



MANAGEMENT DISCUSSION AND ANALYSIS

REVIEW OF OPERATIONS OVERVIEW

For the year ended 31 December 2006, the Group achieved a turnover of HK\$4,201 million (2005: HK\$4,177 million), which represented an increase of 1% over 2005. Cost of sales amounted to HK\$1,778 million (2005: HK\$1,792 million), which represented a decrease of 1% over 2005. Gross profit for the year amounted to HK\$2,423 million (2005: HK\$2,385 million), which represented a gross profit percentage of 58% (2005: 57%).

Included in cost of sales was the cost of programmes, film rights, movies and stocks which amounted to HK\$1,171 million (2005: HK\$1,148 million). This represented an increase of 2% over 2005.

Selling, distribution and transmission costs amounted to HK\$451 million, a similar level as for 2005 (2005: HK\$452 million). General and administrative expenses amounted to HK\$504 million (2005: HK\$491 million), which represented an increase of 3% reflecting a slightly higher staff cost over 2005.

Operating profit included interest income of HK\$58 million (2005: HK\$25 million), and a net exchange gain arising from the translation of inter-company balances denominated in foreign currencies of HK\$58 million (2005: net exchange loss of HK\$1 million).

The Group's share of losses of an associate, TVB Pay Vision Holdings Limited ("TVBPH", formerly known as Galaxy Satellite TV Holdings Limited), decreased from HK\$187 million to HK\$163 million for the year. The better performance of TVBPH was due to the result of an increase in subscription revenue from its larger subscriber base.

The Group's taxation charge amounted to HK\$247 million (2005: HK\$232 million), which represented an increase of 6% over 2005.

The profit attributable to equity holders amounted to HK\$1,189 million (2005: HK\$1,180 million, which included a one-off gain of HK\$149 million arising from the disposal of a 51% equity interest in TVBPH to third parties (the "Gain on Disposal"), which represented an increase of 1% over 2005. The earnings per share was HK\$2.71 (2005: HK\$2.69).

If the Gain on Disposal was excluded, the profit attributable to equity holders would have increased from HK\$1,031 million to HK\$1,189 million, and the earnings per share would have increased from HK\$2.35 to HK\$2.71, which represented an increase of 15% over 2005.



COMMENTS ON SEGMENT INFORMATION

Revenue from terrestrial television broadcasting which comprised predominantly local advertising revenue, decreased slightly from HK\$2,236 million to HK\$2,219 million. This represented a decrease of 1% over 2005.

The cost of programmes comprised the amortised cost of self-produced TV programmes and acquired film rights. The Group continued to provide high quality and customised programming, taking into account audience taste and market trends. Together with our effective cost control, the programme cost for this segment was lower than that in 2005. As a result, this segment contributed an operating profit of HK\$918 million (2005: HK\$859 million), an increase of 7% over 2005.

Revenue from programme licensing and distribution which comprised predominantly licensing income from distribution of our programmes through telecast, video (DVDs and VCDs), and the internet, increased from HK\$693 million to HK\$724 million. This represented an increase of 4% over 2005. The increase was mainly contributed by increase in the licensing revenue from Mainland China. As a result, programme licensing and distribution contributed an operating profit of HK\$441 million (2005: HK\$391 million), an increase of 13% over 2005.

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Revenue from overseas satellite pay TV operations which comprised revenue from TVB Satellite Platform (“TVBSP”) USA, TVB Australia (“TVBA”) and The Chinese Channel (“TCC”) Europe, showed a decrease from HK\$247 million to HK\$245 million. This represented a reduction of 1% over 2005. The segment contributed an operating profit of HK\$28 million (2005: HK\$29 million), a decrease of 3% over 2005.

Revenue from channel operations which comprised revenue from the Taiwanese channels TVBS, the two satellite channels, TVB8 and Xing He, and the supply of the eight channels to TVB Pay Vision Limited (“TVBPV”), showed an increase from HK\$998 million to HK\$1,024 million. This represented an increase of 3% over 2005. The segment contributed an operating profit of HK\$187 million (2005: HK\$194 million), a decrease of 4% over 2005.

BUSINESS REVIEW AND PROSPECTS

Terrestrial Television Broadcasting

(a) Advertising Revenue

Advertisers’ spending from key categories, such as property developers, slimming centres, cosmetics and skin care products, contributed less in the first half of 2006 when compared with the same period in 2005. These advertisers reduced their advertising spending substantially in all media in anticipation of a slowdown in sales and rising operating costs. As noted in our interim report, the drop in our Hong Kong advertising receipt for the first six months of 2006 came to 5% when compared with 2005.

However, we regained some of the above shortfall when the overall advertising market bounced back in the second half of 2006. As a result, advertising sales for the full year declined by a more moderate 1%.

