

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

INTRODUCTION

For the first half of 2001, the Group achieved a pre-tax profit of RMB212.5 million, representing an increase of 28.1% over the first half of 2000. Earnings before interest, tax, depreciation and amortisation (EBITDA) were RMB239.9 million, representing an increase of 12.6% over the first half of 2000. Net profit was RMB208.9 million, which represents an increase of 89.6% over the first half of 2000. The growth in profit was mainly attributable to the increase in the Group's business volume and the income tax preferential treatment.

The turnover and results of the Group mainly derive from its operations in China. The earnings per share of the Group were RMB0.25 for the first half of 2001.

TOTAL REVENUES

The total revenues of the Group in the first half of 2001 rose by RMB66.7 million, or 19.8%, to RMB403.1 million from RMB336.4 million in the first half of 2000. The increase in total revenues was mainly attributable to the growth in the Group's business. The reasons for the increase in total revenues are as follows:

- ETD revenues represented 56.3% of the Group's total revenues in the first half of 2001 as compared to 60.4% in the first half of 2000. ETD revenues increased by 11.8% to RMB227.1 million in the first half of 2001 from RMB203.1 million in the first half of 2000. The increase was principally attributable to various reasons including an increase in the usage of the Company's ETD services by Chinese commercial airlines due to the growth in the Chinese economy and Chinese air travel and tourism industries; an increase in the usage of the Company's ETD services by foreign and regional airlines; as well as an increase in the Company's ETD services charges applicable to both foreign and regional airlines.
- APP revenues accounted for 21.8% of the Group's total revenues in the first half of 2001 as compared to 21.0% in the first half of 2000. APP revenues increased by 24.3% to RMB87.8 million in the first half of 2001 from RMB70.6 million in the first half of 2000. The increase was mainly attributable to both the installation of APP front-end systems in six domestic airports in the first half of 2001 and the increase in the usage of APP services by the Group's existing customers.
- Data network revenues accounted for 15.4% of the Group's total revenues in the first half of 2001 as compared to 15.6% in the first half of 2000. Data network revenues increased by 18.2% to RMB62.1 million in the first half 2001 from RMB52.5 million in the first half of 2000. The increase was attributable to an increase in the business volume of the Group in 2001 as a result of the promotion of BSP in 2000 and the expansion of the Group's business by the newly-established LDCs.
- Equipment sales and other revenues increased by 157.3% to RMB26.2 million in the

first half of 2001 from RMB10.2 million in the first half of 2000. The increase was mainly attributable to the transfer, by the SITA subsidiary to the Group, of the agreed cargo contract revenues from Air China and China Eastern Airlines Corporation Limited in 2001, and an increase in revenues from APP contracts, as well as revenues from the Group's Internet-based travel platform services.

NET REVENUES

Net revenues increased by 19.7% to RMB389.4 million in the first half of 2001 from RMB325.2 million in the first half of 2000.

OPERATING EXPENSES

Total operating expenses increased by RMB34.6 million, or 21.5%, to RMB195.3 million in the first half of 2001 from RMB160.7 million in the first half of 2000. The percentage increase in total operating expenses was more than the 19.8% increase in total revenues due to the establishment and development of its new-generation ETD system by the Group, and an increase in business activities in support of the Group's business development. The reasons for the increase in operating expenses are as follows:

- Depreciation decreased by 7.1% primarily due to the fact that a mainframe computer had been fully depreciated at the end of 2000;
- Total cost of network usage increased by 40.3% due to increased volume of network usage in support of the Group's growing ETD and APP businesses;
- Personnel expenses increased by 43.8% due to an increase in the number of staff for the Group's business development as well as an increase in staff salaries;
- Operating lease rentals increased by 63.3% due to additional area rented by the Company's headquarters for business expansion;
- Cost of technical support services increased by 24.3% due to additional technical support expenses associated with the development of the Group's new generation ETD system;
- Repair and maintenance costs for the first half of 2001 increased by 25.5% due to the signing of a new network equipment maintenance contract with CISCO at the end of 2000;
- Commission and promotion expenses increased by 20.7% due to the growth in new APP customers and the success of the Group's APP promotional programmes; and
- Other operating expenses increased by 12.6% due to increased expenses following the initial public offer of the Company's H shares in the first half of 2001.

