MANAGEMENT'S DISCUSSION AND ANALYSIS

- Consolidated revenue increased 14% to HK$25,637 million
- Consolidated EBITDA increased 3% to HK$6,827 million
- Profit attributable to equity holders of the Company amounted to HK$1,252 million
- Basic earnings per share of 18.59 HK cents
- Final dividend of 12 HK cents per share
- Significant growth of now TV — installed base reached 758,000
- Further strengthened quadruple-play platforms to launch more applications

MANAGEMENT REVIEW

PCCW maintained its leading position in technology and innovation in 2006 by strengthening its quadruple-play platforms in preparation for the launch of various applications in the year ahead.

Consolidated revenue for the year ended December 31, 2006 increased 14% to HK$25,637 million, primarily driven by the higher Bel-Air sales recognized, and the consolidation of a full year of the Group's mobile business results. Telecommunications Services ("TSS") recorded a 2% revenue growth while TV & Content's contribution to the Group became increasingly significant.

Consolidated EBITDA for the year ended December 31, 2006 increased 3% to HK$6,827 million, although profit attributable to equity holders of the Company decreased to HK$1,252 million mainly due to lower net investment and other gains booked in 2006. The Board of Directors (the "Board") has recommended the payment of a final dividend of 12 HK cents per share for the year ended December 31, 2006.

FINANCIAL REVIEW BY SEGMENTS

For the year ended December 31, HK$ million	2006 H1	2006 H2	2006 Full Year	2005 (Restated)[1] H1	2005 (Restated)[1] H2	2005 (Restated)[1] Full Year	Better/ (Worse) y-o-y
Revenue							
TSS	7,405	7,969	15,374	7,389	7,659	15,048	2%
TV & Content	303	436	739	182	249	431	71%
Mobile	585	651	1,236	–	598	598	107%
PCCW Solutions	737	915	1,652	806	773	1,579	5%
Other Businesses	364	227	591	395	216	611	(3)%
Elimination	(546)	(672)	(1,218)	(409)	(486)	(895)	(36)%
Total Revenue (excluding Pacific Century Premium Developments Limited ("PCPD"))	8,848	9,526	18,374	8,363	9,009	17,372	6%
PCPD	5,276	1,987	7,263	3,338	1,789	5,127	42%
Consolidated Revenue	14,124	11,513	25,637	11,701	10,798	22,499	14%
Cost of sales	(7,555)	(5,131)	(12,686)	(5,893)	(4,574)	(10,467)	(21)%
Operating costs before depreciation, amortization and restructuring costs	(2,917)	(3,207)	(6,124)	(2,571)	(2,811)	(5,382)	(14)%
EBITDA[2]							
TSS	3,414	3,589	7,003	3,425	3,568	6,993	0%
TV & Content	(186)	(150)	(336)	(114)	(164)	(278)	(21)%
Mobile	(70)	(116)	(186)	–	25	25	N/A
PCCW Solutions	83	68	151	2	45	47	221%
Other Businesses	(297)	(464)	(761)	(386)	(428)	(814)	7%
Total EBITDA (excluding PCPD)	2,944	2,927	5,871	2,927	3,046	5,973	(2)%
PCPD	708	248	956	310	367	677	41%
Consolidated EBITDA[2]	3,652	3,175	6,827	3,237	3,413	6,650	3%
Consolidated EBITDA Margin[2, 4]	*26%*	*28%*	*27%*	*28%*	*32%*	*30%*	*(3)%*
Depreciation and amortization	(1,467)	(1,569)	(3,036)	(1,296)	(1,398)	(2,694)	(13)%
(Loss)/Gain on disposal of property, plant and equipment, investment properties and interests in leasehold land	(2)	(23)	(25)	33	(9)	24	N/A
Restructuring costs	–	(6)	(6)	–	–	–	N/A
Other gains, net	98	(56)	42	545	81	626	(93)%
Losses on property, plant and equipment	–	(11)	(11)	–	(52)	(52)	79%
Segment results[3]							
TSS	2,401	2,549	4,950	2,362	2,520	4,882	1%
TV & Content	(235)	(215)	(450)	(143)	(200)	(343)	(31)%
Mobile	(292)	(409)	(701)	–	(126)	(126)	(456)%
PCCW Solutions	62	46	108	(36)	1	(35)	N/A
Other Businesses	(356)	(672)	(1,028)	26	(454)	(428)	(140)%
Total segment results (excluding PCPD)	1,580	1,299	2,879	2,209	1,741	3,950	(27)%
PCPD	701	211	912	310	294	604	51%
Consolidated segment results[3]	2,281	1,510	3,791	2,519	2,035	4,554	(17)%