We were able to achieve this result in the second half of 2006 partly through the resurgence of advertising activities from local property developers and partly through our increase in selling efforts targeted at product categories which showed substantial sales growth in recent years, for example: luxury brand watches, personal investment products, such as investment in shares and mutual funds. Moreover, our sales efforts in pushing product sponsorship (commonly known as product placement) to advertisers also contributed to our increased advertising sales in the second half of 2006. We achieved satisfactory revenue growth from product sponsorship in 2006. We are confident that the growth in product sponsorship revenue will continue in 2007 and beyond.

We are cautiously optimistic about our outlook on the 2007 advertising market. With the unemployment rate dropping to its lowest level since 2002 and the gradual rise in wages, we anticipate that the local economy and consumer spending will start to pick up in 2007, and consequently the advertising spending.

The advent of digital television broadcasting in Hong Kong in the last quarter of 2007 will herald a new era in television history. The excitement brought by this new technology is anticipated to boost advertisers’ interest in using more television advertising for communicating their sales messages to consumers.

The 2008 Beijing Olympics also provides us with an unprecedented golden opportunity to increase advertising income both in 2007 and 2008. As Hong Kong is designated by the Organising Committee of the Beijing Olympics to host the equestrian games, we will produce a number of Olympics-related programmes with different programme genres to tap the vast potential of the lucrative Olympic advertising market.

(b) *Jade* Terrestrial Channels Performance

Jade continued to be the favourite TV channel in Hong Kong. *Jade* achieved an overall weekday prime time¹ average audience share² of 85% (2005: 83%) among terrestrial Chinese channels and *Pearl*, a weekly prime time³ average of 75% (same in 2005) among terrestrial English channels during the year under review.

The *Jade* Channel

2006 was a particularly high achievement year for *Jade* in terms of innovation, as well as audience ratings in both drama and non-drama programmes.

The top programme and top special of the year in terms of ratings was *Jade*'s "*TV Awards Presentation 2006*", which garnered 36 TVRs⁴ (2.3 million viewers) and 90% audience share. The success of the "*TV Awards Presentation 2006*", spun-off from a segment of the previous TVB anniversary specials, again demonstrated TVB's forte in creating events and producing star-studded variety specials. The runners-up for variety specials which gained close to 90% audience share were "*TVB 39th Anniversary Gala*", 35 TVRs (2.2 million viewers) and the "*J.S.G. (Jade Solid Gold) Best 10 Awards Presentation 2005*", 32 TVRs (2.0 million viewers).

In the non-drama programmes, *Jade* created another wave of successful game and quiz shows. The combination of celebrities, comedy and game show elements again succeeded in creating instant hits. The top non-drama series of the year, "*Beautiful Cooking*" achieved an average 33 TVRs and 88% audience share on Sunday nights with its finale attaining 93% share; and a new game show "*15/16*", achieved an average rating of 29 TVRs and 89% audience share. The acquired-format "*Deal or No Deal*", in which



¹ *Jade*'s weekday prime time runs from 7-11 p.m.

² Audience share (%) is the percentage of ratings of a particular channel over the total ratings of the base channels for a specific period of time. When calculating audience share for free-to-air terrestrial TV channels in Hong Kong, the base would be the combined TV ratings (TVRs) of terrestrial Chinese channels or the combined TVRs of terrestrial English channels.

³ *Pearl*'s weekly prime time runs from 7 p.m. to midnight.

⁴ TV Rating (TVR) represents the size of audience expressed as a percentage of the total TV population. For 2006, the TV population is 6,426,000, and therefore, 1 TVR represents 64,260 viewers (1% of the TV population). Ratings data source: CSM Media Research.

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audience participants (and also celebrities in charity and anniversary specials) made deals with an anonymous banker in the hope to win the top prize of HK\$3 million, achieved an average rating of 25 TVRs and 87% audience share on Sunday nights.

Jade also developed a new docu-travelogue “*On The Road*” in which cultural exploration in far away places was interwoven with the personal experiences of celebrity hosts and reflections on the meaning of life. The series brought critical acclaim as well as good rating (on average 26 TVRs and 86% audience share during weekday late prime time). On a different road, veteran star Lydia Sham took the audience down the memory lane in “*Where Are They Now?*” and interviewed former Hong Kong TV and movie stars now residing abroad.

