## CHAIRMAN'S STATEMENT

### Financial Review

For the six months ended 30 June 2005, the Group recorded a turnover of approximately RMB42,024,919 (2004: RMB47,009,942), representing a decrease of 10.6% as compared to that of last corresponding period. Of these, turnover derived from the sales of self-developed software was approximately RMB10,674,469 (2004: RMB18,144,179), representing a decrease of 41.2% as compared to that of last corresponding period. Turnover derived from sales of third party software and hardware in relation to system integration increased from approximately RMB22,450,910 in the last corresponding period to approximately RMB29,687,699, representing an increase of 32.2% as compared to that of last corresponding period. During the period under review, turnover derived from system integration, maintenance and other services decreased from RMB6,414,853 to approximately RMB1,662,751.

The Group recorded a gross profit of RMB14,757,023 (2004: RMB23,089,186). The overall gross profit margin was approximately 35.1%, of which the gross profit margin in respect of the sales of self-developed software remained the same as that of last December, while the gross profit margin in respect of sales of third party software and hardware slightly declined by 3%. Net profit attributable to shareholders was approximately RMB5,441,800 (2004: net profit of RMB15,459,862), representing a decrease of 64.8% as compared to that of last corresponding period. Basic earnings per share was approximately RMB1.36 cents (2004: RMB5.15 cents).

The Board of Directors of the Company has resolved not to declare interim dividend for the six months ended 30 June 2005 (2004: nil).

On the whole, decline in both turnover and profit for the first six months of 2005 was due to the slowdown in the investment in telecommunications market in the People's Republic of China ("PRC") and the decrease in investments from the Group's major customers, the four leading PRC telecommunications operators. On the other hand, the Group expects 2G will gradually be replaced by 3G, thereby allocating more resources for development of 3G OSS software business during the period under review in order to speed up the research and development ("R&D") progress. Yet investments in 3G have not generated obvious returns in the first half year, indirectly causing a decrease in sales revenue during that period. Given certain contracts have not been inspected and recognized before 30 June, part of income cannot be reflected in these results.

### Business Review

The Group is principally engaged in the provision of OSS self-developed software products and one-stop integration services to the telecommunications service providers. Our businesses include sales of self-developed software, provision of system integration using mainly our self-developed software, as well as provision of total solutions comprising maintenance, training and other after-sales services. The current end users of the Group's OSS products and solutions include the four major PRC infrastructural telecommunications service providers, such as China Mobile Group.

During the six-month period under review, the Group has practically pursued and achieved the goals set by the end of 2004. With the four vital goals of R&D professionalism, products seriation, projects standardisation and management sophistication, the Group has been ranked the 23rd place out of the OSS product providers in the world in an OSS market perception report issued by Heavy Reading, an international independent research institution, indicating that the Group's products are highly recognized by international professionals.

In respect of the development of OSS, the Group has set up a joint venture company with Shanghai Telecommunications Industry (Group) Co., Ltd., a company under the China Telecom Group, Shanghai Fortune Telecommunications Technology Development Company Limited and Alcatel Shanghai Bell Co., Ltd.. The joint venture company is principally engaged in design, manufacturing and sale of telecommunications connection terminal products, its related services and telecommunications value added business, thereby laying a solid foundation for expansion and technological development of terminal equipment which is used for our key business of OSS self-developed software products. With the rapid development of information and mobile communications, telecommunications operators has focused more on information services, and terminal equipment will become an indispensable key to develop information services. Through the formation of such joint venture company, the Group is able to capture the core terminal technology, which will bring us new opportunities for telecommunications business and will greatly enhance our capability of expanding market channels.

In respect of software development and management, the Group has developed a "large-scaled integrated OSS for mobile network" in alliance with China Mobile Communications Corporation and another company. Such large-scaled mobile network covers 31 provinces nationwide and is mainly used for various kinds of network management such as GSM, transfer and SMS. It also demonstrates the inter-connection of systems under a unified management, maintenance, analysis and processing of OSS data among all provinces in the PRC. This system has been awarded "China Institute of Communications' Science and Technology" First Prize by the China Institute of Communications (an association supported by the Ministry of the Information Industry), thus posing a positive effect on the enhancement of operators' efficiency.

In February 2005, the Group successfully released E2EVIEW 2.x version in compliance with Next Generation OSS (NGOSS) standard set by the Telecommunications Management Forum (TMF). In light of the software structure, such version forms the overall framework for development of the Group's OSS fundamental platform and application system, and builds up the foundation for enhancing the Group's capability of design and exploration.

In connection to the enhancement of E2EEASY, the Group has used integrated core projects to gain in-depth understanding of the requirements of application and customers. Through consolidating our projects in relation to telecommunications integrated resources system in 2005, the Group has completed E2E business

deployment and open-up system for professional resources such as cross-transmission, data and line management. Coupled with a breakthrough by developing business scope in respect of MPLS VPN and ADSL, the Group has substantially upgraded the original E2EEASY core platform.

Another breakthrough of the Group in 2005 is related to network quality analysis and business quality analysis. Through consolidating the framework of E2EVIEW, the Quality Management Platform (QMP) products are well-defined and the breakthrough of the Group's E2EVAS product series is also confirmed. This is exactly the Group's targeted R&D purpose of creating a leading edge against other competitors. The abovementioned product is scheduled to be introduced to the market by the end of 2005.

