

# MANAGEMENT DISCUSSION AND ANALYSIS

## DISPOSAL OF NWPCS GROUP AND ACQUISITION OF CSL NWM GROUP

On 8 December 2005, the Group entered into a merger agreement (the "Merger Agreement") to dispose of the NWPCS Group and make a cash payment of HK\$244.024 million, in exchange for equity holding of 23.6% of the issued share capital of CSL NWM Group and an amount due from CSL New World Mobility Limited ("CSL NWM") of HK\$113.328 million. The merger executed pursuant to the Merger Agreement was completed on 31 March 2006. As a result, the NWPCS Group, which is engaged in mobile communications business, ceased to be subsidiaries of the Group; while the CSL NWM Group comprising the NWPCS Group and Telstra CSL Limited which has changed its name to CSL NWM and its subsidiaries have become associated companies of the Group. The application of Hong Kong Financial Reporting Standard No. 5 Non-current Assets Held for Sale and Discontinued Operations has resulted in a change in the presentation of the results and cash flows of the NWPCS Group in current and prior years but has not impacted prior year's consolidated balance sheet. In the consolidated income statement, a single amount comprising the results of the NWPCS Group, of which an analysis of the results is set out in note 8 to the consolidated financial statements, and gain on disposal of the NWPCS Group constituting discontinued operations is presented whereas the net cash flows of the NWPCS Group attributable to operating, investing and financing activities are also disclosed in the consolidated cash flow statement.

## ACQUISITION OF NEW WORLD CYBERBASE SOLUTIONS (BVI) LIMITED AND ITS SUBSIDIARIES (COLLECTIVELY THE "NWCS GROUP")

On 21 October 2005, the Group acquired from New World CyberBase Limited ("NWC") the entire issued share capital of the NWCS Group and NWC's interests in loans to the NWCS Group for an aggregate consideration of HK\$21 million. The NWCS Group is engaged in the provision of technology related services, mainly mobile Internet services and wireless application protocol ("WAP") services, in Mainland China. The purchase consideration was satisfied by the issuance of 16,153,846 ordinary shares of the Company at HK\$1.3 each.

## FINANCIAL REVIEW

The Group recorded a profit attributable to shareholders of HK\$911.6 million for the current year, as compared to a loss attributable to shareholders of HK\$10.4 million in the previous year. The profit of this year mainly arose from the profit of HK\$1,045.2 million (2005: HK\$36.7 million) from discontinued operations of mobile communications services, slightly offset by the loss of HK\$133.6 million (2005: loss of HK\$47.1 million) from continuing operations.

Profit from discontinued operations comprised after-tax profit of HK\$22.2 million of the NWPCS Group for the nine months ended 31 March 2006 (year ended 30 June 2005: HK\$36.7 million) and the gain of HK\$1,023.0 million on disposal of the NWPCS Group.

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Loss from continuing operations was attributed to the loss of HK\$87.4 million of the technology related business, finance costs of HK\$62.8 million and other corporate expenses, slightly alleviated by the Group's share of results of the CSL NWM Group.

The loss of HK\$87.4 million of the technology related business comprised impairment losses on intangible assets of HK\$73.0 million. The impairment losses on intangible assets were provided for goodwill of HK\$66.0 million arising from the reverse acquisition of the Company and its subsidiaries by the NWPCS Group in July 2004 which was re-allocated to the Group's new continuing operations in technology related services, goodwill of HK\$5.5 million arising from the acquisition of the NWCS Group and a licence of HK\$1.5 million. The continuing operations recorded a turnover of HK\$16.5 million from the technology related business for the post-acquisition period from 21 October 2005 to 30 June 2006, as compared to HK\$4.3 million from logistics services in the previous year. WAP services have become the key growth driver contributing to improvement in turnover. On 30 June 2006, there were more than 270,000 monthly subscribers, over 90% of them are multimedia messaging services ("MMS") and WAP subscribers. During the period under review, product development teams in Shanghai and Guangzhou have developed more than 100 new MMS, WAP and short messaging services.

Finance costs of continuing operations for the current year was HK\$62.8 million, an increase of HK\$18.1 million from HK\$44.7 million for the same period last year. The increase was mainly due to interest expenses of HK\$11.5 million on a new promissory note issued to a fellow subsidiary in March 2006 to replace loans and accrued interest expenses of a total of HK\$886.7 million of the NWPCS Group for which the related interest expenses incurred before the replacement were deducted from the profit from discontinued operations, and interest expenses of HK\$3.6 million on new loans of HK\$278.0 million drawn from the fellow subsidiary in March and June 2006.

