

Management's Discussion and Analysis



*Telford Plaza
Branch of CTSHK*

Business Review

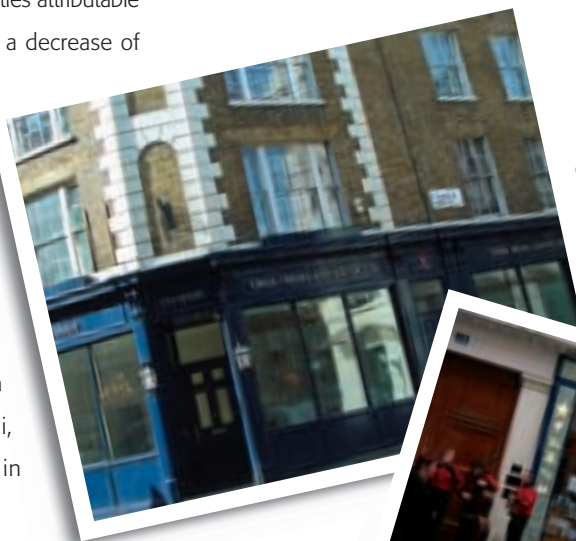
The audited net loss attributable to shareholders of the Group for the year ended 31 December 2003 was HK\$39.81 million. The loss was mainly due to the outbreak of Severe Acute Respiratory Syndrome ("SARS"), decrease of operating profit, impairment of properties and goodwill. Apart from the above impairment of properties and goodwill which amounted to HK\$387 million, the net profit from ordinary activities attributable to shareholders was HK\$347 million, which is a decrease of 37% as compared with last year.

During the outbreak of SARS, besides undertaking a number of cost control measures, the Group has leveraged on this opportunity to expand its travel network in the Mainland and overseas. So far, the Group has established joint ventures of travel agency in four major tourism cities including Shanghai, Shandong, Xiamen and Xian, a call center in

Guangzhou, a wholly owned travel agency in a major country in the Northern Europe – Sweden, and branches in the airport of both Osaka in Japan and Frankfurt in Germany. The Group's travel network in Hong Kong, Mainland and overseas has come into shape which has laid a solid foundation for the future development of the business. In addition, leveraging on the opportunity arose from the "24-hour Passenger Clearance Service", the Group has commenced the operation of overnight coach across the boundary and has achieved satisfactory result. The Group's major project, Zhuhai Ocean Spring Resort has also achieved some progress. The amount of the extractable hot spring reserve is found to be twice the amount of the expected usage. The successful issuance of the US\$150 million convertible bond by the Group has provided sufficient fund for the development of the Phase I of the project.

Tour Operation and Leisure Business

Due to impact of SARS, the turnover of travel and leisure business dropped by 25.1% as compared with last year.



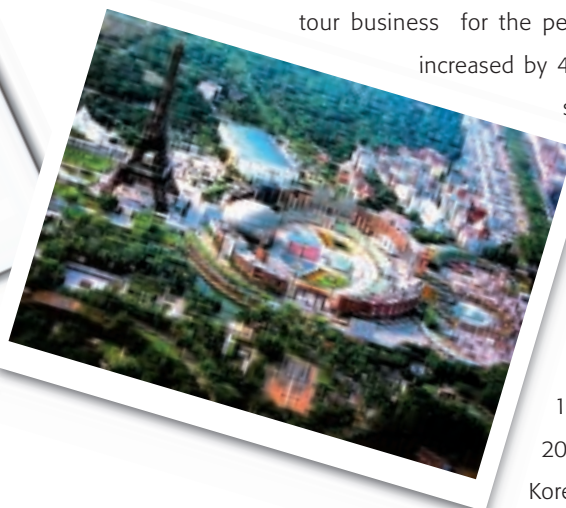
*Office of CTS
(U.K.) and CTS
(France)*



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Theme Parks



During the year, the number of tourists received by China Travel Service (Hong Kong) Limited ("CTSHK") decreased by 21.7% as compared with last year. The business of hotel room reservation and transportation ticket-booking fell by 24.3% and 9.3% respectively. During the SARS period, CTSHK focused on developing Macau and local Hong Kong tours, and after the SARS, it participated in the "We Love Hong Kong" campaign as solicited by the Tourism Coalition of Hong Kong. In the second half year, the number of outbound tours to China increased by 1.36 times when compared with the first half year, resulting in an overall decrease in the number of outbound tours to China by 14% only; and the outbound tours to overseas had increased by 94.2% when compared with the first half year. Meanwhile, driven by the demand on hotel rooms from individual visitors from Mainland, CTSHK had put more effort on booking and leasing of hotel rooms in Hong Kong, and consequently the business of hotel room reservation had improved by 64.8% as compared to first half year. The above measures had, to a certain extent, reduced the losses brought by SARS.

