

Management's Discussion & Analysis



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Business Review

In 2004, the audited consolidated turnover of the Group was HK\$4,802 million, which is an increase of 45% as compared with HK\$3,301 million of last year, and the net profit attributable to shareholders was HK\$902 million. The net profit from operation was HK\$663 million, which is an increase of 91% as compared with HK\$347 million of last year. The growth was mainly attributable to the full recovery and further development of the Group's core travel businesses.

Mainland China remains the most important source of tourists for the Group. During the year, the management strengthened the Mainland travel agency network further by establishing joint venture travel agencies in Taiyuan, Suzhou and Korla City in Xinjiang and studied the possibilities of establishing travel agencies in Zhejiang and Yunnan in 2005. In addition, the Group established a new overseas travel agency in Christchurch in New Zealand. At the same time, the Group integrated its three travel agencies in Beijing and implemented centralized management. Overall, the Group's Mainland travel agency network started to contribute positive earnings. To strengthen the integration and coordination of the travel agency network in Hong Kong, Mainland China and overseas, the Group established the Coordination Centre of Travel Agencies, which coordinated the Group's travel agencies to organise large scale outbound tours to the 2004 Athens Olympics and virgin tours to Europe. Besides, the Coordination Centre of Travel Agencies established a new incentive system, strengthened internal control and unified the brandname of the Group's travel agencies,

thus enhancing the competitiveness of the Group's travel agencies. Taking into account the integrated nature of travel resources of the Group, the management devised the 5-year Development Plan addressing issues such as direction of development, focuses, complement of resources, sources of funds and internal revamp, etc., which lays down a solid foundation for further enhancing the core competitiveness of the Group's travel businesses.



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Tour Operation and Leisure Business

The tour operation and leisure business of the Group, include CTSHK, CT Net, three theme parks, a golf club in Shenzhen and Zhuhai Ocean Hotspring Resort. During the year, the turnover of the Group's travel and travel related operation reached approximately HK\$1,935 million, representing an increase of 48% as compared with last year. The total number of tourists received increased by 20% and the number of tourists received by China Travel Service (Hong Kong) Limited increased by 19%. The reservation of transportation tickets, hotel rooms increased by 25% and 11% respectively. The special tour business including day tour for Individual Visit Scheme ("IVS") travelers, exhibition and conference tour and study tour achieved encouraging results. The aggregate turnover of the Group's three travel agencies in Beijing increased by 88.5% and they possessed the rare capability of organising outbound tour group of several thousand tourists at one time. After three years of development, the Group's three travel agencies in Beijing are already ranked among the top five in the region. At the same time, the Group's overseas travel agencies developed further. The turnover of air-ticketing reservation of China Travel Service (Australia) Pty. Ltd. exceeded HK\$400 million. The coach tour of five European countries developed by China Travel & Trading (Deutschland) GmbH is expected to commence operation in May 2005. China Travel Service (U.K.) Ltd. was voted the top 10 best tour operators in England in 2004. During the year, the gross profit of China Travel Net Hong Kong Limited increased by 68% and the number of website visitors and number of members increased by 30% and 40% respectively, making China Travel Net the most visited travel website in Hong Kong. With high technology and comprehensive functions, the Centralized Platform in development will provide online and offline hotel and air-ticketing reservation services to business and individual clients and will be instrumental in integrating the Group's reservation resources, enlarging the Group's market share and reducing the operating costs of the Group's ground travel agency network. The Group will leverage on its competitive advantages developed through the years to accelerate the development of the Centralized Platform and strive to launch it by the end of 2005.



In 2004, Window of the World, Splendid China and China Folk Culture Villages received a total of 3.73 million visitors, representing an increase of 34% over last year. During the year, Window of the World achieved a pre-tax profit of over RMB100 million. It launched the "International Dance Festival", "International Beer Festival" and "Pop Music Festival" as well as completed the renovation of the park. A new mega evening art performance "Long Heritage" has been in rehearsal and will be launched in the first half of 2005. By strengthening marketing efforts and launching the well-received "Pasture Festival" of Xinjiang, Xishuangbanna and Inner Mongolia, Splendid China succeeded in reversing the trend of declining profits and recorded a profit growth of 200%.

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After producing various successful art performance programs such as “Fantastic Lijiang”, China Heaven Creation International Performance Art Co., Ltd. (“China Heaven”), in which the Group holds a controlling interest, launched another successful program namely, “Legend of Martial Art” in Beijing. The program won high acclaims from domestic and international tourists and attracted the attention of a large international performance agency which decided to bring the program overseas in 2005. The development of China Heaven will definitely strengthen the entertainment operation of the Group.