2006 was also a particularly fruitful year for *Jade* dramas. The channel had successfully engaged the audience on and offscreen. The top drama of the year “*La Femme Desperado*” (“*La Femme*”), weaving its story lines on controversial issues concerning city women, became an instant hit and talk of the town and achieved on average 33 TVRs and 88% audience share. Deemed as a follow-up of “*La Femme*” and based on the experiences of cosmopolitan men, “*Men In Pain*” also gained 88% in audience share with an average 32 TVRs. Venturing in new directions in terms of format and themes, *Jade* produced a cycle of four stories symbolising the life, love and perils of Chinese women through four generations in “*Maidens’ Vow*” gaining on average 32 TVRs and 90% audience share. Another variation on the theme of women’s plight and tenacity and set in the barren north-western highlands of Mainland China, “*The Dance Of Passion*” garnered 36 TVRs and 90% audience share for its debut episode, the highest first episode rating of dramas since 2002 (the series averaged 32 TVRs and 87% audience share). Among dramas with plots developed around crime and legal cases, “*Forensic Heroes*” became the second highest rated drama series with a top final episode rating reaching 41 TVRs, 95% share (overall series average, 33 TVRs, 87% share); and “*Bar Bender*” averaged 32 TVRs, 88% share. Family drama and comedy continued to yield strong audience support during the year with “*Under The Canopy of Love*” which achieved on average 31 TVRs and 88% audience share and set a new trend for romantic comedies.

TVB continued to produce dramas that carry educational and entertainment value. “*Love Guaranteed*” (averaged 32 TVRs and 88% share) built story lines on family and love, and was based on a background of an insurance business and in a contemporary setting. Set in a Chinese traditional guarded-courier business, the period drama “*Land Of Wealth*” told of a young man’s struggle to re-establish his family’s reputation against a background of the banking business in the late Qing Dynasty.

Jade’s acquired programmes also excelled in ratings and acclaim. “*Queen Of The Classroom*” not only broke the record to become the highest rated Japanese drama in Hong Kong’s TV history, with an average of 25 TVRs and 86% share, but also brought about a public discussion agenda on disciplinary measures in classrooms.

TVB continued to provide a balanced news coverage on local, Mainland China, Taiwan and international news. Apart from the regular public affairs flagship programmes “*News Magazine*” and “*Tuesday/Sunday Report*”, TVB News produced a series of special reports on H-share companies in “*Financial Magazine*”. With Hong Kong’s growing importance as a financial centre of the region, TVB began telecasting five live reports daily from its studio at the Hong Kong Stock Exchange on trading days.

In sports programmes, *Jade* presented live telecast of two semi-finals and the final of “*2006 FIFA World Cup*”. Of those home viewers who watched the three live matches, 80% were viewing on *Jade*.



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America's Next Top Model

The Pearl Channel

Pearl attained remarkable achievement in 2006. The top 100 programmes on the English terrestrial channels were programmes on Pearl. The Pic of the Year “*The Day After Tomorrow*” attracted an average of 819,000 viewers (top programme of the year with an average rating close to 13 TVRs, 90% audience share). Other blockbusters included “*Harry Potter and the Chamber of Secrets*”, the “*Terminator*” trilogy, “*X-Men*” and “*X2*” – attained over 9 TVRs and 90% audience share.



Prison Break

During the year, Pearl also further established its position as the premier provider of quality drama series available in the international market. The top drama of the year “*Prison Break*”, which was shown on Pearl on Tuesday nights, became the highest rated acquired-drama on the English terrestrial TV channels since the launch of the PeopleMeter for audience measurement in 1991, with an average of close to 5 TVRs (300,000 viewers) per episode. The channel has cultivated a steady following for dramas on weekday nights, Monday-Thursday, with favourites such as “*Lost*”, “*Nip/Tuck*”,

“*Supernatural*” and “*Without a Trace*”. Pearl also showcased a number of Asian drama series on prime time, including Japanese hit series “*Nyokei Kazoku*”, “*Crying Out Love in the Center of the World*”, “*Proof of the Man*” and “*Engine*”.

Reality programmes continued to excel on Pearl with the continuing series “*America’s Next Top Model*” securing close to 90% share (average 3.5 TVRs) with one of its episodes ranking number 33 on the top 100 list, making it the top non-movie/drama programme of the year. Other popular reality series included “*The Apprentice*” and “*Queer Eye for the Straight Guy*”.

Pearl has also revived its own station-produced weekly half-hour lifestyle show. “*Dolce Vita*” was launched in March 2006 and featured interviews with local and international celebrities, as well as showcasing luxury products and trends in elegant living.

Besides live telecast and coverage of major international sports events such as “*FIFA World Cup*” events, “*2006 Wimbledon Championships*”, “*Watson’s Water Champions Challenge 2006*” and the “*2006 FIVB World Grand Prix – Hong Kong*”, Pearl also started to feature weekly equestrian programmes as a prelude to the 2008 Olympic Games.