Note 1 Certain comparative figures have been restated to conform with the business segment presentation in the current year:

- *TV & Content and Mobile were previously included in TSS but are now presented as separate business segments.*
- *The Group's retail business broadband and directories businesses, both previously included in Business eSolutions, have been reclassified to TSS and Other Businesses respectively. Business eSolutions has also been renamed as PCCW Solutions. Certain Information and Communications Technologies ("ICT") business in mainland China has been restructured during the year.*
- *PCPD is principally the former Infrastructure segment with certain external rental income earned from the Group's telephone exchange buildings reclassified to Other 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, net other gains/losses, losses on property, plant and equipment, 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 Hong Kong Financial Reporting Standards 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 Segment results represent earnings before interest income, finance costs, income tax, impairment losses on interests in jointly controlled companies and associates and the Group's share of results of jointly controlled companies and associates. Consolidated segment results represent the sum of segment results and unallocated corporate expenses set out in note 6 of the financial statements.

Note 4 Year-on-year percentage change was based on absolute percentage change.

Note 5 As of period end, with exception of International Direct Dial ("IDD") minutes, which is total for period.

Note 6 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 and certain restricted cash.

Note 7 Group capital expenditure includes additions to property, plant and equipment, investment properties and interests in leasehold land held for own use. Interests in leasehold land held for development of HK$495 million (2005: Nil) are excluded.

Note 8 SUNDAY Group means SUNDAY Communications Limited (in voluntary liquidation) ("SUNDAY") and its then subsidiaries. The listing of SUNDAY's shares on The Stock Exchange of Hong Kong Limited and its American Depositary Shares on the NASDAQ Global Market was withdrawn on December 20, 2006 and December 21, 2006 respectively. Subsequently, the voluntary liquidation of SUNDAY commenced on December 29, 2006.

	2006		2005		Better/ (Worse)
OPERATING DRIVERS[5]	**H1**	**H2**	H1	H2	y-o-y
Exchange lines in service ('000)	**2,579**	**2,587**	2,514	2,564	1%
Business lines ('000)	**1,176**	**1,180**	1,127	1,164	1%
Residential lines ('000)	**1,403**	**1,407**	1,387	1,400	1%
Fixed line market share[4]					
Business lines	**70%**	**69%**	68%	69%	0%
Residential lines	**66%**	**66%**	65%	66%	0%
Total broadband access lines ('000)	**998**	**1,117**	857	953	17%
(Consumer, business and wholesale customers)					
Retail consumer broadband subscribers ('000)	**840**	**952**	715	798	19%
Retail business broadband subscribers ('000)	**94**	**99**	80	88	13%
Consumer narrowband subscribers ('000)	**132**	**122**	139	132	(8)%
Traditional data (Exit Gbps)	**351**	**485**	262	294	65%
Retail IDD minutes ('M mins)	**819**	**906**	741	786	13%
International Private Leased Circuit ("IPLC") bandwidth (Exit Mbps)	**15,489**	**22,994**	6,503	10,175	126%
Mobile subscribers ('000)	**781**	**921**	702	738	25%
Post-paid ('000)	**491**	**571**	443	456	25%
Prepaid ('000)	**290**	**350**	259	282	24%
now TV installed ('000)	**608**	**758**	441	549	38%

TSS

The table below sets out the financial performance of TSS for the years ended December 31, 2006 and December 31, 2005:

For the year ended December 31, HK$ million	2006 H1	2006 H2	2006 Full Year	2005 (Restated)[1] H1	2005 (Restated)[1] H2	2005 (Restated)[1] Full Year	Better/ (Worse) y-o-y
Local Telephony Services	**2,352**	**2,336**	**4,688**	2,462	2,400	4,862	(4)%
Local Data Services	**2,092**	**2,159**	**4,251**	2,101	2,079	4,180	2%
International Telecommunications Services	**1,060**	**1,097**	**2,157**	1,167	1,166	2,333	(8)%
Other Services	**1,901**	**2,377**	**4,278**	1,659	2,014	3,673	16%
TSS Revenue	**7,405**	**7,969**	**15,374**	7,389	7,659	15,048	2%
Cost of sales	**(2,065)**	**(2,219)**	**(4,284)**	(2,025)	(2,307)	(4,332)	1%
Operating costs before depreciation and amortization	**(1,926)**	**(2,161)**	**(4,087)**	(1,939)	(1,784)	(3,723)	(10)%
TSS EBITDA[2]	**3,414**	**3,589**	**7,003**	3,425	3,568	6,993	0%
TSS EBITDA Margin[2, 4]	**46%**	**45%**	**46%**	46%	47%	46%	0%

TSS continued to deliver stable financial results in a steadily improving business environment. Revenue, EBITDA and segment results for the year ended December 31, 2006 remained fairly stable at HK$15,374 million, HK$7,003 million and HK$4,950 million respectively.

