

NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

For the six months ended June 30, 2006

1. BASIS OF PREPARATION AND ACCOUNTING POLICIES

The unaudited condensed consolidated financial statements have been prepared in accordance with Hong Kong Accounting Standard (“HKAS”) 34 ‘Interim Financial Reporting’ issued by the HKICPA. These unaudited condensed consolidated financial statements should be read in conjunction with the Group’s consolidated financial statements as at and for the year ended December 31, 2005.

The preparation of the unaudited condensed consolidated financial statements in conformity with HKAS 34 requires management to make judgments, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses on a year to date basis. Actual results may differ from these estimates.

The accounting policies and methods of computation used in the preparation of the interim financial statements are consistent with those used in the annual consolidated financial statements for 2005 except for the adoption of the Hong Kong Financial Reporting Standards, HKASs and interpretations (“new HKFRSs”) which were relevant to the Group and were effective for annual periods commencing on or after January 1, 2006. The adoption of these new HKFRSs has no material impact to the Group’s financial statements for the current or prior periods.

2. TURNOVER AND SEGMENT INFORMATION

An analysis of turnover and contribution to the Group's results and capital expenditure by business segment for the six months ended June 30, is set out below:

HK\$ million	Property development		Property investment		Other businesses		Eliminations		Consolidated	
	2006	2005	2006	2005	2006	2005	2006	2005	2006	2005
TURNOVER										
External revenue	5,125	3,179	111	121	40	38	—	—	5,276	3,338
Inter-segment revenue	—	—	—	—	18	19	(18)	(19)	—	—
Total revenue	5,125	3,179	111	121	58	57	(18)	(19)	5,276	3,338
RESULT										
Segment results	655	236	71	85	6	4	—	—	732	325
Unallocated corporate expenses									(31)	(12)
Interest income									198	72
Finance costs									(61)	(66)
Impairment of investment in unconsolidated subsidiaries held for sale									—	(6)
Profit before taxation									838	313
Taxation									(135)	(50)
Profit attributable to equity holders of the Company									703	263
Capital expenditure	9	—	3	4	1	1	—	—	13	5

3. PROFIT BEFORE TAXATION

Profit before taxation is stated after crediting and charging the following:

HK\$ million	Six months ended June 30,	
	2006	2005
Crediting:		
Gross rental income	111	121
Less: outgoings	(7)	(15)
Gain on disposal of investment property	—	8
Charging:		
Cost of properties sold	4,383	2,848
Depreciation	6	5
Amortisation of leasehold land	1	—
Staff costs, included in:		
- Cost of sales	23	21
- General and administrative expenses	46	42
Contributions to defined contribution retirement scheme, included in:		
- Cost of sales	1	1
- General and administrative expenses	3	3
Value of services obtained from directors and employees under share option scheme	2	4

4. TAXATION

Hong Kong profits tax has been provided at the rate of 17.5 per cent on the estimated assessable profits.

Mainland China taxation has been calculated on the estimated assessable profits for the period at the rates prevailing in the respective jurisdiction.

HK\$ million	Six months ended June 30,	
	2006	2005
Current tax expenses		
- Hong Kong profits tax	115	52
- Mainland China income tax	—	1
Deferred taxation provision		
- Origination and reversal of temporary differences	20	(3)
Total	135	50

5. DIVIDEND

HK\$ million	Six months ended June 30,	
	2006	2005
Interim dividend declared of 1.5 Hong Kong cents per ordinary share (2005: 1.5 Hong Kong cents per ordinary share)	36	36

The interim dividend declared after the balance sheet date has not been recognised as a liability as at the balance sheet date.

Final dividend of HK\$132 million for 2005, which comprises 5.5 Hong Kong cents per ordinary share was paid by the Company on May 23, 2006.