The Group's wholly-owned travel agency in Beijing, China Travel International Limited ("CTI") suffered from the SARS impact in the first half of the year. Since August 2003, business has been restored and the inbound and outbound tour business for the period from August to December increased by 49% and 147% as compared to same period last year. CTI received

183,000 tourists, which is an increase of 716.7% as compared with last year. After two years of business consolidation and restructuring, CTI ranked 38th among the "Top 100 Travel Agents in China" in 2002. After the World Cup in South Korea and Japan, CTI has also been appointed as the sole agent for

organizing tour and providing ticketing services for the Chinese citizens to the 2004 Athens Olympics, which has laid a solid foundation for 2004's business.

Impacted by SARS and the policy of "Individual Traveler Permit Scheme", the business of organizing Chinese citizens on Hong Kong & Macau tours shrank significantly. The total number of tourists received during the year was about 132,000, represented a decrease of 26.4% as compared with last year. In the second half year, China Travel (HK & Macau Tour) Management Hong Kong Limited refocused on business and exhibition travel by capitalizing on its competitive advantages on the quality of services and brand name, resulting in the turnaround from losses incurred in the first half year.

China Travel Net Hong Kong Limited has recorded a monthly average of 145,000 website visitors, which is an increase of 6.3% as compared with last year. It has also joined an international business travel organization, Synergi, Inc. and has won a tender for the business travel of the multinational companies.

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The three theme parks, Window of the World, Splendid China and China Folk Culture Villages attracted approximately 2.8 million visitors in total, which is a decrease of 32.1% as compared with last year; among them, the number of visitors of the Window of the World decreased by 24.9% and the number of visitors of the Splendid China and China Folk Culture Villages decreased by 42.9%. In order to reduce the impact of SARS in the first half year, Window of the World had launched a number of new programs such as "Deep Earth Adventure", "Lost City", and "Explore the Pyramids" etc., which are hot spots to the tourists. On the other hand, Splendid China and China Folk Culture Villages has organized some night shows such as "Minorities Music Night", renovated central theatre and re-packaged the famous show, "Horse Fighting". The shows in the three theme parks were very successful and earned the applause of both local and overseas tourists.

Shenzhen Tycoon Golf Club had successfully completed the rebuild of the C Course and has installed lighting facilities in November 2003. There is a substantial growth in the membership sales and the number of golfers. The construction of "Home for Member", which will provide accommodation and conference facilities, will be completed by the end of 2004. It is expected to further enhance the attractiveness of the Club.



Rotunda in Hotel Grandeur

Hotel Operation

The average occupancy rate of the Group's four hotels in Hong Kong was 70.1%, representing a decrease of 20.4% as compared with last year; and the average room rate has increased by 1.5%. Both the room rate and occupancy rate had significantly improved since August 2003. Because the impact of SARS on the business of Hotel Grandeur in Macau was relatively less significant, together with tight cost control measures, the average room rate increased by 13.8%. The operating result was satisfactory.



Rebuild of the C Course of Shenzhen Tycoon Golf Club

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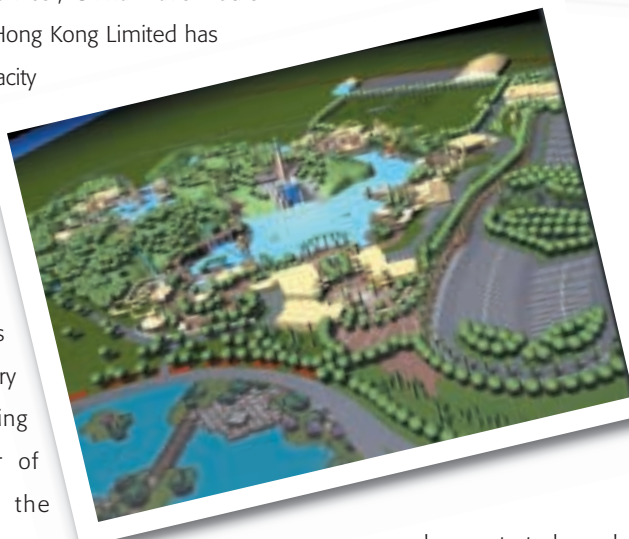
Transportation

The turnover of China Travel Tours Transportation Services Hong Kong Limited and China Travel Express Limited increased by 10% as compared with last year, while the number of passengers increased by 182.5% to 2.428 million. Leveraging on the opportunity arising from the introduction of the "Individual Traveler Permit Scheme" and "24-hour Passenger Clearance Service", China Travel Tours Transportation Services Hong Kong Limited has expanded its loading capacity and sources of customers. In addition to recovering losses in the first half year, the overall profit increased by 12.1%. It is the leader in the industry in terms of both loading capacity and number of passengers. Due to the outbreak of SARS and the cost incurred for the new routes, operating result of the joint venture, Shun Tak-China Travel Shipping Investments Limited decreased as compared with last year.

