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Exchange Rate Information

The Hong Kong dollar is freely convertible into other currencies (including the U.S. dollar). Since 1983, the Hong Kong dollar has been officially linked to the U.S. dollar and the current rate is US$1.00 to HK$7.80. However, even with this official exchange rate, and despite the efforts of the Hong Kong Monetary Authority, or HKMA's currency board to keep such rate stable, the market exchange rate of the Hong Kong dollar against the U.S. dollar continues to be influenced by the forces of supply and demand in the foreign exchange markets. Furthermore, the official exchange rate is itself subject to fluctuations and can be reset in circumstances where the secondary foreign exchange markets move beyond the HKMA's ability to back the official rate with foreign reserves.

Exchange rates between the Hong Kong dollar and other currencies are influenced by the rate between the U.S. dollar and the Hong Kong dollar.

The following table sets forth the average, high, low and period-end noon buying rate between the Hong Kong dollar and the U.S. dollar (in Hong Kong dollars per U.S. dollar) for the fiscal periods indicated:

	Average (1)	High	Low	Period-End
	HK$	HK$	HK$	HK$
Fiscal 2004	7.7821	7.8010	7.7085	7.8000
Fiscal 2005	7.7869	7.8002	7.7684	7.7718
Fiscal 2006	7.7601	7.7796	7.7506	7.7767
Fiscal 2007	7.8029	7.8289	7.7665	7.7968
Fiscal 2008	7.7915	7.8159	7.7497	7.8036
July 2008	7.8001	7.8039	7.7959	7.8017
August 2008	7.8076	7.8142	7.8036	7.8036
September 2008	7.7854	7.8094	7.7582	7.7659
October 2008	7.7589	7.7736	7.7503	7.7503
November 2008	7.7507	7.7560	7.7497	7.7501
December 2008	7.7504	7.7522	7.7497	7.7499
January 2009 (through January 9, 2009)	7.7533	7.7572	7.7504	7.7572

(1) The average of the noon buying rates on the last business day of each month during the relevant fiscal year period or the average noon buying rates for each business day during the relevant monthly period.

Source: Federal Reserve Bank of New York.

B. Capitalization and indebtedness

Not applicable

C. Reasons for the offer and use of proceeds

Not applicable

D. Risk Factors

You should carefully consider the risks described below and other information contained in this annual report before making an investment decision. The risks and uncertainties described below are not the only ones we face. Additional risks and uncertainties not presently known to us, or that we currently deem immaterial, may also impair our business operations. We cannot assure you that any of the events discussed in the risk factors below will not occur. If they do, our business, financial condition or results of operations could be materially adversely affected.

Risks Relating to Our Business and Operations

We cannot assure you that we will be able to maintain an increase in total revenues and operating results

Our total revenues increased to HK$1,303.0 million in fiscal 2008 from HK$1,141.3 million in fiscal 2007, and we recorded a net profit of HK$125.2 million in fiscal 2008 versus HK$28.9 million in fiscal 2007. The increased net profit in fiscal 2008 was mainly due to the benefit of shifting our business mix towards the more sustainable FTNS business, a change in the estimated useful lives for certain major telecommunications equipment effective from June 1, 2007, interest savings from senior-notes buyback and tax benefit from recognition of deferred tax asset on tax loss in prior years. However, we cannot assure you that we will be able to maintain our revenue and profit growth.

A larger portion of our revenue in fiscal 2008 was derived from our fixed telecommunications network business, which carries a higher margin than our international telecommunications business. Revenues from our international telecommunications business decreased by 10.0% in fiscal 2008, primarily due to a decrease in the total number of airtime minutes by 12.9%, which reflected a reduction in the operating scale of our international telecommunications business. With expected competitive pressure on tariff rates and a reduced operating scale, we expect our international telecommunications business to contribute a smaller portion of our revenue and net profit over time.

Revenues from our fixed telecommunications network business increased by 23.8% in fiscal 2008, primarily due to an increase in our average revenue per user and an increase in our subscription base by 17.3%. This increase was mainly driven by the growing demand for high bandwidth broadband Internet access service. However, we cannot assure you that our fixed telecommunications network business will continue to be profitable, as we will need to continue to expend substantial resources in developing and marketing broadband Internet access, local VoIP, IP-TV and corporate data services.

