# FINANCIAL REVIEW

## OVERVIEW

### CONTINUING OPERATIONS

For the year ended 31 December 2015, the Group's continuing operations comprised Hong Kong TV broadcasting, Hong Kong digital new media, programme licensing and distribution, overseas pay TV operations, channel operations and other activities, including movie investment; movie production; music entertainment and publications.

The Group recorded a revenue under continuing operations of HK$4,455 million (2014: HK$4,912 million), a decrease of 9%. Cost of sales decreased from HK$2,016 million to HK$2,009 million, a decrease of 0.3%. As a result, gross profit decreased from HK$2,896 million to HK$2,446 million, a decrease of 16%. The gross profit percentage stood at 55% (2014: 59%).

Overall, revenue from both Hong Kong and overseas businesses reported decline. Income from Hong Kong, comprising mainly advertising revenue, decreased due to the weaker advertising market, and the absence of one-off revenue from the 2014 World Cup. Further, income from the overseas key markets decreased, which was caused mainly by the strength of the US dollars against various foreign currencies, and a weaker performance from licensing and distribution in Mainland China.

Cost of sales decreased from HK$2,016 million to HK$2,009 million, a decrease of 0.3%. Included in the cost of sales were the cost of programmes, film rights and stocks which amounted to HK$1,539 million (2014: HK$1,575 million), a decrease of 2%, partly because of the absence of the licence rights and the production costs for the 2014 World Cup.

Selling, distribution and transmission costs amounted to HK$577 million (2014: HK$556 million), an increase of 4%, which reflected a higher staff cost level principally in Hong Kong.

General and administrative expenses amounted to HK$853 million (2014: HK$763 million), an increase of 12%. The increase was caused mainly by a provision for impairment on trade receivables amounted to HK$36 million made during the year, and one-off professional fees totalling HK$39 million incurred in relation to an aborted corporate reorganisation.

Due to the strength of the US dollar against various foreign currencies, the Group incurred exchange losses of HK$85 million during the year (2014: HK$12 million). Such exchange losses were mainly related to the re-translation of various foreign currencies such as Malaysian Ringgit, Renminbi and a loan in New Taiwan dollar. Last year, other losses also comprised a HK$73 million loss on liquidation of subsidiaries relating to overseas pay TV operations, following the discontinuance of the satellite distribution business model and the migration to TVB Anywhere.

In addition, exchange losses on Renminbi fixed term deposits amounted to HK$42 million was recognised resulted from the depreciation of Renminbi during the year.

Following a review of the operating environment in Hong Kong, the Board had decided to cease construction of the production studios and related facilities at a new site in Tseung Kwan O Industrial Estate, close to TVB City. Accordingly, an impairment loss of a net amount of HK$88 million was recognised, after taking into account of certain amounts refundable upon return of the site to Hong Kong Science and Technology Parks Corporation.

Operating profit before deducting (i) exchange losses on Renminbi fixed term deposits of HK$42 million and (ii) impairment loss on property of HK$88 million, amounted to HK$1,006 million (2014: HK$1,569 million), a decrease of 36%.

Furthermore, a total impairment loss of HK$695 million was recognised during the year (including the impairment loss of HK$654 million already taken up in the six months ended 30 June 2015), representing 100% of the Group's net interest in TVB Network Vision, an associate engaging in Hong Kong pay TV business, at 31 December 2015.

Profit before income tax for the year amounted to HK$126 million (2014: HK$1,482 million), a decrease of 91% over 2014.

The Group's taxation charge amounted to HK$144 million (2014: HK$221 million), a decrease of 35%. Whilst the profits tax rate for Hong Kong remained at 16.5%, the Group's major subsidiaries operate in the countries whose effective rates vary from 0% to 41%.

Overall, the Group's loss attributable to equity holders for continuing operations for the year amounted to HK$4 million (2014: a profit of HK$1,251 million).

## DISCONTINUED OPERATIONS

For the year ended 31 December 2015, the Group's discontinued operations comprised the Taiwan operations under Liann Yee Group. As announced on 29 January 2015, the Group disposed of a 53% equity interest in the Liann Yee Group to certain independent third parties for a cash consideration of NT$4,695 million (approximately HK$1,182 million) (the "First Disposal"). On 6 May 2015, this disposal was completed and a gain of HK$1,396 million (represented by a gain on disposal of the 53% equity interest of HK$852 million and a gain on the revaluation of the 47% retained interest of HK$544 million) was recognised. Prior to the First Disposal, Liann Yee Group had distributed a dividend to the Group and accordingly, a withholding tax of HK$53 million was also recognised.

Post completion of the First Disposal in May 2015, the Liann Yee Group has become a joint venture of the Group, resulting in the adoption of equity accounting in respect of the 47% retained interest in the Liann Yee Group.