6. EARNINGS PER SHARE

The calculations of basic and diluted earnings per share based on the share capital of the Company are as follows:

	Six months ended June 30,	
	2006	2005
Earnings (HK\$ million)		
Earnings for the purpose of calculating the basic earnings per share	703	263
Finance costs on convertible notes	61	54
Earnings for the purpose of calculating the diluted earnings per share	764	317
Number of shares		
Weighted average number of ordinary shares for the purpose of calculating the basic earnings per share	2,402,459,873	2,232,957,111
Effect of dilutive potential ordinary shares on conversion of convertible notes and the Company's employee share options	672,222,222	841,896,134
Weighted average number of ordinary shares for the purpose of calculating the diluted earnings per share	3,074,682,095	3,074,853,245

7. ACCOUNTS RECEIVABLE, NET

An aging analysis of accounts receivable is set out below:

HK\$ million	June 30, 2006	December 31, 2005
Current	256	172
One to three months	132	64
More than three months	67	3
	455	239

The normal credit period granted by the Group ranges up to 30 days from the date of the invoice unless there is separate mutual agreement on extension of the credit period.

8. ACCOUNTS PAYABLE

An aging analysis of accounts payable is set out below:

HK\$ million	June 30, 2006	December 31, 2005
Current	72	181
One to three months	7	5
More than three months	6	—
	85	186

9. LONG-TERM BORROWINGS

HK\$ million	Long-term borrowings	2006 Convertible notes reserve	Total
Balance at January 1, 2006	1,803	769	2,572
Finance costs charged to unaudited condensed consolidated income statement	61	—	61
Interest amount payable included in current liabilities	(12)	—	(12)
Balance at June 30, 2006	1,852	769	2,621
Less: Amount classified as current liabilities	(24)	—	(24)
	1,828	769	2,597
HK\$ million	Long-term borrowings	2005 Convertible notes reserve	Total
Balance at January 1, 2005	2,516	1,160	3,676
Finance costs charged to unaudited condensed consolidated income statement	66	—	66
Reduction in balances as a result of the Conversion (note (a))	(816)	(391)	(1,207)
Interest amount payable included in current liabilities	(12)	—	(12)
Balance at June 30, 2005	1,754	769	2,523
Less: Amount classified as current liabilities	(24)	—	(24)
	1,730	769	2,499

9. LONG-TERM BORROWINGS - CONTINUED

- a. Long-term borrowings comprise the outstanding principal amount of the convertible notes or any part that may, at the discretion of PCCW or its designated subsidiary, the holder of the notes, be converted into the ordinary shares of the Company, issued to PCCW (or as it may direct) at any time and from time to time on or after the date of issue (but on or prior to the maturity date) at the relevant conversion price.

On February 24, 2005, PCCW elected to convert the tranche A note due 2011 with a principal amount of HK\$1,170 million into new shares of HK\$0.10 each at HK\$2.25 per share pursuant to the terms of the tranche A note (the "Conversion"). The Company issued 520,000,000 ordinary shares to a wholly-owned subsidiary of PCCW as a result of the Conversion and increased its issued equity by HK\$52 million. Prior to the Conversion, PCCW held approximately 51.07 per cent of the issued shares of the Company. Immediately after the Conversion, PCCW held approximately 61.66 per cent of the enlarged issued share capital of the Company.

The tranche B note due 2014 with principal amount of HK\$2,420 million could be converted into new shares of HK\$0.10 each at a conversion price of HK\$3.60 per share, subject to adjustment. The tranche B note may be redeemed at 120 per cent of the outstanding principal amount if conversion does not occur.

Interest expense on the convertible notes is calculated using the effective interest method by applying the effective interest rate of 6.87 per cent to the liability component.

10. PROVISIONS

HK\$ million	2006		
	Payment to the Government (note a)	Others	Total
Balance at January 1, 2006	6,705	29	6,734
Additional provisions included in properties under development	90	—	90
Additional provisions made	—	15	15
Provisions settled	(1,162)	(17)	(1,179)
Balance at June 30, 2006	5,633	27	5,660
Less: Amount classified as current liabilities	(4,910)	(27)	(4,937)
	723	—	723
HK\$ million	2005		
	Payment to the Government (note a)	Others	Total
Balance at January 1, 2005	6,380	31	6,411
Additional provisions included in properties under development	1,639	—	1,639
Additional provisions made	—	3	3
Provisions settled	(906)	—	(906)
Balance at June 30, 2005	7,113	34	7,147
Less: Amount classified as current liabilities	(4,608)	(34)	(4,642)
	2,505	—	2,505

