

## Management's Discussion and Analysis of Financial Condition and Results of Operations

### Summary

For the first half of 2002, the Group achieved a profit before tax of RMB235.5 million, representing an increase of 10.9 per cent. over the first half of 2001. Earnings before interest, tax, depreciation and amortisation (EBITDA) amounted to RMB278.3 million, representing an increase of 16.0 per cent. over the first half of 2001. Net profit was RMB237.5 million, which represents an increase of 13.7 per cent. over the first half of 2001. The growth in profit was mainly attributable to the increase in the Group's business volume.

The turnover and results of the Group were mainly derived from its operations in China. The earnings per share of the Group was RMB0.27 for the first half of 2002.

### Total Revenues

The total revenues of the Group in the first half of 2002 rose by RMB71.7 million, or 17.8 per cent., to RMB474.8 million from RMB403.1 million in the first half of 2001. 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 54.2 per cent. of the Group's total revenues in the first half of 2002 as compared to 56.3 per cent. in the first half of 2001. ETD revenues increased by 13.3 per cent. to RMB257.3 million in the first half of 2002 from RMB227.1 million in the first half of 2001. The increase was principally attributable to an increase in the usage of the Company's ETD services by Chinese commercial airlines due to the growth in both the Chinese economy and air travel and tourism industries and an increase in the usage of the Company's ETD services by foreign and regional airlines.
- APP revenues accounted for 24.0 per cent. of the Group's total revenues in the first half of 2002 as compared to 21.8 per cent. in the first half of 2001. APP revenues increased by 30.0 per cent. to RMB114.1 million in the first half of 2002 from RMB87.8 million in the first half of 2001. The increase was mainly attributable to both the installation of APP front-end systems at seven domestic airports in the first half of 2002 and the increase in the usage of APP services by the Group's existing customers.

- Data network revenues accounted for 17.4 per cent. of the Group's total revenues in the first half of 2002 as compared to 15.4 per cent. in the first half of 2001. Data network revenues increased by 32.7 per cent. to RMB82.4 million in the first half of 2002 from RMB62.1 million in the first half of 2001. The increase was attributable to a significant increase in the revenues of LDCs in 2002, which arose as a result of increased marketing and promotion and the commencement of operation of new LDCs during the second half of 2001 and the first half of 2002.
- Equipment sales and other revenues decreased by 20.2 per cent. from RMB26.2 million in the first half of 2001 to RMB20.9 million in the first half of 2002. The decrease was mainly attributable to a decrease in equipment sales due to a fall in the total contracted amount of APP front-end construction contracts.

## Net Revenues

Net revenues increased by 17.9 per cent. to RMB459.3 million in the first half of 2002 from RMB389.4 million in the first half of 2001.

## Operating Expenses

Total operating expenses increased by RMB60.1 million, or 30.8 per cent., to RMB255.4 million in the first half of 2002 from RMB195.3 million in the first half of 2001. The reasons for the increase in operating expenses are as follows:

- depreciation and amortisation increased by 50.3 per cent. primarily due to the fact that depreciation and amortisation expenses have been provided for in relation to the capital expenditures incurred for the hardware and software during the second half of 2001, although the provisions for such depreciation and amortisation expenses were not made for the whole six months of the first half of 2001.
- personnel expenses increased by 66.2 per cent., primarily due to an increase in the number of employees in order to support the development of the Group's businesses and the increase in personnel expenses due to the commencement of the new LDCs;
- technological support costs decreased by 65.0 per cent. due to the postponement of part of the proposed capital expenditures projected for the first half of 2002;

- commission and promotion expenses increased by 54.9 per cent. due to the growth in new APP customers and the success of the Group's APP promotional programmes; and
- other operating expenses increased by 100.8 per cent. due to an increase in expenses following increased marketing activities by LDCs in the first half of 2002 despite a significant increase in revenue at the same time.

As a result of the above changes in net revenues and operating expenses, the operating profit of the Group increased by RMB9.9 million, or 5.1 per cent., to RMB204.0 million in the first half of 2002 from RMB194.1 million in the first half of 2001.

### **Net Financial Income**

Net financial income in the first half of 2002 amounted to RMB25.5 million as compared to RMB17.9 million in the first half of 2001. The increase was mainly attributable to an increase in interest income derived from enhanced capital management by the Company during the first half of 2002.

### **Minority Interests**

Minority interests changed from a net gain of RMB1.4 million in the first half of 2001 to a net loss of RMB3.2 million in the first half of 2002, mainly due to an increase in losses recorded by one of the Company's subsidiaries, InfoSky.

### **Net Profit**

As a result of the above factors, the Group's net profit increased by RMB28.6 million, or 13.7 per cent., from RMB208.9 million in the first half of 2001 to RMB237.5 million in the first half of 2002.

### **Liquidity and Capital Structure**

For details of the cash flows of the Group for the first half of 2002, please refer to the unaudited condensed consolidated statement of cash flows and the explanatory notes attached thereto.

In the first half of 2002, the Group derived its working capital mainly from operating activities. Net cash inflow from operating activities amounted to RMB226.1 million.

During the first half of 2002, the Group had no short-term or long-term bank loans.

As at June 30, 2002, the cash and cash equivalents of the Group amounted to RMB1,843.4 million, of which 58.4 per cent. was denominated in Renminbi, 17.5 per cent. was denominated in US dollars and 24.1 per cent. was denominated in Hong Kong dollars.

### **Capital Expenditures**

The total capital expenditures of the Group decreased by a substantial amount of RMB181.5 million from RMB209.9 million in the first half of 2001 to RMB28.4 million in the first half of 2002.

The capital expenditures of the Group in the first half of 2002 mainly comprised the purchase of hardware, software and equipment under the Group's ETD business strategy.

The total capital expenditures of the Group for the year 2002 is estimated to be approximately RMB205.6 million, which will be used principally for the development and gradual promotion of the new-generation ETD products and services, the development of APP/ACS products and services and the development of other new businesses.

The capital expenditure programmes will be funded by the remaining balance of proceeds from the Company's initial public offering of H shares and internal cash flow from operating activities.

The Board anticipates that the source of capital of the Group in 2002 will be able to fully cover the amount required for its capital expenditure programmes 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.

## **Gearing ratio**

As at June 30, 2002, the gearing ratio the Group was 15.6 per cent. (June 30, 2001: 15.8 per cent.). This ratio is calculated from the sum of liabilities and minority interest of the Group divided by the total assets of the Group as at June 30, 2002.

## **Contingent liabilities**

As at June 30, 2002, the Group had no material contingent liabilities.

## **Employees**

As at June 30, 2002, the total number of employees of the Group was 1,021. Personnel expenses amounted to RMB46.1 million for the first half of 2002, representing 18.1 per cent. of the total operating expenses of the Group in the first half of 2002.

The remuneration package of the Group's employees includes salary, bonus and other benefits. 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 2002, 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 information technology, law and corporate governance.