In total, an amount of HK$103 million profit in respect of Liann Yee Group was recognised in the consolidated financial statements.

As further announced on 4 January 2016, the Group further disposed of the remaining 47% retained interest in Liann Yee Group, for a cash consideration of NT$4,343 million (approximately HK$1,017 million) (the "Second Disposal"). Upon its completion in March 2016, the Group has ceased to hold any interest in the Liann Yee Group.

In view of a plan to repatriate the proceeds of the Second Disposal to Hong Kong in the form of dividend upon completion, a deferred tax provision of HK$111 million had been made in the consolidated financial statement for the year.

Post completion of the First Disposal in May 2015, the Liann Yee Group's assets and liabilities had not been consolidated into the Group's consolidated statement of financial position at the year end. As a result of the Second Disposal entered into post year-end, the carrying value of the 47% retained equity interest together with a shareholder loan to the Liann Yee Group had been shown as "Non-current asset held for sale" and "Loan and receivables" respectively in the consolidated statement of financial position at 31 December 2015.

Certain property assets located in the Neihu District and on Bade Road in Taiwan have been transferred from the Liann Yee Group to the Group. The Group is leasing back these properties on normal commercial terms to the Liann Yee Group for use as studios and offices. These properties have been included as "Investment properties" in the Group's consolidated statement of financial position, and the related income was accounted for under continuing operations for the year.

## EARNINGS PER SHARE

Overall, the Group's profit attributable to equity holders for continuing operations and discontinued operations for the year amounted to HK$1,331 million (2014: HK$1,410 million), a decrease of 6%, giving a basic and diluted earnings per share from continuing and discontinued operations of HK$3.04 (2014: HK$3.22).

## SEGMENT RESULTS

Revenue under Hong Kong TV broadcasting which comprised advertising revenue from the Group's free TV channels and the pay TV channels declined from HK$3,420 million to HK$3,105 million, a decrease of 9%, due to the sluggish advertising market and absence of event in the year. The above decrease in revenue of HK$315 million mainly explained the reduction in the segment profit before non-recurring expenses from HK$947 million to HK$551 million, a decrease of 42%. Non-recurring expenses comprised (i) exchange losses on Renminbi fixed term deposits, (ii) impairment loss on property, and (iii) impairment loss on loan to and amount due from an associate. Taking into account of the non-recurring expenses, the segment results recorded a loss of HK$274 million (2014: a profit of HK$947 million).

Revenue from Hong Kong digital new media which comprised advertising revenue from mobile devices and website portals, declined from HK$196 million to HK$170 million, a decrease of 13%, due to the weaker advertising market resulting in lower advertising revenue. The segment profit decreased from HK$66 million to HK$41 million, a decrease of 38%.

# FINANCIAL REVIEW

Revenue from programme licensing and distribution which comprised licensing income from distribution of our programmes through telecast, video and new media licensing, decreased from HK$1,085 million to HK$951 million, a decrease of 12%. The decrease in revenue was mainly attributable to the lower licence fee receivable from Malaysia resulting from depreciation of the Malaysian Ringgit against Hong Kong dollars, and the lower licence fee from digital new media business in Mainland China. Higher programme costs and exchange losses in relation to a loan in New Taiwan dollars extended to the Liann Yee Group were incurred during the year. As a result, this segment recorded a profit of HK$410 million (2014: HK$619 million), a decrease of 34%.

Revenue from overseas pay TV operations which comprised revenue from our pay TV platforms in North America (USA), Australia and Europe, decreased from HK$243 million to HK$186 million, a decrease of 24%. The decrease in revenue was mainly due to the adverse impact on subscription revenue caused by the proliferation of pirated TV contents overseas. Such unfavourable variance was partly offset by savings in operating costs due to discontinuation of operations of the subsidiaries in Europe resulting from transformation of the business models from satellite distribution to TVB Anywhere. In 2014, we incurred a one-off loss on liquidation of subsidiaries in Europe amounting to HK$73 million. As a result, this segment recorded a loss of HK$31 million (2014: HK$100 million).

Revenue from channel operations which comprised revenue from TVB8 and Xing He, the Group's satellite TV channel operations, decreased from HK$125 million to HK$105 million, a decrease of 16%. The segmental profit decreased from HK$32 million to HK$17 million, a decrease of 47%, which was mainly caused by lower advertising revenue from Malaysia market but partly offset by some savings in costs, primarily staff expenses.

Revenue from other activities which comprised revenue from magazine publishing and production of musical works, recorded an increase from HK$75 million to HK$129 million, an increase of 72%. This segment recorded a profit of HK$11 million (2014: a loss of HK$3 million).

