Financial Review

INTRODUCTION

This Financial Review is designed to assist the readers in understanding the Group's financial information through a discussion of the business performance and financial position of the Group as a whole.

The Interim Report contains the Consolidated Income Statement, Consolidated Statement of Comprehensive Income, Consolidated Balance Sheet, Consolidated Statement of Changes in Equity and Consolidated Cash Flow Statement. Following this financial information are notes that further explain certain figures presented in the report.

The Interim Report contains the report of CITIC Telecom International's auditor, KPMG, of their independent review of the Group's interim financial report.

BASIS OF ACCOUNTING

The Group has prepared its interim financial report in accordance with Hong Kong Financial Reporting Standards issued by the Hong Kong Institute of Certified Public Accountants.

REVIEW OF FINANCIAL PERFORMANCE

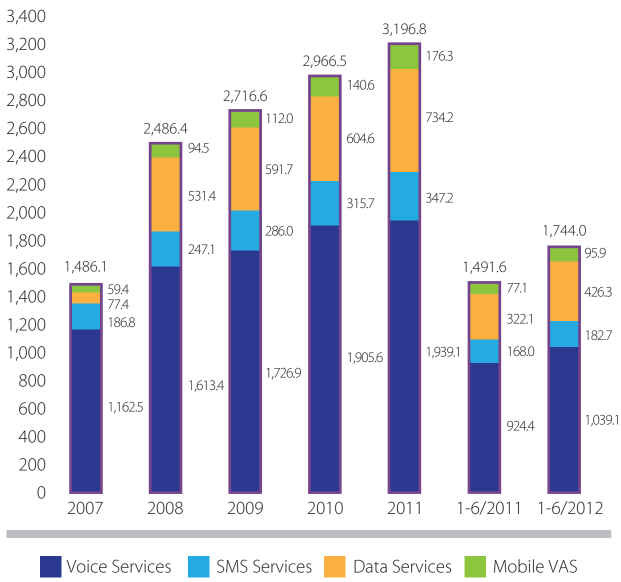
Turnover

The Group's turnover increased 16.9% to HK$1,744.0 million for the six months ended 30 June 2012 compared with HK$1,491.6 million for the corresponding period in 2011.

Voice Services turnover has grown by HK$114.7 million or 12.4% to HK$1,039.1 million for the six months ended 30 June 2012 over the same period in 2011. The Group handled a total traffic of 4.70 billion minutes, 8.8% more when compared with the same period of last year. Total China inbound and outbound traffic remained stable. The increase was mainly due to the Group's successful efforts in strengthening its international coverage which resulted in a 38.8% increase in international traffic. Owing to the change in mix between China and international traffic, the overall revenue per minute increased by 3.3% over the same period of last year.

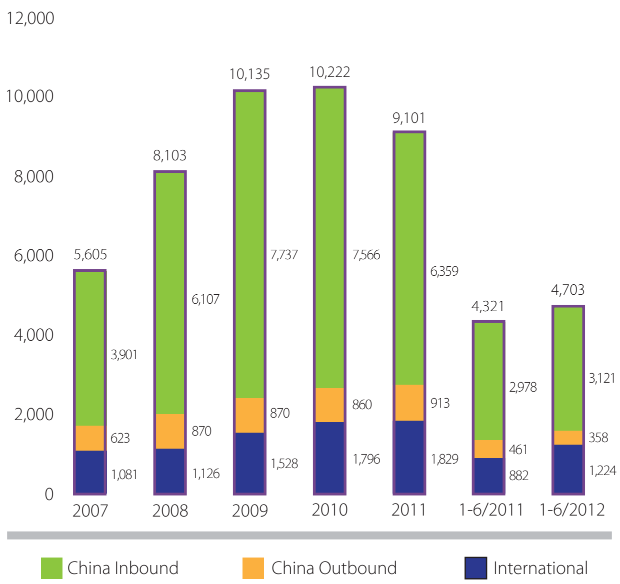
TURNOVER

HK$ Million



TRAFFIC (BY LOCATION)

Minutes in Million



SMS Services sustained stable growth during the first six months of 2012. SMS turnover increased by HK$14.7 million to HK$182.7 million for the six months ended 30 June 2012, an 8.8% growth as compared to the same period of 2011. Owing to the increasing popularity of social networking applications, the number of Hong Kong domestic SMS dropped by 20.0% during the period. International SMS continued to maintain stable growth and the increase in international traffic has partly offset the decrease in local domestic SMS. As a result, the number of messages handled by the Group dropped 1.4% to 964 million messages from the corresponding period of 2011. The average revenue per SMS has increased by 10.3%. During the period, China inbound and outbound traffic increased by 18.3% and 9.8% respectively as the Group secured additional China traffic through the continued expansion of international network coverage and enhanced quality management. The Group's international traffic also experienced a 2.5% growth in the first half of 2012 compared with 2011 as the Group continued to advance its leading market position by enhancing the quality of service and implementing an effective pricing strategy.