(c) Commendations and Awards

At the Asian Television Awards 2006, “*Leo & Miriam Special 2005*” was the Winner of Best Music Programme. “*Hong Kong Disneyland Grand Opening Special*” which was co-produced with Walt Disney Television International (Asia Pacific), also won the Best Entertainment (One-Off/Annual) Special.

At the 2007 New York Festivals, “*News Magazine – Land Grab*” won the Bronze World Medal in Best Public Affairs Programme; “*On The Road #16*” was a finalist for The Arts category; “*Miss Chinese International Pageant 2006*” won the Silver World Medal for Best Art Direction (Variety/Music); “*Be My Valentine – Make Love Fresh*” was a finalist for Station/Image Promotion; and “*Forensic Heroes*”, also a finalist in Director: Promotion Spot.

TVB’s on-air promotion also won a number of awards in other international festivals. At the 2006 PROMAX World Gold Awards, “*Be My Valentine – Make Love Fresh*” won the Gold Award in the category of Broadcast Television Station

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Consumer Promotion while “*Miss Chinese International Pageant 2006 Promotion*” also won the Gold Award in the category of Interstitial/Promotainment – General Programming. “*The 10th National Games*” won the Silver Award in the category of Sports Program Promotion.

At 2006 BDA World Gold Awards, “*Greed Mask*” won the Gold Award in the category of Total Package Design – Topical On-Air. “*The 10th National Games*” and “*J.S.G. Best 10 Awards Presentation 2004*” both won Silver Awards in the category of Art Direction & Design and in the category of Scenic – One Time Only Set respectively. “*Be My Valentine – Make Love Fresh*” won the Bronze Award in the category of General Entertainment In-House Art Direction & Design: Special Events Promos. “*Miss Chinese International Pageant 2006 Promotion*” also won the Bronze Award in the category of Total Package Design – Topical On-Air.

(d) Community and Public Service

Besides providing free TV entertainment and information to the public, TVB continued to contribute to the Hong Kong community through outreach community service and fund-raising programmes and activities.

A total of HK\$139 million was raised during the year for local and international charity organisations in aid of a wide range of worthy causes. Among such were the annual fund raising programme “*Tung Wah Charity Show 2006*” which not only entertained 1.5 million viewers, but also raised HK\$82 million for the Tung Wah Group of Hospitals. “*Caritas Star Studded Charity Show*” drew 1.1 million viewers and raised HK\$6 million for Caritas Hospital. “*Yan Chai Charity Show*” also captured 1.2 million viewers and raised HK\$24 million for Yan Chai Hospital. The anniversary special charity event, “*Community Chest Charity Show 2006*”, drew 1.3 million viewers and raised HK\$16 million for The Community Chest of Hong Kong.

(e) Digitisation

Development work on the infrastructure for our Digital Terrestrial Television (“DTT”) networks has started after obtaining town planning approval and land grant, in May and June 2006 respectively, for the Temple Hill Main DTT Station. All major site works had been completed by end of 2006 and work on the superstructure started in early 2007. The Temple Hill Station is expected to be ready for trial transmission at the beginning of the third quarter of 2007 and service launch in the fourth quarter of 2007, to meet the 2007 year-end roll-out deadline.

Our proposal for the DTT transmission standard for Hong Kong had been submitted to the Government on 30 December 2006. Our proposed specifications on the various relevant technical standards necessary for the launch of DTT are expected to be approved by the Government progressively starting in March 2007.

On the programme service side, besides continuing to provide existing free TV service on *Jade* and *Pearl* via our analogue network and simulcasting the channels in digital format on our half of the new digital Multiple Frequency Network, TVB will be providing a new programme channel broadcast in high definition TV format via our own Single Frequency Network. In preparation for this channel, plans to convert and upgrade studio and field production facilities are in progress to meet the service launch schedule.

International Operations

(a) Programme Licensing and Distribution

As a major producer and international content provider of Chinese-language TV programmes, TVB continued to benefit from international programme licensing and distribution as a major revenue source, in addition to the domestic terrestrial TV broadcasting activities. Our strategic shift to diversify into providing content for new media, and increase in the supply of titles through telecast licensing, channel distribution and video sell-through have resulted in steady overall single-digit percentage growth, successfully offsetting the down trend impact of traditional video licensing due to piracy and changes in technology.

The advent of new multi-media technology has enabled new business opportunities as well as posted challenges such as illegal internet downloading. During the year in review, we have started to provide contents under licensing arrangements to new channel operators and video-on-demand programme service providers via digital cable or internet platforms in Mainland China and Taiwan, with substantial growth in Mainland China. Similar activities will be extended to other countries in the new year.



We shall continue to expand through content licensing and distribution to new media platforms enabled by new technology, including internet download, via mobile phone and portable media players.