We have substantially less financial and human resources for the development of our business than some of our main competitors.

The telecommunications and pay-television markets in Hong Kong are highly competitive. Some of our main competitors for Internet access, local telephony, pay-television and international telecommunications services have longer operating histories and others are subsidiaries of large business conglomerates. Consequently, our competitors may have the following advantages over us:

- greater financial, technical, marketing and other resources;
- greater existing infrastructure;
- greater name recognition; and
- larger customer bases.

In addition, certain areas of the fixed telecommunications network business are very capital intensive. Our competitors may be able to devote more human and financial resources to research and development, network improvement and marketing than we can.

Our growth and profitability could be affected by an increasing number of local and foreign entrants in the international and local telecommunications, Internet access and television broadcasting markets.

The Hong Kong government continues to liberalize access into the telecommunications industry in Hong Kong, including issuing new wireless and wire-line FTNS Licenses. We expect the Hong Kong government to continue to open the telecommunications market in the next several years. In particular, the Company may be adversely affected as a result of the following:

- As of January 6, 2009, 246 PNETS Licenses had been issued in Hong Kong for the provision of external telecommunications services as defined in the Telecommunications Authority's Determination as of December 30, 1998. Some of these licenses are held by subsidiaries of major foreign telecommunications providers, which have competitive advantages due to their global presence and size.
- Around December 31, 2007, TVB and ATV, the only two licensed domestic territorial broadcasters in Hong Kong, launched their digital terrestrial television services and have since broadened such services to cover an increasingly large percentage of the viewing public in Hong Kong. The services offer a total of 13 free channels in both standard and high definition. This improvement in the quality of free television may result in a reduction in the number of subscribers for pay-television services.

Increasing liberalization of the telecommunications market in Hong Kong may continue to attract new local and foreign entrants to the market, which may broaden the variety of telecommunications services supplied by existing service providers, thereby heightening the overall level of competition in our industry. Increased competition could result in price reductions, reduced gross margins or loss of market share, any of which could adversely affect our future growth and profitability.

The development of our Next Generation Network requires significant capital expenditures. These capital expenditures may vary materially from those currently planned and may impose a burden on our financing and operating activities.

Our business is capital intensive, and our capital expenditures may not have the positive effect on our business and revenues that we expect. We have made, and will continue to make, capital investments in the expansion and upgrade of our self-owned Next Generation Network and the development of our telecommunications services. We incurred total capital expenditures of approximately HK$211.7 million in fiscal 2008 and expect to incur capital expenditures of approximately HK$650 million in total in fiscal 2009 and 2010, a large majority of which will be spent on the continued expansion and upgrade of our network.

While we intend to fund such expenditures by using our currently available cash as well as cash flow from operations, we may not have adequate capital to fund our projected capital expenditures. Future, additional debt or equity financing may not be available, and debt financing, if available, may involve restrictions on our investing, financing and operating activities.

We may not realize the commercial benefits we expect from our investments, which may adversely impact our business.

To compete effectively, we need to launch from time to time new and commercially viable products and services. Any of these new services may not be commercially successful, and we may not be able to adapt the new services effectively and economically to meet consumers' demand. Because we are required to continue to make significant investments in our network infrastructure in order to support these services, we cannot assure you that we can generate satisfactory investment returns. Specifically, we cannot assure you that any services enabled by upgrading and expanding our Next Generation Network will be accepted by the public to the extent required to generate an acceptable rate of return. Furthermore, we cannot assure you that our estimate of the necessary capital expenditure to offer such services will not be exceeded. The failure of any of our services to achieve commercial acceptance could result in additional capital expenditures or, to the extent that we are required under the applicable accounting standards to recognize a charge for the impairment of assets, a reduction in our profitability. Any such charge could materially and adversely affect our financial condition and the results of our operations.

We may need to improve our internal controls over financial reporting and our independent auditors may not be able to attest to their effectiveness.