The CSL NWM Group is a major mobile telecommunications network operator in Hong Kong, providing 2G and 3G services under three brands: "One2Free", "1010" and "New World Mobility". On 30 June 2006, there were over 2.6 million subscribers to its services. The Group's share of 23.6% of the results of the CSL NWM Group for the three months from 1 April 2006 to 30 June 2006 amounted to HK\$27.7 million.

### CAPITAL STRUCTURE, LIQUIDITY AND FINANCE RESOURCES

As at 30 June 2006, total borrowings of the Group amounted to HK\$2,371.0 million (30 June 2005: HK\$2,043.5 million). These borrowings comprised subscription note of HK\$1,178.0 million, convertible bond of HK\$28.3 million, promissory note of HK\$886.7 million issued to New World Finance Company Limited ("NWF") and loans of HK\$278.0 million from NWF. The promissory note was issued to settle debts of the NWPCS Group before disposal of the NWPCS Group to CSL NWM. Loans of HK\$278.0 million were obtained to finance the acquisition of the CSL NWM Group and meet requirements on the Group's working capital. These borrowings are denominated in Hong Kong dollars, and bear interest rates of 0.75%, 3%, 0.65% above HIBOR and 0.65% above HIBOR per annum respectively.

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The maturity date of the convertible bond has been extended to 1 November 2007. The promissory note is repayable on demand after eighteen months from its date of issue of 30 March 2006. Loans of HK\$244.02 million and HK\$34.0 million from NWF are repayable upon demand after eighteen months from 31 March 2006 and after 28 August 2007 respectively.

Since most of the borrowings of the Group are considered as shareholders' loans, the gearing ratio of the Group calculated thereon is considered misleading and therefore, not presented.

As at 30 June 2006, the Group's cash and bank balances were of HK\$27.7 million (30 June 2005: HK\$116.5 million). The reduction was mainly the result of the disposal of the NWPCS Group. The Group had undrawn loan facility of HK\$36.0 million as at 30 June 2006.

Total capital expenditure of the Group was HK\$97.4 million for the year (2005: HK\$140.8 million), which was mainly spent on the NWPCS Group's mobile communications business.

The key operations of the Group are located in Hong Kong and Mainland China. Therefore, our assets and liabilities are mainly denominated in either Hong Kong dollars or Renminbi. Since no significant exposure to foreign currency gains and losses are expected, the Group does not conduct any foreign currency hedging activities.

### EMPLOYEES AND REMUNERATION POLICY

As at 30 June 2006, the Group had a total of 143 employees (30 June 2005: 662). The reduction in number of employees was mainly due to the disposal of the NWPCS Group. The Group's remuneration policy is to pay salaries competitive in the industry, in a way that is motivational, fair and equitable. The salaries are also dependent on individual and company's performance. Apart from salaries, the Group also provides other fringe benefits to employees, which include provident fund schemes, medical insurance and bonus on performance basis.

### OUTLOOK

According to the June 2006 report by China Internet Information Centre, there are over 123 million Internet users in China, a 19.4% growth from the previous year. The Ministry of Information Industry also expects the number of mobile phone users to reach 440 million at the end of 2006. Judging from the trend of growth of both Internet and mobile phone users, there will be ample room for growth for value added services.

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In July 2006, a major mobile operator partner implemented new control policies for value added service providers. It is expected that the improvement of the mobile Internet business will be slowed down due to the implementation of these new measures. The Group will re-align the strategic imperatives of the business to minimise the impact while capturing the growth opportunities in the explosive market potential in the long-term.

The Group is determined to carry on its expansion into the mobile Internet services area, with a focus on music and city infotainment services. In the music sector, the Group will continue its effort in building a platform for local music talents to create and publicise their works. Currently a platform has been created for music lovers to enjoy pop music as well as new local music. In addition to forming partnership with international record labels, building alliances with music industry players is essential to the Group's business expansion. Therefore, the Group has established strategic alliances with over 15 local record labels. Continuous alliance formation will be an important component to our success in the coming years.

In 2006, the Group has re-launched ChinaQuest.com, a web-based city infotainment service, with a powerful search engine. The partnership with China Telecom's yellow page has not only enabled us to increase the spectrum of services, but also contributed to the enrichment of the city information content. Currently the Group has rolled out city information content services in 12 cities. In 2007, the Group will expand the city infotainment service in these cities and into other untapped markets.

In 2006, the Group has strengthened the base to its mobile Internet platform. Building on this foundation, the Group will seek to secure greater market share in 2007. One of the key strategic directions for the provision of services in 2007 is to increase user interactivities by implementing Web 2.0 applications in both the Internet and WAP services. The Group believes that success in enhancing customer satisfaction in and fondness to our services will result in continuous growth of our technology related business.

The Group's investment in the mobile communications business through its equity holding of 23.6% of the CSL NWM Group will also continue to generate profit to the Group.