Mobile Value-added Services ("VAS") registered strong growth in the first half of 2012 with turnover increasing 24.4% to HK$95.9 million compared with the corresponding period for 2011. The growth was due to the Group's successful strategy to customise existing products to address changing market needs and providing bundled services which were well received by China operators.

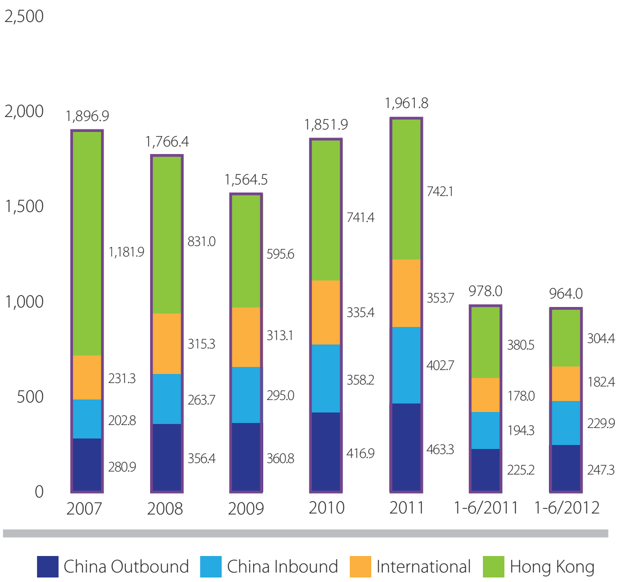
The Group's Data Services comprise managed VPN services and other services such as data centre services. During the first six months of 2012, turnover from Data Services increased by 32.4% to HK$426.3 million compared with HK$322.1 million for the same period of 2011. The significant increase was mainly due to the increase in demand of VPN services, cloud services and the first time inclusion of revenue from China Enterprise Netcom Corporation Limited ("CEC-HK").

Net foreign exchange gain/(loss)

Net foreign exchange gain/(loss) arose mainly from the normal trading business of both local and overseas operations of the Group and funding arrangements for overseas operations. The Group's major trading currencies were the United States dollar, the Hong Kong dollar and the EURO. The Group has not entered into any foreign currency hedging arrangements during the period.

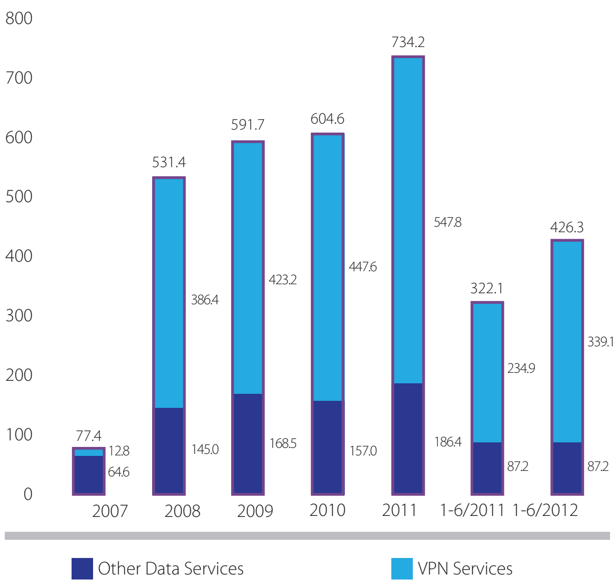
NUMBER OF SMS

Messages in Million



DATA SERVICES TURNOVER

HK$ Million



Network, operations and support expenses

Network, operations and support expenses amounted to HK$1,233.7 million in the first half of 2012, an increase of 20.3% as compared with the corresponding period of 2011. Owing to the first time inclusion of CEC-HK, the increase in network, operations and support expenses was higher than the turnover. The percentage of network, operations and support expenses of turnover was 70.7% for the first half of 2012, similar to the corresponding period for 2011.

Staff costs

Staff costs for the six months ended 30 June 2012 amounted to HK$140.8 million, an increase of 3.4% over HK$136.2 million for the same period of 2011. The increase was mainly due to the increase in equity-settled share-based payment expenses for 2012.