The United States Securities and Exchange Commission, or the SEC, as required by Section 404 of the Sarbanes-Oxley Act of 2002, adopted rules requiring every public company to include a management report on such company's internal controls over financial reporting in its annual report, which contains management's assessment of the effectiveness of the company's internal controls over financial reporting. In addition, an independent registered public accounting firm must attest to and report on the effectiveness of the company's internal controls over financial reporting. As a non-accelerated filer, we are required to file management's first report on internal controls over financial reporting for fiscal 2008 and our first auditor's report on the effectiveness of our internal controls over financial reporting for fiscal 2010.

We have evaluated our internal controls surrounding the financial reporting process for the current fiscal period so that management can attest to the effectiveness of these controls, as required by Section 404 of the Sarbanes-Oxley Act of 2002. We have implemented appropriate steps to strengthen the internal controls. However, we may identify conditions that could result in significant deficiencies or material weaknesses in the future. As a result, we could experience a negative reaction in the financial markets and incur additional costs in improving the condition of our internal controls. For a detailed discussion of controls and procedures, see Item 15 "Controls and Procedures".

Notwithstanding our efforts, our management may conclude that our internal controls over our financial reporting are not effective. However, in fiscal 2010, even if our management concludes that our internal controls over our financial reporting are effective, our independent registered public accounting firm may conclude that our internal control over financial reporting is not effective.

If we do not successfully design and implement changes to our internal controls and management systems, or if we fail to maintain the adequacy of these controls as such standards are modified or amended from time to time, we may not be able to comply with Section 404 of the Sarbanes Oxley Act of 2002. This could subject us to regulatory scrutiny and penalties that may result in a loss of public confidence in our management, which could, among other things, adversely affect our customers and vendor confidence, stock price, our ability to raise additional capital and operate our business as projected.

Our growth and expansion may impact our ability to manage our operations, increase our costs of operation and adversely affect the quality of our services.

We have been pursuing a strategy of aggressive growth in our fixed telecommunications network services business. As part of this strategy, we intend to continue to expand and invest in our Next Generation Network infrastructure to support our range of broadband Internet access, local VoIP, IP-TV and corporate data services. The deployment of these projects has resulted and will result in significant demands on our systems and controls and may impact our administrative, operational and financial resources. Our ability to manage our future growth will depend upon our ability to:

- simultaneously manage implementation of our infrastructure development and marketing plans;
- effectively monitor our operations so as to contain costs and maintain effective quality controls; and
- continue to offer competitive prices to customers for our services.

Our failure to achieve any of the above in an efficient manner and at a pace consistent with the growth of our fixed telecommunications network services business could have an adverse effect on the quality of our services and increase our costs of operation.

We depend on certain key personnel, and our business and growth prospects may be disrupted by the loss of their services.

Our future success is dependent upon the continued service of our key executives and employees. While we have employment agreements with members of our senior management staff, we cannot assure you that we will be able to retain these executives and employees. If one or more of our key personnel are unable or unwilling to continue in their present positions, or if they join a competitor or form a competing company, or if they shift their focus away from Hong Kong operations, we may not be able to replace them easily, our business may be significantly disrupted and our financial condition and results of operations may be materially and adversely affected. Furthermore, as our industry is characterized by high demand and increased competition for talent, we may need to offer higher compensation and other benefits in order to attract and retain key personnel in the future. We cannot assure you that we will be able to attract and retain the key personnel that we will need to achieve our business objectives.

Expansion of our Next Generation Network into certain buildings and residences may be limited by physical limitations or our ability to obtain access rights.

We intend to continue to expand the coverage of our Next Generation Network. To expand coverage to a new physical site within a residential or commercial building, we are required to connect our Next Generation Network to the site by installing fiber-to-the-home or fiber-to-the-building plus Category-5e copper wiring, which we refer to as in-building wiring. Our target is to increase the coverage of our Next Generation Network from the current number of 1.5 million residential home passes to our target of 2.0 million residential home passes by 2010. Such expansion, however, may be hindered by the following constraints:

- Because at least one of our competitors has already installed in-building wiring in virtually all buildings, other fixed telecommunications network service providers, including us, may encounter a bottleneck when installing our own in-building wiring because many buildings have limited physical space for additional in-building wiring.
- Some single-owner commercial buildings may grant rights of access to our competitors while barring us from installing our own in-building wiring.
- Certain developers may have affiliations with our competitors and may attempt to delay our wiring installations.