Local Telephony Services. Local telephony services revenue for the year ended December 31, 2006 decreased by 4% to HK$4,688 million primarily due to the general downward pricing pressure in a highly saturated local fixed-line market and lower revenue from leasing of "last mile" local access lines by other fixed-line network operators. Nevertheless, the competitive environment appeared to become more benign and ARPU remained relatively stable in the second half of the year. With the Group's effective customer retention and win-back campaigns, PCCW strategically managed net fixed-line gain and maintained a stable market share of approximately 66% for residential lines and 69% for business lines.

In 2006, the number of direct exchange lines operated by the Group increased by nearly 1% to 2,587,000. This was in line with the modest growth in the Hong Kong fixed-line market, according to the industry statistics provided by the Office of the Telecommunications Authority, as a result of the continuing recovery of the local economy.

Local Data Services. Local data services revenue for the year ended December 31, 2006 increased by 2% to HK$4,251 million, reflecting improvements in both local data and broadband network revenue. During the year, PCCW successfully secured more data business benefiting from the improved market conditions. Driven by the momentum of now TV's growth and the high-quality value-added services including now.com.hk and MOOV, NETVIGATOR continued to maintain its market leadership in broadband access, with total broadband access lines, including wholesale customers, growing 17% year-on-year to 1,117,000 at the end of 2006. Pricing for broadband Internet access products and services stabilized during the course of the year.

International Telecommunications Services. International telecommunications services revenue for the year ended December 31, 2006 decreased by 8% to HK$2,157 million. The revenue decline was concentrated in the year's first half. Revenue rebounded in the second half of 2006 as further downward pricing pressure was more than offset by strong growth in volume. IPLC bandwidth rose 126% to 22,994 Mbps at the end of 2006, and retail IDD minutes grew 13% year-on-year to 1,725 million minutes. Unit prices of IDD, IPLC and other international data products were lower than those in 2005, in line with the global market trend.

Other Services. Other services revenue primarily includes revenue from the sale of network equipment and customer premise equipment ("CPE"), provision of technical and maintenance services including contracts secured by CASCADE, certain IP-based international connectivity products and services and teleservices business. Other services revenue for the year ended December 31, 2006 reported a significant increase of 16% to HK$4,278 million, primarily due to the increase in revenue from technical and maintenance services, sale of network equipment and CPE, and teleservices business.

CASCADE continued to build its external business during 2006 and was awarded significant network operation outsourcing and consultancy projects from various telecommunications operators in Southeast Asia and elsewhere. Revenue from the Group's teleservices business also achieved encouraging growth during the year with the increasing demand for contact center outsourcing services from multinational corporations.

TV & Content

Revenue from TV & Content surged by 71% to HK$739 million for the year ended December 31, 2006, driven by the strong growth of the now TV business. By the end of December 2006, now TV installed base reached 758,000 with 501,000 paying an ARPU for content and interactive services of HK$140 per month, an increase of 23% from HK$114 at the end of 2005.

now TV further strengthened its market position as the most comprehensive pay-TV platform in Hong Kong by adding more than 30 channels bringing its total offering to more than 120 channels by the end of 2006. In November 2006, the Group won exclusive rights to the live broadcast of EPL matches in Hong Kong for three seasons beginning 2007/08. These exclusive live broadcasting rights apply not only to now TV, but also extend to the mobile, broadband and fixed-line platforms. Furthermore, in December 2006, now TV also won the exclusive right to broadcast the prestigious UEFA Euro 2008™ in Hong Kong.