Depreciation and amortisation

Depreciation and amortisation expenses amounted to HK$74.5 million, an increase of HK$16.0 million as compared with the corresponding period of 2011. The rise was mainly due to the new data centre and the network system upgrade in 2011 and also due to the increase in the amortisation of intangible assets recognised on the acquisition of CEC-HK in July 2011.

Other operating expenses

Other operating expenses for the six months ended 30 June 2012 amounted to HK$96.7 million, an increase of 17.5% compared with HK$82.3 million for the corresponding period of 2011. The rise was mainly due to the inclusion of CEC-HK's operating expenses subsequent to its acquisition, higher utilities charges incurred by the new data centre, and an increase in repairs and maintenance expenses during the period, which were consistent with the Group's operational growth.

Share of profit of an associate

During the first six months of 2012, the Group's 20% share of the profit of the associate, Companhia de Telecomunicacoes de Macau, S.A.R.L. ("CTM") amounted to HK$75.2 million which has decreased by 2.3% compared with the corresponding period of 2011. The decrease was mainly due to the one-off rebate to CTM customers as a result of its service outage in the beginning of the year. The decrease in contribution from CTM was partly offset by the reduction in amortisation of intangible assets.

Income tax

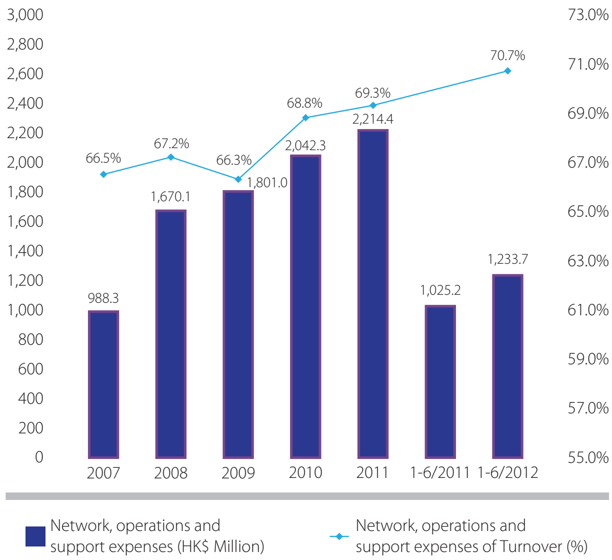
The Group's income tax expense for the six months ended 30 June 2012 amounted to HK$33.9 million, similar to the corresponding period of last year and if we excluded the profit contribution from CTM, the effective tax rate for both 30 June 2012 and 2011 was approximately 17.3%.

Profit attributable to equity holders of the Company

The Group recorded a net profit of HK$238.8 million for the six months ended 30 June 2012, an increase of 2.1% compared with the same period of 2011. The increase was mainly due to the growth of business which was partly offset by the increase in depreciation and amortisation expenses and increase in other operating expenses as mentioned above.

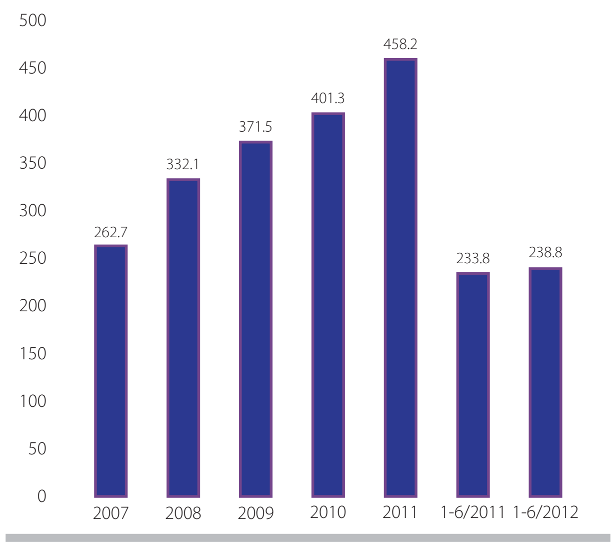
NETWORK, OPERATIONS AND SUPPORT EXPENSES

HK$ Million



PROFIT ATTRIBUTABLE TO EQUITY HOLDERS OF THE COMPANY

HK$ Million



Earnings per share ("EPS")

Basic EPS and diluted EPS were both HK10.0 cents for the six months ended 30 June 2012, representing an increase of 2.0% and 2.0% respectively as compared with the corresponding period of last year. The rise was mainly due to the growth of the Group's business.