We may be unable to capitalize on any economy of scale benefits if we fail to expand our network coverage at our projected rate. Our growth opportunities will also be limited as a result.

Internet security concerns could adversely affect our Internet access services.

We intend to continue to upgrade our broadband Internet access, local VoIP, IP-TV and corporate data services. Computer viruses, break-ins and other inappropriate or unauthorized uses of our Next Generation Network could affect the provision of our full suite of Internet Protocol services. Computer viruses, break-ins or other problems could have the following effects on our fixed telecommunications network business:

- interruption, delays or cessation in services to our customers;
- a threat to the security of confidential information stored in the computer system of our customers; and
- illegal viewing or download of our contents.

There is no assurance that computer viruses and other harmful attacks could not affect our business. We may incur significant costs to protect us against the threat of security breaches or to alleviate problems caused by such breaches. We intend to continue to strengthen our network security to alleviate these problems. Our efforts, however, may cause interruptions, delays or cessation of our services, and our customers may stop using our service or assert claims against us as a result.

Although we have expressed our interest in obtaining a Broadband Wireless Access ("BWA") license, we cannot assure you that we will be the successful bidder, and, if we are granted the license, that the business in relation to BWA will be successful.

Even though we have participated in the auction, we cannot assure you that our bid will be successful, if succeeded and the related license is granted to HKBN eventually, that our business and operation in relation to BWA will generate sufficient revenues to result in profitability. We are also subject to the risks of unforeseen technological development or other technological difficulties and/or cost overruns.

Risks Relating to Our Technological Infrastructure

We may be unable to further expand our Internet access business unless we obtain additional network capacity.

Our Internet access network has limited capacity. Our ability to continue to increase Internet service depends on our ability to expand the network bandwidth on a timely basis, which in turn is subject to:

- the expansion and development of our own international telecommunications facilities;
- the availability of leased capacity from third party carriers at favorable rates; and
- the possible termination or cancellation of our existing contracts.

If we fail to increase the capacity of our international bandwidth, our ability to increase our market share and revenue in the Internet access business will be limited.

We are vulnerable to natural disasters and other disruptive regional events, which could cause damage to our network and result in lost revenue and perhaps lost customers.

Our network is vulnerable to damage or cessation of operations from fire, earthquakes, severe storms, heavy rainfall, power loss, telecommunications failures, network software flaws, vandalism, transmission cable cuts and other catastrophic events. We may experience failures or shut downs relating to individual points of presence or even catastrophic failure of our entire network. Any sustained failure of our network, our servers, or any link in the delivery chain, whether from operational disruption, natural disaster or otherwise, could have a material adverse effect on our business, financial condition and results of operations.

The loss of key suppliers or their failure to deliver equipment on a timely basis could negatively impact our business prospects.

We rely on our suppliers for our Next Generation Network infrastructure and follow-up maintenance. Further, because an IP set-top-box must be installed in order to access our IP-TV services, we must have an adequate supply of such installation equipment on hand to respond to new customer subscriptions in a timely manner.

We purchase all of our IP set-top boxes and other equipment from our suppliers on a purchase order basis and have no long-term contracts. If our suppliers are unable to supply us with these products in a timely manner or the costs of these products increase due to unforeseen causes, this could negatively impact our operating results, especially if we are unable to acquire new subscribers or effectively appropriate our costs on to our customers.

Our reliance on third parties to provide maintenance and repairs for our Next Generation Network could adversely affect our operating results if their services are not timely or do not meet our standards.

We depend on our suppliers and other third parties for ongoing support and assistance with respect to maintenance and repairs of major network equipments. We are also dependent on certain Hong Kong rail transport providers to maintain and provide us with access to their infrastructure to support the proper functioning of our equipment and fiber-based backbone. If these third parties fail to respond or are untimely in their response to our maintenance and repair needs, our customers may experience interruptions or variations in the quality of our fixed telecommunications network services. Any service interruptions or variations may adversely affect our operating results and our ability to retain or add new customers.

If we are unable to stay ahead of technology trends and evolving industry standards, our services may become obsolete.