Considering the issuance of 3G license in the future, the Group has put considerable resources on the development of 3G business during the period under review. Nearly 60 staff are assigned to work for 3G R&D department and the total investment cost in 3G amounts to RMB4,067,118. The development of version one of a 3G platform-based application middleware has been completed in mid-June, and the development of the fundamentals of version three of ISMC software, which is compatible to 3G, has also been completed. To cope with the changes in the market, the Group has undergone each and every development to get ready for the huge 3G market in the future.

During the period under review, the Group has signed 53 new contracts which totalled approximately RMB40,000,000, showing that the Group has not only committed to complete the fundamental development of 3G OSS software, but has also actively dedicated itself to expand its businesses and endeavoured to seize opportunities for collaboration.

## Customers

The Group's customers comprise the four major telecommunications operators including the China Mobile Group, covering 31 provinces, municipalities and cities in the PRC, as well as enterprises and private network customers. The Group has maintained a concrete relationship with the customers and has collaborated with major strategic partners, including various international telecommunications conglomerate such as Alcatel Shanghai Bell Co., Ltd., as well as domestic and international reputable system integrators and software providers.

## Product research and development

As the second largest OSS software provider in the PRC, the Group actively grasp the essence in the R&D of OSS products in order to implement different stages of professional division and cooperation throughout the R&D procedures which comprise of demand analysis, series design, code test and product development. The Group has also implemented professional division on the R&D of various technological fields including typical data access, data processing, data management and data display. In addition, the Group has improved its working efficiency, lowered the overall costs and ensured its product quality through different professionals.

For the sake of long-term development, the Group has relocated to a new office on 16 June 2005. The new address is located in the core area of Zhongguancun, adjacent to various renowned professional scientific research institutes and prominent colleges and universities. Leveraging on the rich atmosphere of scientific research in such place and its edge of high caliber staff, the Group will have a more rapid and stable development. Total number of R&D staff has increased from 180 of last corresponding period to 209 for the current period. Influenced by industry restructuring and uncertainties related to the grant of 3G license, telecommunications sector experienced a decline in capital expenditure during the first half of 2005 compared to the same period of last year in the PRC. The Company allocated part of experienced human resources (about 60 staff) to focus on the R&D of 3G in the first half of 2005. It is expected that the telecommunications operators will expand their investments in telecommunications market in the second half of this year, and the sales revenue of the Group is expected to increase correspondingly. With a view to allocating half (30) of 3G R&D officers to the new business, the Group will put more efforts to complete the fundamental development of 3G OSS software by this third quarter.

## Sales strategies

2005 is the year of sales channels for the Group. During the period under review, the Group has continued to thoroughly develop its "foothold" in its existing markets including Shanghai, Beijing and Gaungzhou. In addition, the Group has designated permanent staff stationed in major provinces and municipals such as Sichuan, Liaoning and Anhui in order to effectively control its sales and business development. The Group has also actively explored markets for other core businesses and large-scale application network enterprises. For the sake of further boosting the sales of its self-developed software products, the Group has established the sales, engineering and services network developed through collaboration of Beijing, Shanghai and Guangzhou, and continued to seize opportunities for cooperation with different strategic partners. In this regard, the Group's core competitiveness will further be enhanced.

## Prospect

3G development has recently been the crucial development of telecommunications industry in the PRC. According to the specific research report issued by CCID Consulting Company Limited ("CCID"), it is predicted that 3G OSS software market in the PRC telecommunications industry will develop rapidly in an annual compound growth rate of approximately 33.5% from the first year after the launch of 3G till the sixth year, while demand from other industries will have a strong growth at the same time. To capture such opportunity, the Group has not only developed ISMC software and a 3G platform-based application middleware, but has also commenced research and prototyping work in respect of the 3G portal systems as well as R&D work for 3G element management system products. In this regard, the Group will further invest in 3G market, with an aim to provide total solutions for telecommunications service provider in this market. In connection with the R&D of 3G products, the Group is one of a few well-positioned OSS product and solution providers in the PRC, and it is expected that the launch of 3G in China will bring tremendous growth to the Group's business.

In order to maintain and expand its market share, it is necessary for the Group to cope with changing customers' requirements as well as to keep abreast of the latest technological developments in the industry. As such, the Group intends to expand its products and services portfolio by developing and introducing new OSS products such as the E2E VAS series by the end of this year. At the same time, the Group will keep on seeking cooperative partners for further business expansion.

With an aim to strengthening its position as a leading OSS products and solutions supplier in the PRC, the Group plans to further expand the existing R&D team by recruiting more experts within the industry to join its R&D team, provide continual training to improve its technical know-how and purchase additional R&D equipment so as to enhance the quality of its products and services. Besides, the Group will actively participate in overseas exhibitions not only to keep pace with the latest OSS technology for strengthening its R&D capability in the 3G area, but also to raise the reputation of the Group.

Looking ahead, the Group believes that the fund allocated for 3G development will generate remarkable returns in future. Taking advantage of the 3G license to be issued in the PRC in the future, the development pace of PRC's telecommunications industry will speed up and this segment will become the major growth potential of the Group. Furthermore, the Group will keep adhering to its target of being PRC's leading and a world renowned OSS products and solutions provider. Through active provision of leading software products and solutions for different businesses and quality services for customers, the Group is confident to create the best values to its shareholders.

### Acknowledgement

On behalf of the Board, I would like to express my sincere gratitude to all the management and the staff for their dedication and contribution. I would also like to take this opportunity to express my sincere thanks to our shareholders, investors and customers for their dedicated support and continuous encouragement.

By Order of the Board

**Wang Feixue**
*Chairman*

Beijing, the PRC, 14 September 2005