## LIQUIDITY, FINANCIAL RESOURCES AND CAPITAL STRUCTURE

The Group continued to maintain a strong financial position as at 31 December 2015. Total equity stood at HK$7,836 million (2014: HK$8,704 million), a decrease of 10%. There has been no change in the share capital of the Company, namely 438,000,000 shares in issue.

At 31 December 2015, the Group had unpledged bank and cash balances of HK$2,817 million (2014: HK$3,332 million), a decrease of 15%. Out of the unpledged bank and cash balances, 37% were in Hong Kong dollars, 35% in US dollars, 26% in Renminbi and 2% in other currencies. About 10% of the unpledged bank and cash balances (approximately HK$287 million) were maintained in overseas subsidiaries for their daily operations. Cash not immediately required for operations are being placed as time deposits with banks.

During the year, the Group had invested a joint venture to develop, produce and invest in primarily Chinese-language motion pictures. This investment was classified under "Available-for-sale financial assets" in the consolidated statement of financial position.

Trade receivables from third parties amounted to HK$1,381 million (2014: HK$1,551 million) decreased by 11% over the last year end, as trade receivables from the Liann Yee Group were not included in the consolidated statement of financial position as explained in "Discontinued operations". Special provision has been made, where appropriate, to cover any potential bad and doubtful debts. As more prepayments had been made during the year for the purchases of programmes and contents, the amount of "Other receivables, prepayments and deposits" at 31 December 2015 increased, when compared with 2014.

As the Group had reached a settlement with the Inland Revenue Department of Hong Kong on the tax audit in respect of the profits generated by the Group's programme licensing and distribution business carried out overseas, the tax reserve certificates purchased as at last year end were used for settlement during the year. Over-purchased tax certificates had been refunded during the year. Accordingly, the current income tax liabilities of the Group at 31 December 2015 decreased, when compared with 2014.

At 31 December 2015, the Group's net current assets amounted to HK$5,622 million (2014: HK$5,314 million), an increase of 6%. At 31 December 2015, the current ratio, expressed as the ratio of current assets to current liabilities, was 8.8 (2014: 5.0).

At 31 December 2015, the Group's total bank borrowings decreased to HK$235 million (2014: HK$392 million), which were related to a secured bank loan which is denominated in New Taiwan dollars and floating interest bearing. The maturity profile of the Group's borrowing was as follows: in the second year, HK$11 million (5%); in the third to fifth years, HK$54 million (23%); over five years, HK$170 million (72%). At 31 December 2015, the gearing ratio, expressed as a ratio of gross debts to total equity, was 3.0% (2014: 4.5%).

At 31 December 2015, certain investment properties of a subsidiary of the Group with net asset value of HK$584 million had been pledged to secure a bank loan granted to that subsidiary. In addition, bank deposits of HK$2 million had been pledged to secure banking facilities granted to certain subsidiaries of the Group.

At the year end, the Group had capital commitments totalling HK$166 million (2014: HK$100 million), an increase of 66%.

## FINANCIAL GUARANTEE

At 31 December 2015, there was guarantee given to a bank amounting to HK$7 million for banking facilities granted to an investee company (2014: HK$22 million granted to an investee company and a joint venture).

## 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 arise 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. In order to mitigate the potential impact of currency movement, the Group closely monitors its foreign exchange exposures and uses suitable hedging arrangements against significant foreign currency exposures, where necessary. No forward exchange or hedging contract was entered into by the Group during the year.

## HUMAN RESOURCES

At the year end, the Group employed, including contract artistes and staff but excluding Directors and freelance workers, a total of 4,221 (2014: 5,273) full-time employees. The reduction was due to the exclusion of the staff of the Liann Yee Group this year.

For employment in Hong Kong, different pay schemes apply to contract artistes, sales and non-sales personnel. Contract artistes are paid either on a per-show basis or by a package of shows basis. Sales personnel are remunerated on commission based schemes. Non-sales personnel are remunerated on a monthly salaries basis. About 4% of the Group's manpower was employed in overseas subsidiaries, and was paid on scales and systems relevant to the respective localities and legislations.

For Hong Kong employees, discretionary bonuses may be awarded as incentive for better performance. For the year, all qualified personnel received discretionary bonuses averaging 1.2 of their monthly basic salaries. The Group does not operate any employee share option scheme.

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 sponsorship of training programmes that employees may enrol on their own initiatives.

To sustain the long term steady supply of human resources for production, the Group has implemented a number of new initiatives during the year targeting the training and the development of internal staff for TV production in the areas of design and construction of settings for production, make-up and costume design, with a view to ensure that the necessary skills sets are appropriately retained and developed within our business.

The Group has also been running a scheme of staff rotation between different departments so that a selected number of staff can acquire the basic understanding of the operations of the participating departments, before settling into one of the departments. During the year, a total of three staff was carefully selected under this scheme, which is now in the second year of running.