Content introduced by now TV during the year included the self-produced now Business News Channel ("now BNC"), an expanded suite of HBO channels, National Geographic Wild, TV5MONDE Asie, Jia Yue Channel, CNN International, AXN, A1, 5X Channel, the TVB PAY VISION pack and the UEFA Champions League matches. Interactive features already in service include now shop, now Ticketing, now Game channel and Stock Market Express.

now.com.hk, the Group's Internet portal, continued to bring high-quality value-added services exclusively to PCCW's broadband customers. MOOV, the largest online digital music service with over 60,000 songs and music videos and the first-in-Hong Kong monthly subscription model with unlimited streaming, was launched during the year. The MOOV service helped to increase the number of now.com.hk subscribers by 9% to 229,000 at the end of 2006.

Mobile

PCCW completed the acquisition of all the operating businesses and assets of SUNDAY Group[8] in December 2006. The full integration of the mobile business into the Group beginning in 2007 is expected to improve operational efficiency and bring the integration of the fixed and mobile businesses forward to the next stage.

Revenue from the Group's mobile operations was HK$1,236 million for the year ended December 31, 2006. During the year, the Group further enhanced its mobile network quality and coverage with more cell sites added. Backed by the Group's large customer base for other services and extensive distribution channels, market share rose and the total mobile subscriber base increased 25% to 921,000 by the end of 2006. PCCW mobile began migrating its 3G trial users to monthly service plans in August 2006. Initial ARPU for 3G was encouraging, although pricing of 2G services remained under pressure in a highly competitive environment.

PCCW mobile introduced the world's first real-time mobile TV service using Cell Multimedia Broadcast technology in May 2006. Currently 13 channels are offered including now BNC, 24-hour ATV News Channel, CNN International, CNBC, Mobile ESPN and TVB news and entertainment, etc. Later in the year, PCCW mobile also introduced other innovative services including PCCW EasyWatch Service, a multi-functional mobile camera remote monitoring service, "MOOV on mobile", the largest online digital music library in Hong Kong made available on handsets and MobileTix, allowing customers to buy movie tickets electronically on mobile.

PCCW Solutions

PCCW Solutions revenue for the year ended December 31, 2006 increased 5% to HK$1,652 million. PCCW Solutions continued to expand its external business as it focused on providing outsourcing services during 2006 and was awarded significant contracts. The Group's ICT business in mainland China underwent restructuring during the year to improve efficiency. Recent significant projects awarded include the implementation of an Enterprise Application Integration platform based on service-oriented architecture for the Dah Sing Banking Group, and a project to meet the IT needs of a joint venture in Wuhan involving Nokia and China Putian.

Other major contracts awarded include high-profile public sector contracts such as the 10-year Electronic Passport System (e-PASS) contract and the Government Financial Management Information System (GFMIS) contract, both with the Government of Hong Kong. In the private sector, a contract with Bossini International Holdings Limited was also signed to provide comprehensive implementation services and manage its new Oracle Financial system rollout in the region.

PCPD

PCPD revenue for the year ended December 31, 2006 increased 42% to HK$7,263 million, reflecting the higher sales of Bel-Air units recognized.

The Bel-Air project continued to be the leading driver of success for PCPD, on the back of the strong economy and positive sentiment in the property market in Hong Kong. Co-operation between PCCW and PCPD to redevelop a number of telephone exchange buildings in Hong Kong has continued to make good progress during the year. In mainland China, development work on the prestigious residential project at Pacific Century Place in Chaoyang District, Beijing with an approved gross floor area of approximately 46,300 square metres, will commence in 2007.

For more information about the performance of PCPD, please refer to its 2006 annual results released on March 28, 2007.

Other Businesses

Other Businesses primarily include the Group's directories businesses in Hong Kong and mainland China, its telecommunications business in Taiwan, its wireless broadband business in the United Kingdom, and all corporate support functions. Other Businesses revenue decreased 3% to HK$591 million largely due to the Group's disposal of its entire interest in JALECO Ltd. ("JALECO") in the second half of 2005.

Elimination

Elimination of HK$1,218 million predominantly relates to internal charges for telecommunications services consumed, IT support and computer system network charges, customer support services and rental among the Group's business units. Elimination increased 36% in 2006 due primarily to the inclusion of a full year of consolidated results of the mobile business.

COSTS

Total cost of sales for the year ended December 31, 2006 increased 21% to HK$12,686 million primarily reflecting higher cost of sales of the Cyberport project recognized in relation to the increased Bel-Air revenue. A full year's cost of sales was recognized for the Group's mobile business versus half a year in 2005. Excluding the Group's property and mobile businesses, total cost of sales remained fairly stable on a year-on-year basis. A higher cost of sales for TV & Content corresponding to the strong business growth was partially offset by the lower cost of sales for TSS and Other Businesses.