To compete successfully, we are required to continually improve our performance, services and network. Telecommunications businesses are characterized by rapidly changing technology and industry standards, evolving subscriber needs and the changing nature of services with increasingly shorter life cycles. To respond successfully to technological advances and emerging industry standards, we may be required to make substantial capital expenditures and gain access to related or enabling technologies in order to integrate the new technology with our existing technology.

Further, new technology or trends in the telecommunications industry could have an adverse effect on the services we currently offer. For example, the replacement of traditional fixed line home telephones with mobile telephones and/or VoIP services may lead to a decline in our revenue from international telecommunications services and local telephony services. Further, technology substitution from global VoIP providers, some of which offer free PC-to-PC based international calls, is also becoming more prevalent. Changing our services in response to market demand may require the adoption of new technologies that could render many of the technologies that we are currently implementing less competitive or obsolete.

Finally, our new products and services may contain design flaws or other defects that could have a material adverse effect on our business, operating results or financial condition. We may not be successful in modifying our network infrastructure in a timely and cost-effective manner in response to these changes, which will affect our ability to continue to offer the products and services demanded by our customers.

Risks Relating to the Regulatory, Political and Economic Environment

Regulatory reforms and currently contemplated regulatory initiatives in the telecommunications industry may adversely affect us.

The Hong Kong telecommunications industry is undergoing continuous regulatory reform. Our business and results of operations may be adversely affected by changes in the telecommunications regulations, especially in the following areas:

- In July 2004, a new provision of the Telecommunications Ordinance came into force. This anti-competition provision specifically regulates the conduct of all carrier licensees (in particular merger and acquisition transactions) in the Hong Kong telecommunications industry by giving the Telecommunications Authority the power to review the conduct and transactions concerning carrier licensees and to take appropriate actions if it determines that the transaction would, or is likely to, prevent or substantially lessen competition in a telecommunications market. The Telecommunications Authority has the power under this provision to conduct an investigation into any questionable transaction. It might consent to the transaction (unconditionally or subject to any conditions it deems appropriate) or reject the transaction outright. The decision of the Telecommunications Authority will take into account of whether the transaction will adversely affect the public interest and benefit. This provision may have an adverse effect on our ability to grow our business through mergers and acquisitions.

- We offer local VoIP services through our Next Generation Network under HKBN’s FTNS License. Following the conclusion of a public consultation on the regulation of Internet Protocol Telephony Services, the Telecommunications Authority issued a statement on June 20, 2005, setting out its views and decisions on the regulatory and licensing framework for the provision of VoIP services, including the creation of a licensing framework, conformance to the existing system of assigning telephone numbers, imposition of interconnection charges and establishing guidelines with respect to the quality of services.

- We offer fixed but not mobile telecommunications network services. The Telecommunications Authority has implemented a new fixed-mobile convergence licensing practice by way of the Unified Carrier License (“UCL”). The implementation of the UCL regime started from August 1, 2008 and replaces the existing four classes of carrier licenses for the provision of fixed and mobile services. Going forward the UCL will be the only carrier licence to be issued for the provision of fixed, mobile and/or converged services. Existing carrier licenses will remain effective until their expiry date. Licensees can choose to apply to convert their existing licences to UCLs before then or apply for a UCL upon expiry. This regulatory change, together with the development of new technologies, may further accelerate the convergence of fixed and mobile telecommunications services, resulting in more structural competition between fixed-line and mobile telecommunications operators. As we do not have a mobile license, and are not currently authorised to provide mobile services, our ability to compete may be hindered by our inability to offer such services independently.

- We provide our IP-TV services over our Next Generation Network under HKBN's FTNS License. The Hong Kong government has indicated that because our IP-TV services are carried over the Internet, we are exempt under the Broadcasting Ordinance from the requirement to obtain a domestic pay-television program service license. However, the government's Communications and Technology Branch has informed us that the government is considering a review of the broadcasting regulatory regime and may introduce changes to the existing regulatory framework, including the existing exemption in the Broadcasting Ordinance. However, we cannot predict whether the government may require us to obtain a pay-television program service license in the future.

We require licenses from the Telecommunications Authority to provide our services. If one of these licenses is revoked or not renewed, we would be unable to deliver the services authorized by that license.