Despite tough competition in the market, growth in revenue from telecast licensing in Mainland China continued. We are encouraged by the good rating performance when CCTV1, the general entertainment channel of the state-owned national broadcaster, telecasted four TVB drama series ("*Strike At Heart*", "*A Pillow Case of Mystery*", "*Justice Sung*" and "*Not Just A Pretty Face*") which marked the first time that CCTV1 showed imported dramas from Hong Kong in many years.

Further progress was made in the collection of the licence fees under the Guangdong Landing Rights Agreement. Though the total revenue from telecast licensing in Malaysia and Singapore recorded a single-digit percentage decline, income from our major clients ASTRO All Asia Networks plc in Malaysia and Starhub Cable TV in Singapore showed encouraging growth over 2005.

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(b) Overseas Satellite Pay TV Operations

(i) TVB Satellite Platform (“TVBSP”) USA

In the United States, the number of subscribers to our five-channel Jadeworld package offered via DirecTV platform, achieved single-digit percentage growth.

TVBSP launched a Vietnamese-language channel with dubbed TVB programmes in November 2006. The channel has been well-received. In 2007, TVBSP is planning to expand via additional channels, and to widen its distribution network by exploring possible cooperation with new Internet Protocol Television (“IPTV”) platforms.

(ii) TVB Australia (“TVBA”)

In Australia, while subscription to our 12-channel Jadeworld pay platform grew at a single-digit percentage rate, it has reached the critical mass in its subscriber base. TVBA has started to record a small operating profit since the last quarter of 2006, with increase in both subscription and advertising revenue.

To strengthen its service line-up, TVBA launched an acquired Korean drama channel in July 2006 together with a nominal increase in subscription fee. It is exploring into launching Mandarin and/or Asian channels in 2007 to attract more subscribers and advertisers.

(iii) The Chinese Channel (“TCC”) Europe

In Europe, the number of subscribers to our single channel platform was relatively stable but advertising revenue achieved double-digit percentage growth, producing a single-digit percentage growth in operating profit when compared with 2005.

Capitalising on the growing digital market in Europe, TCC is considering launching new Cantonese and Mandarin channels through digital cable and IPTV platforms.

(c) Channel Operations

(i) TVBS – Taiwan

Despite the slow economy and a more competitive market with overall TV advertising spending down by more than 10% in Taiwan, TVBS managed to report a slightly improved total revenue figure in 2006 when compared with that of 2005 and maintained a relatively high Cost Per Rating Point (“CPRP”). The growth was made possible by successfully securing a bigger market share through

higher ratings, favourable brand image, aggressive and innovative marketing and a more desirable audience profile.



With comprehensive reports on major stories such as the Taipei and Kaohsiung mayor elections and the high profile corruption cases, our news channel *TVBS-News*' full year average prime time (6 pm to midnight) rating grew to 0.63 TVRs from 0.53 TVRs in 2005. Total daily rating also increased to 33.90 from 28.61⁵ (Source: AGB Nielsen, Taiwan). Similar improvement in rating performance was also experienced by the other TVBS channels.

The entertainment channel *TVBS-G*'s average rating in 2006 also went up with the Asian Games, which was a significant contributor in the last quarter. The channel is planning to emphasise on promoting TVB's new generation of artistes to further improve its desirable audience profile in 2007.

While Taiwan's media market would continue to be affected by its weak domestic economy resulting from political controversies, the National Communications Commission's (“NCC”, media industry's main governing body) efforts to promote full digitisation of all cable TV systems would offer more channel distribution and a la carte subscription opportunities. We would continue to cultivate new revenue sources and explore distribution and subscription potentials in the growing digital TV landscape in Taiwan.

⁵ *The TV industry in Taiwan operates on a guaranteed rating point system in which daily accumulative Gross Rating Points (GRPs) are indicative of the individual channel's inventory and performance.*

(ii) TVB8 and Xing He Channels

Both advertising and licensing income for the TVB8 and Xing He channels grew substantially in 2006, with particularly high growth in the South East Asian markets.

Xing He, featuring mainly TVB dramas produced a few seasons ago, was launched on ASTRO's (ASTRO All Asia Networks plc) Pay TV platform in Indonesia which contributed additional revenue to the operation. High rating performance of TVB dramas on Xing He and weekend specials on TVB8 helped to achieve more advertising sales for both channels. The variety shows "Minutes To Fame" (adapted from the programme format produced and broadcast on TVB Jade in 2005) and "Parkson Charity Show" (a musical event) organised by TVB8 in Malaysia, received enthusiastic responses. The localisation efforts by TVB8 in Malaysia through audience and contestant participation in variety shows, have proven successful. The channels will continue to explore these opportunities.

In Mainland China, TVB8 was actively involved in the co-production events organised by different domestic TV stations. (e.g. "Travel Around China – A Night Show in Ningbo 2006"). It has not only helped in promoting the TVB8 brand but also provided business opportunities for further development of our operation.

