrowing facilities utilized by the Group.

Certain quoted investments, with an aggregate value of HK$178 million (2004: HK$224 million), were placed as collateral in relation to certain equity-linked transactions entered into by the Group in 2002.

As at December 31, 2004, the Group's interest in REACH was also used to secure the Telstra Note. The charge was released upon the full redemption of the Telstra Note on June 30, 2005.

In connection with the undertakings relating to the capital reduction approved by the High Court of Hong Kong on August 3, 2004, the bank guarantee issued in favor of the Company was secured by a bank deposit placed by another indirect wholly-owned subsidiary of the Company amounting to approximately HK$259 million as at December 31, 2005 (2004: Nil), which was included in "Restricted cash" in the consolidated balance sheet.

CONTINGENT LIABILITIES

As at December 31, HK$ million	2005	2004
Performance guarantee	403	129
Others	34	119
	437	248

On April 23, 2002, a writ of summons was issued against PCCW-HKT Limited ("HKT"), an indirect wholly-owned subsidiary of the Company, by New Century Infocomm Tech Co., Ltd. for HKT's failure to purchase 6,522,000 shares of Taiwan Telecommunication Network Services Co., Ltd. ("TTNS"), an indirect subsidiary of the Company, pursuant to an option agreement entered into on July 24, 2000. The total claim against HKT amounted to approximately HK$99 million (NT$418 million), being the purchase price of shares in TTNS, contractual interest for the period from January 1, 2001 to January 2, 2002 at 6.725% per annum and interest on the due amount pursuant to Sections 48 and 49 of the High Court Ordinance, Chapter 4 of the Laws of Hong Kong. However, this figure should be reduced by the current market value of the shares in TTNS which would be transferred to HKT in the event that the claimants are successful in their claim. A defense was filed by HKT on May 29, 2002 and proceedings are ongoing. Based on legal advice received, the Directors consider that HKT has valid defenses and therefore no provision has been made.

HKTC is in dispute with Hong Kong's Inland Revenue Department (the "IRD") regarding the deductibility of certain finance expenses. The IRD had raised two assessments for part of the disputed finance expenses on April 21, 2005 and February 3, 2006. HKTC had lodged an objection to both assessments and successfully obtained a holdover of the tax assessed through the purchase of Tax Reserve Certificates in the amount of HK$308 million. The estimated tax impact of the dispute may amount to HK$322 million up to December 31, 2005. Based on the information available to the Group to date, HKTC has made a provision based on the best estimate of the amount that may ultimately be required to settle the dispute. The directors consider that the impact of any unprovided amounts which may materialize is immaterial.

The Group is subject to certain corporate guarantee obligations to guarantee performance of its wholly-owned subsidiaries in the normal course of their businesses. The amount of liabilities arising from such obligations, if any, cannot be ascertained but the directors are of the opinion that any resulting liability would not materially affect the financial position of the Group.

HUMAN RESOURCES

As at December 31, 2005, the Group had approximately 14,108 employees (2004: 12,248), including employees of SUNDAY. The majority of these employees work in Hong Kong. The Company has established incentive bonus schemes designed to motivate and reward employees at all levels to achieve the Company's business performance targets. Payment of bonuses is generally based on achievement of net profit after tax target for the Group as a whole and revenue and EBITDA[2] targets for the Company's individual businesses. The Company also operates a discretionary employee share option scheme and two share award schemes to motivate employee performance in enhancing shareholder value.

FINAL DIVIDEND

The Board has recommended the payment of a final dividend of 12 (2004: 9.6) HK cents per share for the year ended December 31, 2005 subject to the approval of shareholders of the Company at the forthcoming annual general meeting. An interim dividend of 6.5 (2004: 5.5) HK cents per share was paid by the Company on October 4, 2005.