After the rebuilding of the “C” course and the installation of night light facilities, the number of golfers and the turnover of Tycoon Golf Club increased by 50% and 44% respectively in 2004. Tycoon Golf Club was voted “Best Landscape Golf Club” by the magazine “China Golf”.



The construction of the Zhuhai Ocean Hotspring Resort has been making steady progress. The construction work of the Conference Hotel, the twelve blocks of Villa Hotel and the two wings of the Main Hotel was completed whereas the construction work of the Hotspring Centre, Fisherman’s Wharf, Theatre, Theme Park and the lagoons and canals have been carried out rapidly. At the same time, preparation work for the opening of the resort was undertaken. It is expected that phase one of the Zhuhai Ocean Hotspring Resort will be completed in October 2005 and the soft opening will follow. With its unique ocean hotspring resources, the Zhuhai Ocean Hotspring Resort is expected to capture the growing demand of healthy and leisure holiday experiences and to be different from and complementary to the Hong Kong Disneyland. On the backdrop of economic growth of Pearl River Delta, improvement in transportation infrastructures and growing number of travelers visiting Hong Kong and Macau, the Zhuhai Ocean Hotspring Resort will bring contributions to the Group from 2006 and beyond.



Hotel Operation

Benefiting from the increase in number of travelers visiting Hong Kong and Macau brought by IVS, the average occupancy rate of the Group’s four hotels in Hong Kong reached 90.5%, representing an increase of 29% over last year, and the average room rate increased by 27%. Whereas the average occupancy rate and average room rate of Hotel Grandeur in Macau increased by 8% and 30% respectively. During the year, the profit contributed by the Group’s five hotels reached HK\$308 million, which was the highest level since 1997.

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Transportation

Regarding the passenger transportation operation, the number of passengers carried by China Travel Tours Transportation Services Hong Kong Limited and its subsidiaries ("CT Tours") (excluding those 24 hours passage passengers carried by a joint venture of CT tours) reached 1.4 million in 2004, representing an increase of 53% as compared with last year. Turnover increased by 68% to HK\$213 million and the after-tax profit increased by 226%. Benchmark measures such as the number of passengers carried, number of safety mileages, turnover and profit all achieved new records. Not only did the business in Hong Kong grow rapidly, new businesses were developed in the Pan Pearl River Delta region including Macau, Guangdong, Guangxi and Zhejiang, etc. Hence CT Tours became a well-known cross-border bus company. On the backdrop of recovery in Macau tourism, the turnover and net profit of the joint venture passenger ferry operation of Shun-Tak China Travel Shipping Investments Limited recorded a remarkable increase.

Regarding the freight forwarding operation, the turnover and net profit increased by 45% and 214% to reach HK\$1,857 million and HK\$38 million respectively in 2004. CTS International Transportation Company Limited ("CTS



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International”) in Shanghai, with its stronghold in Yangtse River Delta and the Eastern region, established branches in Nanjing, Wuxi and Nantong and these branches achieved profits in their first year of operation. In 2004, CTS International entered a stage of rapid development after strengthening its base over the past few years and the consolidated turnover and net profit increased by 48% and 70% respectively. Although the import and re-export freight volume through railway handled by China Travel Service (Cargo) Hong Kong Limited continued to decline, the logistics operation building on Hip Kee Godown (No. 3) began to take off, together with the contribution by Shenzhen operations, led the turnover to increase by 16%.

Infrastructure

Through taking measures to increase turnover and reduce costs, the Shaanxi Weihe Power Plant overcame the adversity brought by the substantial increase in coal cost. The technical benchmark measures of the Weihe Power Plant improved and the number of days of safety operation reached a new high of 650. The annual volume of electricity generated reached 7.597 billion Watt, its highest level in history and the annual volume of on-grid electricity increased by 19.5%.

Number and Remuneration of Employee

At the end of 2004, the Group had approximately 6,824 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 Board of Directors consider that financial position of the Group is strong. At the end of 2004, the cash and bank balance of the Group amounted to HK\$1,786 million whereas the interest bearing bank debts and the convertible bonds amounted to HK\$712 million and HK\$808 million respectively. The interest bearing debt to equity ratio was 18.2%.