The import and re-export freight volume through railway handled by China Travel Service (Cargo) Hong Kong Limited continually deteriorated and decreased by 13.2% and 11.8% respectively. On the other hand, the business of CTS International Transportation Company Limited in Shanghai had



Elevation of the Conference Hotel of Zhubai Hot Spring Resort



3D Computer Model of the Theme Park of Zhubai Hot Spring Resort

demonstrated a relatively better growth as the turnover increased by 85%. When compared with last year, the sea freight volume ranked among the top three in Shanghai.

Infrastructure

The economic and technical benchmark measures of Weihe Power Plant have achieved the top in its history and broke the record of 500 days of safety production. The annual volume of on-grid electricity increased by 6.5% as compared with last year.

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Number and Remuneration of Employee

As at 31 December 2003, the Group has approximately 6,694 employees.

The employees are remunerated based on their work performance, professional experience and prevailing industry practices. The remuneration policy and package of the Group's employees are periodically reviewed by the management. Apart from pension funds and in-house training programs, discretionary bonuses and share options are awarded to certain employees according to the assessment of individual performance.

Liquidity, Financial Resources and Capital Structure

The financial position of the Group is strong. As at 31 December 2003, the cash and bank balances of the Group amounted to HK\$2,344 million whereas the interest bearing debts from the bank and the convertible bonds amounted to HK\$1,177 million and HK\$1,168 million respectively. The interest bearing debt to equity ratio was 32.4%.

During the year, 9,466,636 bonus warrants were exercised for 9,466,636 shares of HK\$0.10 each at the subscription price of HK\$1.22 per share. Accordingly, the number of issued share capital of the Company has been increased from 4,222,731,839 shares to 4,232,198,475 shares as at 31 December 2003.

Future Prospects

Amid the economic recovery in Hong Kong and the rest of the world, the consumption power of tourists will increase. With the further extension of the "Individual Traveler Permit Scheme" to cover more Mainland regions, it is forecasted that the number of travelers to Hong Kong will exceed 20 million in 2004. Together with the opening up of European countries participating in the Schengen Agreement to Mainland travelers, the Group will be able to capture unlimited business opportunities.

The established direction of the Group is to strengthen and develop core travel businesses. The important sources of customers of the Group include outbound travelers of Mainland citizens and inbound travelers to Hong Kong. The competitive advantage of the Group is the complement of its passenger transportation business, hotels, theme parks, golf club and domestic and overseas travel networks. Through consolidating travel resources, centralizing purchasing, and coordinating sales and marketing activities, the costs of the Group will be reduced and the market share and competitiveness of the Group will be enhanced.



Entry View of Theme Park of
Zhuhai Hot Spring Resort

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The financial position of the Group is strong with abundant funds, which provides supports to the continuous development of new travel and leisure projects. Besides closely monitoring the development of the Zhuhai Ocean Spring Resort, the Group will carry out feasibility studies of natural attractions, acquire quality travel-related assets, and strengthen the construction of online travel platform, so as to enhance the core travel business of the Group.

To cope with the demand of individual visitors from Mainland and local tourists, the Group will strengthen its cross-border passenger transportation services between Hong Kong and the Mainland by increasing loading capacity and exploring new routes.

The Group will further develop its freight forwarding business centralized in Shanghai, an air freight godown located at Pudong International Airport was completed and started operation by the end of 2003. It has strengthened and improved the air freight handling power, thereby it will further reduce the operation cost. Amid the development of freight network infrastructure, freight transportation business will have substantial growth.

Development of Online Travel Company

Because of the rapid development of the Internet and advanced applications, the usage of online travel products and services have been growing tremendously. Online travel companies provide convenience, 24 hours and value added services to customers through modern and high technological means including internet, call centers, WAP phones, mobile PDA etc. The trend towards more and more online travel transactions are imminent. Some of the more successful example of online travel companies include Expedia, Travelocity, and Orbitz. Their business models and success have been well accepted by the market.

Whereas the online travel industry in the Mainland is still in its infancy. There is still no one major player that has emerged yet. But yet many of the general demographic and many market elements for a successful Internet travel industry in the Mainland are very similar to the US. The Mainland has now the second largest Internet population next to the US. It is inevitably that the Mainland Internet travel industry will evolve towards the success as seen in the US in due time.

The Board of Directors, after long and careful study and independent research, has concluded that the Group has sufficient resources and networking to develop a world class independent online travel company. The Group will leverage on its abundant travel related resources, its ground networking, its experienced travel manpower and huge cash reserves to create a competitive advantage for its online travel business. The Board of Directors is fully committed in this online travel investment as a long term core development strategy.

After emerging from the difficult times of the SARS epidemic, the Group still has to expose to fierce competition in the industry, lower gross profit margin and other unpredictable adverse factors. The board of Directors and the management are confident to overcome the difficulties and challenges faced by the Group, and will implement action plans to achieve established goals and strive for better results for the shareholders.