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CORPORATE BROCHURE



Networking Hong Kong

On 18 March 2010, NiQ Lai and his colleagues celebrated 10 years on NASDAQ by ringing the opening bell: he tells John O'Hanlon how after 10 years of investing, City Telecom is now in harvesting mode, being profitable, with positive free cash flow and achieving its goal to dominate the Hong Kong broadband market

A business that sets out to crush its competitors and which annually terminates the lowest-performing five per cent of its workforce could look ruthless. Single minded would be a better description, though. In the 1990s founder Ricky Wong chucked a stone into a local telecoms market dominated by former monopoly incumbent Hong Kong Telecom (now known as PCCW) by leveraging callback opportunities to undercut the competition on international calling. With the cost of outward calls from Hong Kong being higher than inbound calls, reversing the direction of the call created value for the subscriber and made City Telecom a lot of money over the next decade and a half.

Taking a 10-year view and investing in its people are two things that distinguish this company, says NiQ Lai, City Telecom's CFO and head of Talent Engagement. "We have a very distinct way of doing business and we stick to our guns: through good and bad times we don't falter." The callback opportunity drove deregulation in Hong Kong and long-distance calling quickly became a commodity, but the battle moved on as data became more important than chat, and bandwidth the Holy Grail. Downloading high definition video or large data files requires fibre optic, so City Telecom started laying down its own network in Hong Kong in the early 2000s, a seriously capital-intensive venture.

Lai had joined the company in 2004 at a fraction of the salary he was earning as director and head of Asia Telecom Research at Credit Suisse First Boston. However, after over a decade of researching telecom companies, he knew the business well enough to believe it was worth selling his home to give him the capital to buy a share of the equity. Two years later he stepped into his present role as CFO and head of Talent Engagement. The same year City Telecom set its 10-year BHAG, or big hairy audacious goal, to become the city's largest internet protocol (IP) provider by 2016.

In 2007, after seven years in the red, the company became cash-flow positive. Today, it is now free of debt, profitable, with positive free cash flow, over US\$50 million in the bank, and positioned to take advantage of the exponential growth of internet traffic driven by online video, gaming, learning, cloud computing and the like. "We are proud to be the provider of the fattest, dumbest pipes in town to the households and then charge a monopoly rent on them," says Lai. "We are not a sexy technology or content business. We roll up our sleeves, dig up the roads, lay fibre down, and we have been doing this for 10 years now."

None of this was as obvious in 2000 as it is today. "We started 10 years ago, just after the technology bubble burst when the industry was not ready and people did not believe in fibre. In fact, as we started just after the technology crash, our competitors were looking to cut capital expenditure rather than invest. But we continued to chug away for the first seven years losing money!"

Lai admits, "Most companies would have sacked their CEO long before that! But our founders own the majority of our company, which helps them to keep their jobs during the investment period and allows them to invest according to their vision rather than short term market pressures." City Telecom built the biggest network in town by stealth, putting it in an unassailable position because what it was doing was counter intuitive.

The technology is very routine and 'off-the-shelf', but deployed differently, Lai explains. Standard enterprise routers from Cisco Systems created a LAN (local area network) like that found in any large office, but City Telecom deployed this on a much more massive scale to 1.75 million homes.



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Telecoms incumbents instinctively avoid commoditisation of bandwidth, he says, preferring to add value by developing sexy content and other applications. City Telecom takes the diametrically opposite view. "A commodity business is a great place to be if you are the lowest cost provider. We want to collapse bandwidth pricing and commoditise it to unbelievably low prices whereby 1,000 Mbps becomes the industry norm for the mass residential market. We did this with callback in the 1990s and made lot of money doing it; we want to do it again with fibre. The rest of the industry can't understand how we run this company. We are paranoid about change, which is why we are constantly changing."

It would be very difficult to start this fibre upgrade process again today for another new entrant, so there's not much the competition can do to catch up with City Telecom now. "We are the only fixed line new entrant in the world that we know of, with a specific timeframe to overtake the incumbent network," he says. "Our competitors are responding with short term measures, so they copy our prices but they can't match our bandwidth. Even if our competitors start to build a similar fibre network now by copying our model, it would still take them a few years to match our coverage, by which time our position will be firmly established."

It's unusual for a CFO to double as HR director but for Lai, it is a role that comes naturally from the company's approach to 'Talent'—a word that

is used in preference to 'employee'. So firing the bottom five per cent is less a Draconian measure as an admission that no company can expect to get its hiring 100 per cent right. And no company takes more trouble to get it right. "We are taking the McDonald's Happy Meal approach to Talent acquisition. Get them when they are young!"

Hong Kong university student Ray Chau, a 2010 intern, was amazed to be taken by Lai to meetings with high powered equity analysts. "Talk flat," Lai told him, "and think about ways that you can add value to them." Chau says he will never forget the experience.

If he joins City Telecom after graduating Chau may find himself on the aggressive 'CXO' management trainee programme. The X can be substituted by any letter, e.g. CEO, CFO, CTO (Chief Talent Officer) etc as participants are expected to aim for the board. "There are two ways I can find my own replacement—when the time comes in 15 to 20 years time, I could hire a head hunter to search for my replacement; or I can try to groom someone today. I much prefer the latter option."

People who have survived the CXO 18 month programme are Talents indeed. They are stretched intellectually and physically, expected to read a management book a month, run a half marathon and crucially pass Level 1 of the Chartered Financial Analyst exams. "CFA is extremely tough to get through but it gives them the ability to talk the common language of business, and I think that is vital for a future CXO."

While other operators outsource everything they can, he says, "we are very parental to the extent of being paranoid about owning our customer contact points. Our management structure is set up to be customer-friendly. We have broken Hong Kong up into five manageable regions each run by a mini-CEO." Unlike a traditional corporation with its operational departmental structure, the buck stops with that mini-CEO if anything goes right or wrong in her region.

To reach its 10-year big hairy audacious goal of becoming the largest IP service provider in Hong Kong by 2016, City Telecom will need to woo 75,000 customers a year for 10 years from competing networks; in FY2010 it added 132,000! It's a stretch goal, but City Telecom's investment in Talent will see it through that and its next goal to provide 'Free TV via Fibre', Lai believes. "Disrupting the landscape is something that's in our corporate DNA." <http://www.ctigroup.com.hk/ctigroup/eng/global/home.htm> ●

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