We require licenses from the Telecommunications Authority to provide our international telecommunications and fixed telecommunications network services. Our PNETS License is subject to the Telecommunications Authority's annual renewal. HKBN's FTNS License was initially granted in 2000 for a term of 15 years and may be renewed for such further period not exceeding 15 years at the discretion of the Telecommunications Authority. The Telecommunications Authority's failure to renew or its revocation of any of these licenses for any reason would prohibit us from continuing to offer the services authorized by that license, which would have a significant adverse impact on our revenues and profitability. In addition, there may be future changes in Hong Kong's telecommunications regulations or policies that would require us to obtain additional licenses, which could have an adverse impact on our operations.

Our international telecommunications revenues may be adversely affected by increases in tariffs in China.

In China, tariffs for all domestic and international long distance services offered through public switched telephone networks, leased lines and data services are jointly set by the Ministry of Information Industry and the State Development Planning Commission. Certain tariffs payable by us to our carrier partners are based, among other things, on the tariffs set by these agencies with respect to the calls our subscribers make to persons in China. In fiscal 2008, approximately 77% of our international call traffic volume was to China. We cannot predict the timing, likelihood or magnitude of any tariff adjustments that may be imposed by the Ministry of Information Industry and the State Development Planning Commission, nor can we predict the extent or potential impact upon our business of any future tariff increases. Such increases may lead to a decrease in traffic, reduce our revenues and adversely affect our business and results of operations. In addition, if we are unable to effectively manage the increased network costs, it would have an adverse effect on the profit margins for our international telecommunications services.

As approximately 49% of our staff are located in Guangzhou, China, changes in Chinese labor or business laws may significantly affect our operations and our ability to service our Hong Kong based customers.

Our call center in Guangzhou employs over 1,400 persons and is an important resource for us. We are therefore significantly affected by the laws and regulations that govern foreign companies with operations in China. As the Chinese legal system develops, changes in such laws and regulations, their interpretation or their enforcement may lead to restrictions on our ability to hire and retain our employees in China, which could impact our ability to provide service to our Hong Kong-based customers.

Currency fluctuations of the Hong Kong dollar, our functional currency, may increase our operating costs and long term liability.

Our revenues are predominantly denominated in Hong Kong dollars. A major portion of our operating costs consist of interconnection charges paid to overseas carriers for the delivery of our international calls. Substantially all of these interconnection charges are denominated in U.S. dollars or other foreign currencies. In addition, the equipment and hardware we purchase for the expansion of our Next Generation Network constitutes a large portion of our capital expenditures and is also denominated in U.S. dollars. Finally, payment of interest, principal and any other amounts due under our 8.75% senior notes due 2015 are made in U.S. dollars. Since October 17, 1983, the Hong Kong dollar has been linked to the U.S. dollar at the rate of HK$7.80 per US$1.00. We, however, cannot assure you the link will be maintained in future.

The expenses that we incur in relation to our call center located in Guangzhou, China are denominated exclusively in Renminbi, the official currency of the People's Republic of China. These include the salaries that we pay to our personnel as well as various operating expenses that we incur to maintain our operations. As a result, we are exposed to a certain amount of foreign exchange risk based on fluctuations between the Hong Kong dollar and the Renminbi. The Renminbi is presently pegged to a basket of currencies, and there remains significant international pressure on the PRC government to further liberalize its currency policy. This could result in a further and more significant appreciation in the value of the Renminbi against the Hong Kong dollar, which would increase the cost of operating our call center.

Any depreciation of the Hong Kong dollar against the U.S. dollar, Renminbi or other currencies would increase our operating costs, including our debt servicing costs, make our capital expenditure plans more expensive, and adversely affect our profitability.

Impact of credit crunch on local and global economy may negatively impact our business and our progress on NGN development.

The current credit crunch will affect both the local economy and global economy. Although we have sufficient cash to meet our anticipated cash needs for at least the next 12 months, the current market conditions may affect our ability to obtain further financing to support our network expansion in the future. Failure to do so will negatively impact our business and slow down our progress on NGN deployment. The economic downturn may also dampen the demand for broadband services or affect our customers' ability to continue with existing services.