10. PROVISIONS - CONTINUED

- a. Pursuant to the Cyberport Project Agreement, the Government of the Hong Kong Special Administration Region (“HKSAR”) shall be entitled to receive payments of approximately 65 per cent from the surplus cashflow arising from the sales of the residential portion of the Cyberport project, net of certain allowable costs incurred on the project, as stipulated under certain terms and conditions of the Cyberport Project Agreement. Provision for payment to the Government of the HKSAR is included in properties under development as the amount is considered as a part of the development costs for the Cyberport project. The provision is based on estimated sales proceeds of the residential portion of the project and the estimated development costs of the Cyberport project. The estimated amount to be paid to the Government of the HKSAR during the forthcoming year is classified as current liabilities.

11. ISSUED EQUITY

	The Group	
	Number of shares (note a)	Issued equity HK\$ million (note a)
Ordinary shares of HK\$0.10 each at January 1, 2006	2,402,459,873	4,631
Less: Share premium reduction (note b)	—	(322)
Ordinary shares of HK\$0.10 each at June 30, 2006	2,402,459,873	4,309

- a. Due to the use of reverse acquisition basis of accounting (as stated in note 2(d) to the 2004 Financial Statements), the amount of issued equity, which includes share capital and share premium in the consolidated balance sheet, represents the amount of issued equity of the legal subsidiary, Ipswich Holdings Limited, at date of completion of the reverse acquisition plus equity changes attributable to the Group after the reverse acquisition. The equity structure (i.e. the number and type of shares) reflects the equity structure of the legal parent, Pacific Century Premium Developments Limited for all accounting periods presented.
- b. On May 16, 2006, a special resolution was passed at the Company’s Annual General Meeting approving the reduction of share premium by cancelling a sum of approximately HK\$322 million standing to the credit of the Company’s share premium account against the accumulated losses of the Company of same amount.

11. ISSUED EQUITY - CONTINUED

c. Details of the share capital of the Company are as follows:

	The Company	
	Number of shares	Nominal value HK\$ million
Authorised:		
Ordinary shares of HK\$0.10 each at June 30, 2006 and December 31, 2005	10,000,000,000	1,000
Issued and fully paid:		
Ordinary shares of HK\$0.10 each at June 30, 2006 and December 31, 2005	2,402,459,873	240

12. CAPITAL COMMITMENTS

HK\$ million	June 30, 2006	December 31, 2005
Authorised and contracted for	1,820	2,120
Authorised but not contracted for	708	772
	2,528	2,892

13. CONTINGENT LIABILITIES

HK\$ million	June 30, 2006	December 31, 2005
Performance guarantee	1	1

On December 21, 2004, Partner Link Investments Limited (“Partner Link”), an indirect wholly-owned subsidiary of the Company, entered into a formal sales and purchase agreement (the “Property Sales and Purchase Agreement”) with Richly Leader Limited (the “Purchaser”) for the disposal of the property known as PCCW Tower (the “Property”) for a consideration of HK\$2,808 million in cash. The consideration was arrived at after arm’s length negotiations. The Property Sales and Purchase Agreement was completed on February 7, 2005 and the Group has recorded a gain on disposal of HK\$8 million for 2005.

Under the Property Sales and Purchase Agreement, on completion of the disposal of the Property, there is a rental guarantee pursuant to which Partner Link will undertake to the Purchaser that it will pay a guaranteed net monthly rental of approximately HK\$13.3 million to the Purchaser for a period of 5 years commencing from the date following completion of the disposal of the Property. The Property Sales and Purchase Agreement was completed on February 7, 2005. The rental guarantee was accounted for as a financial liability at fair value and movements in fair values are reflected in the income statement. As at June 30, 2006, the Group has remaining provision of approximately HK\$23 million (December 31, 2005: HK\$41 million) in relation to the rental guarantee over the remaining guarantee period included in ‘Accruals, other payables and deferred income’ on the balance sheet.

14. BANKING FACILITY

An indirect wholly-owned subsidiary of the Company had been granted a banking facility amounting to approximately HK\$20 million from a bank for the purpose of providing guarantee to the Government of the HKSAR. Such facility was secured by a bank deposit placed by the subsidiary from time to time to secure the amount of guarantee issued by the bank. Aggregate banking facility as at June 30, 2006 was HK\$20 million (December 31, 2005: HK\$20 million) of which HK\$20 million (December 31, 2005: HK\$20 million) was unused.