Dividend per share

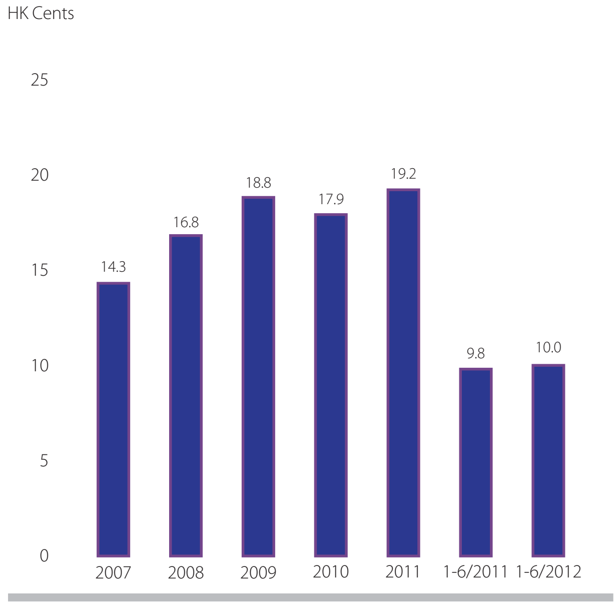
An interim dividend of HK2.4 cents per share is proposed for the first half of 2012.

Capital expenditure

Capital expenditure was HK$50.9 million for the first six months of 2012, a decrease of 23.3% as compared to the same period of 2011. As the new data centre in 2011 has proven to be very popular to customers, the Group has undertaken to expand its data centre at CITIC Telecom Tower where HK$15.3 million of fitting-out costs were incurred during the first half of 2012.

Excluding the capital expenditure on the data centre, the capital expenditure for the first half of 2012 amounted to HK$35.6 million, a rise of 36.4% compared to the six months ended 30 June 2011. The increase was mainly incurred in the network system upgrade in order to enhance the Group's quality of service.

BASIC EARNINGS PER SHARE



TREASURY POLICY AND RISK MANAGEMENT

General

Managing financial risks to which the Group is exposed is one of the primary responsibilities of the Group's treasury function. Financing and cash management activities are centralised to maintain a high degree of financial control and strengthen the Group's risk management.

Exchange rate risks

A substantial portion of the Group's sales revenue and cost of sales are denominated in the United States dollar, to which the Hong Kong dollar is pegged. In addition, the Group's financial assets, financial liabilities and transactions are mainly denominated either in Hong Kong dollars or United States dollars. Management considers that the Group's exposure to foreign currency risk is not material and continues to monitor closely all possible exchange rate risks and implement the necessary hedging arrangement to mitigate risk from any significant fluctuation in foreign exchange rates.

Credit risk

Credit evaluations are performed on all customers with a credit level exceeding a certain amount. Trade receivables are due within 7 to 180 days from the date of billing. The Group will assign an officer who will be responsible to agree on a settlement plan with those debtors having balances due over one year to reduce the outstanding balance within a reasonable period.

The Group has certain concentration risk in respect of trade receivables due from the Group's five largest customers who accounted for approximately 55% and 54% of the Group's total trade receivables at 30 June 2012 and 31 December 2011 respectively. The credit risk exposure to trade receivables balance has been and will continue to be monitored by the Group on an ongoing basis and the impairment loss on doubtful debts has been within management's expectations.

DIVIDEND PER SHARE

GROUP LIQUIDITY AND CAPITAL RESOURCES

The Group manages its exposure to liquidity risk by reviewing the cash resources required to meet its business objectives.

During the six months ended 30 June 2012, the Group's cash and cash equivalents remained stable at HK$266.9 million (31 December 2011: HK$253.3 million).

The Group had net operating cash inflow plus dividends received from an associate totaling HK$322.5 million at 30 June 2012, a decrease of HK$28.7 million when compared with the corresponding period for 2011. The decrease was mainly due to the short delay in settlements of trade receivables by certain customers in June 2012.

The Group raised loans of HK$100 million for the payment in relation to the completion of acquisition of China Enterprise Communications Ltd. ("CEC") upon obtaining approval from the PRC government and capital expenditure for the new data centre. In addition, the Group received HK$180.7 million in dividends from the associate and the Group paid dividends of HK$171.8 million for return of profits to its shareholders during the six months ended 30 June 2012. The loan from its associate which amounted to HK$124.1 million was fully settled during the current period.

At 30 June 2012 and 31 December 2011, the Group had a net cash balance of HK$170.6 million and HK$133.7 million respectively.