(iii) Supply of Channels to TVB Pay Vision Limited ("TVBPV")

Under a revamped format, TVB continues to supply eight channels to TVBPV on an exclusive basis since the second quarter of 2006.

The eight channels are *TVBN*, *TVB Classic*, *TVB Drama*, *TVB Kids*, *TVB Entertainment News*, *TVBM*, *TVBN2* and *TVB Lifestyle*.

TVB Drama established itself as a source for the best and latest available acquired popular dramas with the launch of many hit titles from Japan, Korea and Taiwan. *TVB Lifestyle* has successfully built up a following for its flagship programme "Be My Guest". The series'



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interviews with The Honourable Donald Tsang, the Chief Executive of Hong Kong, and media veteran Lai Chi Ying became talk of the town furthering the programme's acclaim. *TVB Kids* organised talent shows and activities, besides providing programmes that inform, educate and entertain its young viewers. During the year, *TVB Entertainment News* provided a platform for artistes and social groups to voice out concerns on the Gillian Chung incident and the local media's responsibility on privacy issues of individuals including artistes and public figures. *TVBM*, a music channel, launched and received positive response on "*Your Music Choice Festival*" which provided opportunities for aspiring musicians to show their talents. *TVB Classic* offered anthologies from the coveted vault of TVB classic dramas organised around particular well-known stars: The Andy Lau and Chiu Ngar Chi anthologies were especially well-received. *TVBN* continues to provide 24-hour news service, with up-to-date local and around the world news and financial, sports and weather information; while *TVBN2*, also a 24-hour news service, provides full length coverage of selected local and international news events.

Other Businesses

(a) Investment in TVB Pay Vision Holdings Limited ("TVBPVH")

TVB has 49% interest in the share capital of TVBPVH which operates one of the pay TV platforms in Hong Kong. Pay channels are distributed through satellite master antenna television and broadband service provided by Hutchison Global Communication Limited and PCCW Limited's NOW TV. Apart from being an investor in the platform, TVB also supplies a total of eight channels to TVBPVH on an exclusive basis, as noted above.

Subsequent to securing the distribution agreement with NOW TV in February 2006, the TVBPVH's channels were heavily promoted in the second quarter of 2006 in anticipation of the launch of this service on the NOW TV platform. The uptake of new subscribers was significant, due mainly to the offering of channels that complements the NOW TV channels, and the ready-availability of the channels through the existing set-top boxes which require minimal installation effort. TVBPVH is in the process of scaling up its sales effort, with a view to increasing subscriber uptake.

Whilst we are optimistic of the long term future of the pay TV business, the market remains extremely competitive. During the year, TVB shared losses of HK\$163 million of TVBPVH, which when compared with the losses shared of HK\$187 million for 2005, represented an improvement of 13%.

(b) Internet Operations

We continued to provide our programme contents to all of the four licensed 3G operators in Hong Kong. This resulted in a significant percentage growth in revenue. In addition, sale of contents to broadband operators remains an important source of revenue.



In 2007, we will seek to improve the quality and quantity of the contents in our portal – www.tvb.com. These improvements are aimed to increase site traffic and attract more advertising income. Having extended our content distribution to the Sony's Playstation Portable platform in 2006, we will also continue to be aggressive in the sale of our programme contents to handheld devices.

(c) Magazine Publishing

TVB Weekly is the Group's official magazine in Hong Kong which promotes our station and artistes. The year of 2006 was a difficult year for TVB Weekly as it was adversely affected by intense competition in the magazine publishing market. However, the positive image of our magazine has earned us a unique position that has won the support of TV

viewers and advertisers. Our special content and market promotion strategies have served to mitigate the decrease in circulation. Advertising revenue had increased by a low single-digit percentage. However, increase in publishing costs and decrease in magazine sales had resulted in a reduction in profits.

The editorial team will embark on a series of proactive measures to enrich the content and enhance the magazine's design. It has also planned to focus on women and family readers, in order to secure advertising revenue from related advertisers.

We shall capitalise on the magazine's 10th anniversary in 2007, and are planning to hold a series of promotional activities to help raise circulation and advertising revenue.

(d) Movie Investment

Despite having a satisfactory box office in Hong Kong in 2005 and receiving many awards in major Greater China Film Competitions, the movie "*Perhaps Love*" recorded a relatively weak performance in France and Japan. As the movie had been unable to win any Oscar nominations, distributors in Europe and North America did not have sufficient confidence in the marketability of the movie. Therefore, distribution sales in these two markets were below expectation. An overall small loss is anticipated.