15. MATERIAL RELATED PARTY TRANSACTIONS

The Group is controlled by PCCW, a company incorporated in Hong Kong, which owns 61.66 per cent of the Company's shares. The remaining 38.34 per cent of the shares are widely held. PCCW is also regarded as the ultimate holding company of the Group.

The following transactions were carried out with related parties:

- a. During the period, the Group had the following significant transactions with related companies

HK\$ million	Six months ended June 30,	
	2006	2005
Sales of services:		
Fellow subsidiaries		
- Facility management services	21	24
- Office leases rental	5	12
Other related companies		
- Facility management services	11	11
Purchases of services:		
Fellow subsidiaries		
- Corporate services	3	2
- Office sub-licences	4	5
- Information technology and other logistic services	3	26

The above transactions were carried out after negotiations between the Group and the related parties in the ordinary course of business and on the basis of estimated market value as determined by the directors. In respect of transactions for which the price or volume has not yet been agreed with the relevant related parties, the directors have determined the relevant amounts based on their best estimation.

The related party transactions in respect of items above also constitute connected party transactions or continuing connected party transactions as defined in Chapter 14A of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited.

15. MATERIAL RELATED PARTY TRANSACTIONS - CONTINUED

b. Details of key management compensation of the Group

HK\$ million	Six months ended June 30,	
	2006	2005 (note 16)
Salaries and other short-term employee benefits	9	9
Bonuses	7	12
Directors' fee	—	—
Post-employment benefits	1	1
Share-based compensation accounting adjustment (note i)	17	22
	1	2
	18	24

- (i) Share-based compensation accounting adjustment involves calculation of the fair value of share options granted to certain directors under PCCW's share option scheme using trinomial option pricing model. The figures shown in the above table do not represent realisable gains which are affected by a combination of a number of factors, including, performance of PCCW's share price, vesting period, timing of exercise, etc.
- (ii) For executive directors employed by PCCW Limited, the ultimate holding company of the Group, their remunerations are borne by PCCW.

15. MATERIAL RELATED PARTY TRANSACTIONS – CONTINUED

c. Period-end balances arising from sales/purchases of property, plant and equipment/services and loan interest

HK\$ million	June 30, 2006	December 31, 2005
Receivables from related parties:		
- Fellow subsidiaries	1	10
- Other related companies	2	2
	3	12
Payables to related parties:		
- Ultimate holding company	—	—
- Fellow subsidiaries	17	24
	17	24

d. Loans from/amount due to related parties

The balance due to ultimate holding company as at June 30, 2006 of HK\$2,542 million (December 31, 2005: HK\$3,180 million) is interest free and recorded under the current liabilities in the unaudited condensed consolidated balance sheet.

HK\$ million	Six months ended June 30,	
	2006	2005
Loans from / amount due to ultimate holding company:		
Beginning of period	3,180	7,528
Conversion of convertible note	—	(1,170)
Repayment of loans	(638)	(497)
Interest expenses	—	12
Interest amount payable included in current liabilities	—	(12)
Provision for redemption premium	—	24
End of period	2,542	5,885

15. MATERIAL RELATED PARTY TRANSACTIONS – CONTINUED

d. Loans from/amount due to related parties - Continued

The balance due to a fellow subsidiary as at June 30, 2006 represents the aggregated amount of the face value of the convertible note (tranche B note due 2014) with face value of HK\$2,420 million together with the provision for redemption premium of HK\$103 million as at June 30, 2006 (December 31, 2005: HK\$79 million). Such convertible note was assigned, as directed by PCCW, from PCCW to a wholly-owned subsidiary of PCCW during 2005.

HK\$ million	Six months ended June 30,	
	2006	2005
Loan from a fellow subsidiary:		
Beginning of period	2,499	—
Interest expenses	12	—
Interest amount payable included in current liabilities	(12)	—
Provision for redemption premium	24	—
End of period	2,523	—

16. COMPARATIVE FIGURES

Certain comparative figures have been reclassified to conform to current period presentation.