Currency portfolio

The original denomination of the Group's cash and bank deposits by currencies at 30 June 2012 is summarised as follows:

	Denomination				
HK$ Million Equivalent	HKD	USD	SGD	Others	Total
Cash and Bank Deposits	103.3	122.9	7.7	36.7	270.6
Percentage of Total Amount	38.2%	45.4%	2.8%	13.6%	100.0%

The Group maintained currencies other than the Hong Kong dollar and United States dollar as at the balance sheet date to meet the business needs in different regions.

Banking facilities and borrowings

At 30 June 2012, the Group had available banking facilities of approximately HK$136.8 million. A total of HK$100 million was drawn as uncommitted revolving loans which were unsecured and bore interest at prevailing market rates and approximately HK$12.9 million was utilised as guarantees for the Group's procurement of services from telecoms operators, performance to customers and rental deposits.

Around HK$6.8 million of these facilities was required to be secured by pledged deposits.

Securities and guarantees

At 30 June 2012, the Group pledged approximately HK$3.7 million of deposits to secure its banking facilities. The Group had not created any other security over its assets nor had it provided any corporate guarantee.

Capital commitments

At 30 June 2012, the Group had outstanding capital commitments of HK$79.2 million, mainly for the acquisition of telecommunications equipment which had yet to be delivered to the Group and fitting out costs of the new data centre. Of these commitments, HK$71.0 million were outstanding contractual capital commitments and HK$8.2 million were capital commitments authorised but for which contracts had yet to be entered into.

Other commitments

On 2 September 2010, the Group entered into a framework agreement (the "Framework Agreement") with CITIC Group Corporation, CE-SCM Network Technology Co., Ltd. ("CE-SCM"), Information Centre of State-owned Assets Supervision & Administration Commission of the State Council ("SASAC") and CEC, pursuant to which the Group, through CITIC Telecom International CPC Limited ("CPC"), a wholly-owned subsidiary of the Company, will, upon satisfaction of certain conditions set out therein, acquire:

(i) 40.77% equity interest in CEC from CE-SCM;

(ii) 8.23% equity interest in CEC from CITIC Group Corporation together with a purchase right (the "Purchase Right") to acquire the remaining 45.09% equity interest in CEC held by CITIC Group Corporation, in which the Purchase Right shall be exercisable by CPC when CPC is permitted to hold more equity interest in CEC under the then prevailing PRC laws and regulations; and

(iii) all the issued shares of China Enterprise Netcom Corporation Limited ("CEC-HK") held by China Enterprise Communications Technology (Holding) Limited ("CEC-HK Holding"), a wholly-owned subsidiary of CEC.

The aggregate consideration payable by the Group is approximately HK$283.7 million comprising:

(i) Renminbi ("RMB") 93.3 million (approximately HK$113.9 million) payable to CE-SCM by instalments;

(ii) RMB80.8 million (approximately HK$98.6 million) payable to CITIC Group Corporation at completion, out of which RMB62.0 million (approximately HK$75.7 million) is to be paid as advance payment for the acquisition of the remaining 45.09% equity interest in CEC held by CITIC Group Corporation upon CPC exercising the Purchase Right;

(iii) HK$0.4 million as consideration for the entire equity interest in CEC-HK; and

(iv) the assumption of debts in amount of United States dollar 9.1 million (approximately HK$70.8 million) owed by CEC-HK to a subsidiary of CITIC Group Corporation.

Details of the Framework Agreement are set out in the Company's circular to shareholders dated 22 October 2010.

On 29 July 2011, the Group completed the acquisition of CEC-HK pursuant to the Framework Agreement. At 30 June 2012, included in non-current other receivables and deposits was an amount HK$53.6 million (31 December 2011: HK$Nil), being a deposit paid for the acquisition of subsidiaries and included in other payables was HK$48.2 million (31 December 2011: HK$48.2 million), being the unpaid portion of the acquisition cost in CEC-HK. The Group has a remaining sum of approximately RMB75.2 million (approximately HK$91.8 million), being the unpaid portion of the aggregate consideration, which shall be payable at completion after the Framework Agreement becoming unconditional.

FORWARD LOOKING STATEMENTS

The Interim Report contains certain forward looking statements with respect to the financial condition, results of operations and business of the Group. These forward looking statements represent the Company's expectations or beliefs concerning future events and involve known and unknown risks and uncertainty that could cause actual results, performance or events to differ materially from those expressed or implied in such statements.

Forward looking statements involve inherent risks and uncertainties. Readers should be cautioned that a number of factors could cause actual results to differ, in some instances materially, from those anticipated or implied in any forward looking statement.