The net book value of the Group's fixed assets held under finance leases and hire purchase contracts included in the total amount of motor vehicles and furniture, fixtures and equipment at 31 December 2004 amounted to HK\$1,324,167 (2003: HK\$3,318,183).

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During the year, 33,194,718 bonus warrants were exercised for 33,194,718 shares of HK\$0.10 each at the subscription price of HK\$1.508 per share and US\$48.19 million of convertible bonds were converted into 204,265,355 shares of HK\$0.10 each at the conversion price of HK\$1.84 per share. Taking into account the repurchase of 2 million shares of HK\$0.10 each by the Company during the year, the number of issued share capital of the Company increased from 4,232,198,475 shares at the end of 2003 to 4,467,658,548 shares at the end of 2004.

As at 31 December 2004, the Company had loan facilities, which were subject to, inter alia, a specific performance obligation on the controlling shareholder of the Company, CTS Holdings, during the tenure of such loan facilities. The specific performance obligation is that CTS Holdings shall maintain a holding of no less than 51% of the total issued share capital of the Company throughout the tenure of the loan facilities granted to the Company. A breach of the obligation will constitute an event of default. As a result of such breach, the loan facilities may become due and repayable on demand by the relevant lenders according to the respective terms and conditions thereof. The details of the loan facilities are as follows:

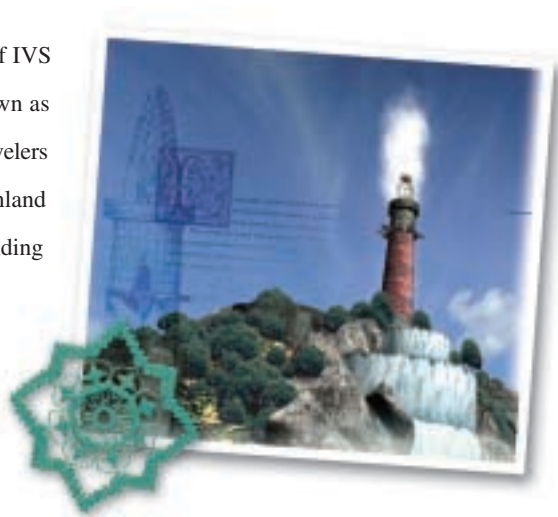
Amount outstanding as at 31 December 2004 Final maturity of the loan facilities

HK\$700 million	30 October 2007
Nil	30 April 2005

Interest is charged on the outstanding balance at 0.5% per annum over the Hong Kong Interbank Offered Rate for the applicable loan period. The loans are secured by the corporate guarantee given by the Company.

Future Prospects

Amid the opening of the Hong Kong Disneyland, further extension of IVS and regional cooperation within the Pan Pearl River Delta (also known as "9+2"), Hong Kong tourism will continue to grow and the number of travelers visiting Hong Kong is expected to reach 22.9 million in 2005. In Mainland China, the economy is growing steadily and it will spur the travel spending of PRC tourists. Together with the favorable policies adopted by the PRC government to develop tourism and the opening of more countries with the Approved Destination Status for PRC tour groups, all these favorable developments will provide ample business opportunities for the travel businesses of the Group.



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The Group will expand its travel agency network in Hong Kong, Mainland China and overseas by establishing new agencies. Through integration of operation of its travel agencies and centralized procurement, the Group aims to reduce operating costs and increase competitiveness. Leveraging on its extensive ground travel agency network and the technical edges of its Centralized Platform, the Group will develop core competitiveness in providing quality and comprehensive travel information, products and services to business, conference and leisure customers.

Seizing the opportunities brought by the opening of the Hong Kong Disneyland and the further extension of IVS, the Group will strengthen its internal integration and leverage on its brandname and resources to launch products and services targeting IVS travelers. In addition, the Group will augment its leisure and sightseeing tour operation in Hong Kong and Pearl River Delta to stimulate further developments of its theme parks, the Zhuhai Ocean Hotspring Resort, transportation and hotel operation.

The management is confident that positive developments in the Group's core travel businesses will prevail. However, the Group is facing a few challenges. The rise in coal and fuel prices will inevitably increase the costs of certain operations of the Group. The Zhuhai Ocean Hotspring Resort and the Centralized Platform are still in their development stage and their contributions will only be reflected in the following years. And the competition remains fierce in different travel businesses. Nevertheless, the competitiveness of the Group's core travel businesses has been enhanced through the past few years, which lays down a solid foundation for the continuous and rapid development of the Group. The management will continue to develop and innovate so as to bring better returns to the shareholders.