For the year ended December 31, HK$ million	2006	2005	Better/ (Worse) y-o-y
Staff costs	**2,989**	2,677	(12)%
Rent, rates and utilities	**876**	802	(9)%
Other operating costs	**2,259**	1,903	(19)%
Total operating costs before depreciation, amortization and restructuring costs	**6,124**	5,382	(14)%
Depreciation and amortization	**3,036**	2,694	(13)%
Loss/(Gain) on disposal of property, plant and equipment, investment properties and interests in leasehold land	**25**	(24)	N/A
Restructuring costs	**6**	–	N/A
General and administrative expenses	**9,191**	8,052	(14)%

General and administrative expenses for the year increased 14%. Total operating costs increased 14% and depreciation and amortization increased 13% primarily due to the consolidation of the Group's mobile operations beginning in the second half of 2005. Operating costs also increased due to higher costs for TV & Content corresponding to the strong business growth.

EBITDA[2]

Consolidated EBITDA for 2006 increased 3% to HK$6,827 million. EBITDA recognized from PCPD increased 41% to HK$956 million, but the Group's TV & Content and Mobile businesses recorded higher EBITDA losses at their respective early stages of the business life cycle. TSS EBITDA remained steady at HK$7,003 million while PCCW Solutions EBITDA increased substantially due to efficiency gains and upon completion of certain contracts.

The Group continued to exercise cautious cost control and reduced its corporate overhead during the year. As a result, Other Businesses EBITDA loss narrowed in 2006 by 7%.

Consolidated EBITDA margin narrowed to 27% in 2006 from 30% in 2005 while TSS EBITDA margin was maintained at 46%.

Other Gains, Net

Net other gains decreased to HK$42 million in 2006 from HK$626 million in 2005 due to lower net investment and other gains. The substantially larger 2005 net other gains included the gain on disposal of the Group's entire interest in JALECO and net realized and unrealized gains on cross currency swap contracts. The net gains for 2006 primarily included write back of provision for loss on legal claims and net realized gain on certain investments of the Group, offset by net realized and unrealized losses on cross currency swap contracts.

Segment Results[3]

Consolidated segment results decreased 17% from a year ago to HK$3,791 million. The decrease was primarily due to a higher depreciation and amortization charge in 2006, which reflected the impact of a full year of mobile operations, and a significant decrease in net other gains as discussed above, which offset the growth in consolidated EBITDA.

Interest Income and Finance Costs

Interest income increased 37% to HK$732 million in 2006 mainly due to the higher average interest income rate. Finance costs decreased 10% to HK$2,008 million after the US$1,100 million 3.5% guaranteed convertible bonds due 2005 were redeemed in December 2005. Average cost of debt for 2006 per annum was 6.5% and average maturity was approximately 5 years.

Share of Results of Associates

Share of results of associates decreased to HK$37 million for the year ended December 31, 2006 from HK$120 million in 2005 after the Group's disposal of its entire interest in MobileOne Ltd in October 2005.

Taxation

Taxation expenses, net of recovery of deferred tax mainly arising from recognition of tax losses, for the year ended December 31, 2006 decreased 17% to HK$920 million and the Group's effective tax rate for the year ended December 31, 2006 was 36% (2005: 37%). 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$380 million primarily represented the net profit attributable to the minority shareholders of PCPD.

Profit Attributable to Equity Holders of the Company

Profit attributable to equity holders of the Company for the year ended December 31, 2006 decreased to HK$1,252 million (2005: HK$1,595 million). This decrease was due to the lower net other gains and lower share of results of associates, partially offset by the increase in consolidated EBITDA and the reduction in net finance costs and taxation expenses.

LIQUIDITY AND CAPITAL RESOURCES

Net cash generated from operating activities for the year ended December 31, 2006 increased to HK$6,522 million (2005: HK$4,639 million) primarily due to increased receipts from the Bel-Air project and changes in restricted cash.

The Group's gross debt[6] totaled HK$28,977 million as at December 31, 2006 (2005: HK$29,165 million). Cash and cash equivalents decreased to HK$4,951 million (2005: HK$9,679 million). During 2006, HK$4,301 million was transferred into restricted cash to defease certain liabilities of the Group including principally the US$450 million 1% guaranteed convertible bonds due in January 2007. On January 29, 2007, the convertible bonds were redeemed in full. The Group also exercised a call option under the US$456 million 7.88% guaranteed notes due 2013 and redeemed the notes in full on January 24, 2007. The Group's net debt[6] was HK$19,725 million as at December 31, 2006 compared to HK$19,486 million as at December 31, 2005.

