

MANAGEMENT DISCUSSION AND ANALYSIS

Business Review

City e-Solutions Limited (“CES”) made good progress in its effort to be a solutions provider for the hospitality industry through its 85% owned subsidiary SWAN Holdings Limited (“SWAN”).

Over the first six months of 2001, SWAN has continued to execute on its vision of being a premier global hospitality solutions provider. It has put in place a strong management team and is earning positive recognition in the US hospitality industry.

SWAN has developed distinct identities for its five business units (Richfield Hospitality, Sceptre, Source, Shield and Solve) and has been marketing itself aggressively to the industry through trade shows and targeted advertising. The regional sales teams are now fully operative in the field, after careful hiring and extensive training. Consequently, the sales pipeline should be enhanced in the second half of the year.

The Hospitality industry has been impacted negatively by the downturn in the US economy. While SWAN’s reservation and management fees have been affected by the drop in the business volumes of existing hotels using its services, the interest level in SWAN’s solution has risen because of the difficult environment.

A key component of SWAN’s plans is to leverage the latest technology to enable customers to maximize the potential of their hotels’ performance. In April, SWAN’s reservation unit, Sceptre transitioned 100 of its hotels to a new state-of-the-art technology platform.

In Asia, CES continues to make progress in sourcing high-quality manufacturers in low-cost producing countries to provide goods to SWAN’s hospitality clients.

Financial Commentary

Group Performance

CES Group recorded a turnover of HK\$54.3million. For the period under review, Group turnover comprises interest income of HK\$13.3 million and revenue contribution of HK\$41 million from SWAN’s business units. Following the Group restructuring during the last financial year, comparison between the results under review to those of the previous corresponding period will not be meaningful.

SWAN Group reported a loss of HK\$4.6 million for the first six months of 2001 due to start-up costs incurred relating to the development of its core business units and the recruitment of key members of the management team. Included under other net expenses, HK\$26.3 million is principally attributed to unrealised exchange loss from foreign currency bank deposits denominated in Sterling Pound which were received in the year 1999 from the disposal of its interest in subsidiaries and dividends. Disregarding this unrealised exchange loss, the Group achieved close to a breakeven results for its first full half year performance.

Consequently, for the six months ended 30 June 2001, the Group reported a loss of HK\$26.5 million attributable to its shareholders.

Financial Position

As at 30 June 2001, the Group's gross assets stood at HK\$627.6 million down from HK\$670 million as at the end of the last financial year ended 31 December 2000. The main decrease was in the Group's cash and cash equivalents which was reduced to HK\$482.1 million from HK\$561.7 million.

Cash Flow and Borrowings

For the period under review, cash outflow from operating activities amounted to HK\$71.7 million. The main non-operational cash outflow related to the final dividend payment in respect of the last financial year ended 31 December 2000 and capital expenditure of HK\$7.7 million and HK\$3.3 million respectively. SWAN Group also paid HK\$10.5 million to an affiliated company being amount owed in respect of hospitality related transactions carried out in the last financial year ended 31 December 2000. On the return of investments, the Group received interest income of HK\$13.8 million during the period under review. The Group's cash and cash equivalents accordingly decreased by HK\$79.9 million for the period under review.

The Group has no borrowings for the financial period ended 30 June 2001.

Treasury Activities

The Group's major foreign currency exposure continues to be the Sterling Pound deposits received previously from the disposal of its interest in subsidiaries and dividends. The most substantial part of the Group's cash deposit continues to be in Sterling Pound, with the remaining balance largely in US dollar. With respect to the US dollar deposits, as long as the Hong Kong dollar trades within the existing US dollar peg arrangement, currency flows will be minimal. The Group takes a medium to long term view on the Sterling Pound and Hong Kong dollars exchange rate risk and enters into currency swap where appropriate to reduce its foreign exchange exposure.

Employees

As at 30 June 2001, the Group had 81 employees on its payroll and the total payroll costs for the six months was HK\$23.6 million.

Prospects

While the economic environment, globally, and particularly in the US, continues to be challenging, there is substantial hospitality market share upside for SWAN. The uncertain environment is dictating longer sales cycles but we believe that the strong solution offered by SWAN will be compelling to the small and mid-size chains and independent hotels.

Although initial losses are inevitable in building a business, we continue to be prudent with cost containment and at the same time remain acutely aware of the need to achieve profitability.

Notwithstanding the difficult economic environment, SWAN is poised to make substantial progress as a global hospitality solutions provider.