As a result of the above changes in net revenues and operating expenses, the operating profit of the Group increased by RMB29.6 million, or 18.0%, to RMB194.1 million in the first

half of 2001 from RMB164.5 million in the first half of 2000.

NET FINANCIAL INCOME

Net financial income in the first half of 2001 amounted to RMB18.0 million as compared to RMB1.2 million in the first half of 2000. The increase was mainly attributable to the substantial increase in interest income accrued from the deposit of the proceeds from the initial public offering of the Company's H shares in the first half of 2001.

TAXATION

Taxation decreased by 96.1% to RMB2.1 million in the first half of 2001 from RMB54.6 million in the first half of 2000 since the Company was subject to income tax at a rate of 33% in the first half of 2000 and was entitled to exemption from enterprise income tax in the first half of 2001.

NET PROFIT

As a result of the above factors, the Group's net profit increased by RMB98.7 million, or 89.6%, to RMB208.9 million in the first half of 2001 from RMB110.2 million in the first half of 2000.

LIQUIDITY AND CAPITAL STRUCTURE

For details of the cash flows of the Group for the first half of 2001, please refer to the unaudited condensed consolidated statement of cash flows and the explanatory notes attached thereto.

In the first half of 2001, the Group derived its working capital mainly from operating activities and financing activities. Net cash inflow from operating activities amounted to RMB173.5 million. Cash inflow from financing activities was attributable to the net proceeds generated from the initial public offering of the Company's H shares in February 2001.

During the first half of 2001, the Group had no outstanding short-term or long-term bank loans.

As at June 30, 2001, the cash and cash equivalents of the Group amounted to RMB656.9 million, of which 96.8% was denominated in Renminbi, 2.8% in US dollars and 0.4% in Hong Kong dollars.

CAPITAL EXPENDITURES

The total capital expenditures of the Group increased by a substantial amount of RMB169.8 million from RMB40.1 million in the first half of 2000 to RMB209.9 million in the first half of 2001.

The total capital expenditures of the Group in the first half of 2001 mainly comprised of the

purchase of hardwares, softwares and equipment under the Group's ETD business strategy, and the softwares required for ACS.

The total capital expenditures of the Group for the year 2001 are estimated to be approximately RMB335.5 million, principally to be used for the development and gradual promotion of the new-generation ETD products and services, and the development of APP, ACS and other new businesses.

The capital expenditure programme will be funded by the net proceeds from the Company's initial public offering and internal cash flow from operating activities.

The Directors expect that the capital resources of the Group in 2001 will be able to fully cover the capital required for the capital expenditure programme and daily operations.

FOREIGN EXCHANGE RISK

The Group is exposed to foreign exchange risk related to its capital expenditures given the fact that a substantial portion of its capital expenditures is paid in US dollars for imported equipment. Under the current foreign exchange system in the PRC, apart from foreign currencies in the form of cash and bank deposit which can be hedged against part of the foreign exchange risks, the Group is not able to fully hedge against its currency risks.

EMPLOYEES

As at June 30, 2001, the total number of employees of the Group was 743. Personnel expenses amounted to RMB27.7 million for the first half of 2001, representing 14.2% of the total operating expenses of the Group in the first half of 2001.

The remuneration package of the Group's employees includes salary, bonus and other benefits. In situations where the relevant laws and regulations in the PRC permit the Group to do so, the Group offers salaries of different levels to different employees based on factors which include their performance, qualifications and duties.

In the first half of 2001, the Group continued to provide its employees with learning opportunities in the areas of air travel and tourism, computer technology and business management, as well as the latest developments in the areas of computer technology, law and economy.