In July 2006, the Company strengthened its liquidity position by entering into a HK$6,450 million four-year revolving loan facility for general corporate purposes. In October 2006, PCCW-HKT Telephone Limited ("HKTC"), an indirect wholly-owned subsidiary of the Company, further entered into a HK$10,150 million six-year revolving loan facility. As at December 31, 2006, the Group had a total of HK$16,698 million in banking facilities available for liquidity and debt retirement, of which HK$10,387 million remained undrawn.

The Cyberport project continued to generate surplus proceeds from the sale of Bel-Air units. Net surplus proceeds distributed to the Group over the course of the Cyberport project totaled HK$3,632 million, including HK$1,985 million received in 2006.

The Group's gross debt[6] to total assets was 59% as at December 31, 2006.

Credit Ratings of HKTC

As of December 31, 2006, HKTC had investment grade ratings with Standard & Poor's Ratings Services (BBB/Stable), Moody's Investors Service (Baa2/Stable) and Fitch Ratings (BBB+/Negative).

CAPITAL EXPENDITURE[7]

Group capital expenditure for the year ended December 31, 2006 increased to HK$3,366 million (2005: HK$2,441 million, excluding the indefeasible rights to use the international undersea cable capacity and other related equipment acquired from Reach Ltd. of HK$1,627 million). The increase was due primarily to the inclusion of a full year of mobile capital expenditure. The majority of capital expenditure was spent on meeting the demand for new products and services, such as now TV, broadband network expansion, mobile network enhancement and new initiatives including the next generation fixed-line services.

PCCW has made significant investments in fixed-line and mobile network in previous years. This included the upgrade and expansion of network coverage, and building a platform for broadband and fast developing IP initiatives. 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 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. During 2006, certain cross currency swap contracts were designated as cash flow hedges for certain of the Group's foreign currency denominated long-term liabilities.

CHARGE ON ASSETS

As at December 31, 2006, certain assets of the Group with an aggregate carrying value of HK$119 million (2005: HK$62 million) were pledged to secure loan and borrowing facilities utilized by the Group.

As at December 31, 2005, certain financial assets at fair value through profit or loss, with an aggregate value of HK$178 million were placed as collateral in relation to certain equity-linked transactions entered into by the Group in 2002. In October 2006, all these equity-linked transactions were terminated and the underlying investments were sold.

CONTINGENT LIABILITIES

As at December 31, HK$ million	**2006**	2005
Performance guarantee	**611**	403
Others	**29**	34
	640	437

Apart from the above, as disclosed in the Group's annual financial statements for the year ended December 31, 2005, 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. ("NCIC") for HKT's alleged 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.

During the year, the Group decided to raise its stake in TTNS. The Group negotiated with NCIC to acquire 6,522,000 shares of TTNS and completed the acquisition in July 2006. Following the purchase, the Group's effective interest in TTNS was increased to 62.56% from 56.56%.

In July 2006, HKT and NCIC filed a consent summons with the High Court of Hong Kong permanently staying the court action as mentioned above which has effectively terminated these legal proceedings.

HKTC is in dispute with Hong Kong Government's Inland Revenue Department (the "IRD") regarding the deductibility of certain finance expenses. The IRD had raised assessments for part of the disputed finance expenses for the years of assessment 2000/01 to 2005/06 on April 21, 2005, February 3, 2006 and February 5, 2007. HKTC had lodged objections to the assessments and requested for holding over of the tax assessed through the purchase of Tax Reserve Certificates. 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 unprovided tax expense as at December 31, 2006 in respect of the subject dispute is approximately HK$192 million. 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, 2006, the Group had approximately 14,500 employees (2005: 14,108). About three quarters of these employees work in Hong Kong and the others are based outside of Hong Kong, mainly in mainland China. 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 EBITDA[2] and 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 to enhance shareholders' value.

FINAL DIVIDEND

The Board has recommended the payment of a final dividend of 12 HK cents (2005: 12 HK cents) per share for the year ended December 31, 2006 subject to the approval of shareholders of the Company at the forthcoming annual general meeting. An interim dividend of 6.5 HK cents (2005: 6.5 HK cents) per share for the six months ended June 30, 2006 was paid by the Company on October 11, 2006.