(e) Music

During the year, TVB Music Limited, a wholly-owned subsidiary, co-invested in or participated as the production house for various concerts in public arenas in Hong Kong with satisfactory results.



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FINANCIAL REVIEW

IMPORTANT EVENT

On 24 August 2006, TVB Airtime Sales (Guangzhou) Limited, a wholly-owned subsidiary incorporated in Mainland China under CEPA II arrangement was set up to undertake advertising sales business in Mainland China for the Group's channels.

LIQUIDITY, FINANCIAL RESOURCES AND CAPITAL STRUCTURE

The balance sheet remains strong and well-capitalized. Non-current assets amounted to HK\$2,259 million, as compared to HK\$2,522 million at 31 December 2005. The net decrease was mainly attributable to the decrease in the net book value of property, plant and equipment by HK\$165 million, and decrease in interest in associate by HK\$95 million.

Trade and other receivables, prepayments and deposits increased from HK\$1,354 million to HK\$1,372 million which represented a 1% increase from the end of 2005. This mainly related to a higher level of billing to customers. Specific provision had been made, where appropriate, to cover any potential bad and doubtful debts.

Trade and other payables and accruals decreased from HK\$643 million to HK\$594 million which represented an 8% decrease from the position at the end of 2005. This was principally attributable to the reduction in the amount payable for a financial asset (51% equity interest in TVBPHV) as the remaining unpaid share capital which amounted to HK\$57 million was paid up in March 2006.

The Group continues to have a strong financial position attributable to the steady and growing cashflow from the business operations. As at 31 December 2006, the Group had bank and cash balances of HK\$1,597 million, an increase of 63% over 2005 (2005: HK\$980 million). About 10% of the cash balance was maintained in overseas subsidiaries for their daily operation. Cash and cash equivalents held by the Group were denominated in Hong Kong dollars, Renminbi, US dollars and New Taiwan dollars.

The Group generally finances its operations and business development with internally generated resources. As at 31 December 2006, the Group's net current assets amounted to HK\$2,752 million (2005: HK\$2,051 million). The current ratio, expressed as a percentage of current assets to current liabilities,

improved from 3.74 as at 31 December 2005 to 5.07 as at 31 December 2006. The total equity was HK\$4,868 million (2005: HK\$4,405 million).

As at 31 December 2006, the capital structure of the Company is constituted exclusively of 438,000,000 ordinary shares of HK\$0.05 each. There is no outstanding bank loan and other borrowings, and accordingly, the gearing ratio was zero as at 31 December 2006 (2005: zero).

The capital commitments of the Group as at 31 December 2006 were HK\$821 million (2005: HK\$183 million). There was a significant growth of 349% over 2005 reflecting an extensive capital expenditure programme for the development of Digital Terrestrial Television network and High Definition Television production plan.

CONTINGENT LIABILITIES

As at 31 December 2006, there were guarantees given to banks amounting to HK\$8.7 million (2005: HK\$8.7 million) for banking facilities granted to an investee company.

In March 2005 and February 2006, the Group received additional profits tax assessment notices from the Inland Revenue Department of Hong Kong ("IRD") for the years of assessment 1998/99 and 1999/2000 on the profits generated by the Group's programme licensing and distribution business carried out overseas. The total amounts of the additional assessments of profits tax for 1998/99 and 1999/2000 were HK\$98 million and HK\$99 million respectively. The Group was granted a holdover of these additional assessments by the IRD. Further additional profits tax assessment notices for the year of assessment 2000/2001 are expected to be issued before 31 March 2007.

The Group had filed an objection to these additional assessments. The Group believes that the objection is well-founded, and is determined to defend the Group's position vigorously. On this basis, the Group is of the view that no additional tax provision is necessary.

EXPOSURE TO FLUCTUATIONS IN EXCHANGE RATES AND RELATED HEDGES

The Group's foreign exchange exposures comprise trading and non-trading foreign currency translation exposures. Foreign exchange trading exposures mainly arises from trade receipts from overseas customers.

The Group is also exposed to currency fluctuation on translation of the accounts of overseas subsidiaries and also on the repatriation of earnings and loans. During the year, the appreciation of some foreign currencies such as the Australian dollars, UK pounds etc. had a positive impact on the Group. In order to mitigate the potential impact of currency movement, the Group will closely monitor foreign exchange exposure and will consider hedging significant foreign currency exposure when necessary. No forward exchange contract was entered into by the Group during the year under review.

HUMAN RESOURCES

As of 31 December 2006, the Group employed, excluding Directors and freelance workers but including contract artistes and staff in overseas subsidiaries, a total of 4,557 (2005: 4,519) full-time employees.

About 26% of our manpower was employed in overseas subsidiaries and was paid on a scale and system relevant to their localities and local legislations. For local employment, different pay schemes are operated for contract artistes, sales and non-sales employees. Contract artistes are paid either on a per-show basis or by a package of shows. Sales personnel are remunerated based on commission schemes. Non-sales personnel are remunerated on a monthly salary.

For local employees, discretionary bonuses may be awarded as an incentive for better performance. Depending on individual's performance, qualified personnel received discretionary bonuses between 0.75 and 1.25 of their monthly basic salaries for 2006.

No employee share option scheme was adopted by the Group during the year.

From time to time, the Group organises, either in-house or with vocational institutions, seminars, courses and workshops on subjects of technical interest, such as industrial safety, management skills and other related studies, apart from sponsoring of training programmes that employees may enrol on their own initiatives.

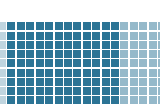
DRAMA HIGHLIGHTS



女人唔易做¹



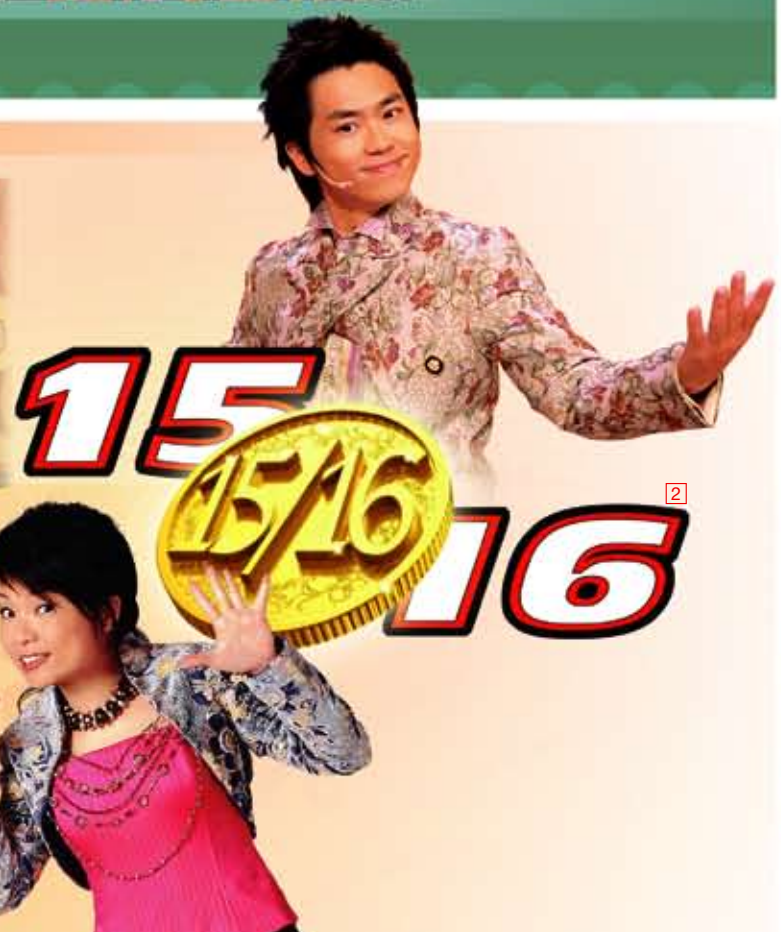
法證先鋒²



1. "La Femme Desperado" became an instant hit and the top drama of the year and achieved an average of 33 TVRs and 88% audience share on the Jade Channel.
2. "Forensic Heroes" became the second highest rated drama series and achieved an average of 33 TVRs and 87% share on the Jade Channel.
3. "Love Guaranteed" averaged 32 TVRs and 88% share on the Jade Channel.
4. "The Dance Of Passion" garnered 36 TVRs and 90% audience share for its debut episode, the highest first episode rating of dramas since 2002 (the drama series averaged 32 TVRs and 87% audience share).
5. "To Grow With Love" achieved an average of 32 TVRs and 91% audience share on the Jade Channel.



NON-DRAMA HIGHLIGHTS



1. "Beautiful Cooking", which combined celebrities, comedy and game show, achieved an average rating of 33 TVRs and 88% audience share on Sundays evening, the Jade Channel.
2. "15/16", a new quiz show, achieved an average rating of 29 TVRs and 89% audience share on weekdays evening, the Jade Channel.
3. "TVB 39th Anniversary Gala" achieved an average of 35 TVRs and 90% audience share on 19 November 2006, the Jade Channel.
4. "TV Awards Presentation 2006" achieved an average of 36 TVRs and 90% audience share on 10 November 2006, the Jade Channel.
5. "On The Road", a new docu-travelogue, achieved an average of 26 TVRs and 86% audience share on the Jade Channel.
6. "Be My Guest", a flagship programme on TVB Lifestyle Channel.

