

# FINANCIAL REVIEW

## MANAGEMENT DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis should be read in conjunction with the financial information of the Group contained in the financial statements (together with the notes thereto) reproduced in this annual report. The financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS"). The following discussion on the synopsis of historical results do not represent a prediction as to the future business operations of the Group.

### OVERVIEW

For Year 2006, profit before taxation of the Group was approximately RMB627.9 million, representing an increase of approximately 5.6% over that in the year ended December 31, 2005 ("Year 2005"). Earnings before interests, tax, depreciation and amortization (EBITDA) reached approximately RMB789.5 million, representing an increase of approximately 9.1% over that in Year 2005. Profit attributable to equity holders of the Company was approximately RMB515.6 million, a decrease of approximately 2.7% over the previous year was mainly due to the expiration of the tax holiday of the Company on December 31, 2005, and the enterprise income tax rate increased to 15% for Year 2006 from 7.5% for year 2005.

The basic and diluted earnings per share of the Group in Year 2006 was RMB0.58.

### TOTAL REVENUE

The total revenue of the Group in Year 2006 amounted to approximately RMB1,711.7 million, representing an increase of approximately RMB214.9 million, or 14.4%, from approximately RMB1,496.8 million in Year 2005. Such increase was mainly due to the rapid increase in the business volume of the Company's AIT services in 2006. The increase in total revenue is reflected as follows:

- AIT service revenue represented 81.5% of the total revenue of the Group in Year 2006 as compared to 82.7% in Year 2005. AIT service revenue increased by approximately 12.7% to approximately RMB1,395.2 million in Year 2006 from approximately RMB1,238.0 million in Year 2005. The increase of revenue resulted primarily from the increase in ETD business.
- Data network and other revenue represented 18.5% of the total revenue of the Group in Year 2006 as compared to 17.3% in Year 2005. Data network and other revenue increased by approximately 22.3% to approximately RMB316.5 million in Year 2006 from approximately RMB258.8 million in Year 2005.

### NET REVENUE

Net revenue increased by 14.4% to approximately RMB1,655.3 million in Year 2006 from approximately RMB1,447.0 million in Year 2005.

## OPERATING EXPENSES

Operating expenses for Year 2006 amounted to RMB1,093.5 million, representing an increase of RMB190.3 million, or 21.1%, from RMB903.2 million in Year 2005. The increase in operating expenses reflected the following:

- Depreciation and amortization increased by 25.9% from RMB182.0 million in 2005 to RMB229.2 million in 2006, mainly due to increase in provision for depreciation and amortization of capital expenditure commenced in 2006;
- Network usage charge, increased 27.6% from RMB60.0 million in 2005 to RMB76.5 million in 2006, mainly because of increase in the flight bookings in foreign and regional commercial airlines and increase utilisation of APP system of the Company by foreign and domestic commercial airlines;
- Personnel expenses increased by 15.1%, primarily attributable to the increased number of staff to support the business development of the Group;
- Technical support and maintenance fee increased by 46.5% due to the continuous increase in investment in new products, research and development of new technologies of the Company and an increase in the maintenance fee of hardwares and softwares purchased in Year 2006; and
- Commission and marketing expenses increased by 31.1%, primarily due to the development of businesses such as APP, hotel reservation.

As a result of the above changes in net revenue and operating expenses, the operating profit of the Group increased by RMB17.9 million, or 3.3%, to RMB561.8 million in Year 2006 from RMB543.9 million in Year 2005.

## ENTERPRISE INCOME TAX

The Company, registered as a new technology enterprise in October 2000 in Zhongguancun Haidian Science Park, has been approved by the Haidian State Tax Bureau that an enterprise income tax (“EIT”) rate of 15% was effective from January 1, 2006. The Company was subjective to EIT rate of 7.5% in 2005.

As stated in the Company’s announcement issued on January 31, 2007, the Company was recognized as one of the 2006 Important Software Enterprises under the National Planning Layout (“Important Software Enterprises”). According to relevant regulations, recognized Important Software Enterprises which are not in their tax holiday period are entitled to an EIT preferential tax rate of 10% in the relevant year. Accordingly, the Company, recognized as one of 2006 Important Software Enterprises is entitled to enjoy the above EIT preferential tax rate in the financial year ended December 31, 2006.

The Company has already paid EIT at the rate of 15% for the financial year ended December 31, 2006. According to the related regulations, the EIT paid by the Company for the financial year ended December 31, 2006 over the newly announced preferential tax rate of 10% will be refunded to the Company in the subsequent year. Its impact will be accounted for in 2007 financial statements accordingly.

## PROFIT ATTRIBUTABLE TO EQUITY HOLDERS OF THE COMPANY

As a result of the above factors, the profit attributable to equity holders of the Company decreased by approximately 2.7% to approximately RMB515.6 million in Year 2006 from approximately RMB529.6 million in Year 2005.

## RESERVES AVAILABLE FOR DISTRIBUTION

After the appropriation of the statutory surplus reserve fund and the discretionary surplus reserve fund from the profit attributable to shareholders as reflected in the statutory financial statements prepared separately under PRC Accounting Standards and regulations and IFRS, the reserves available for distribution as at December 31, 2006, as stated in Note 32 to the financial statements, amounted to RMB787.9 million.

## DISTRIBUTION OF DIVIDEND AND PROPOSED BONUS ISSUE OF SHARES

On March 28, 2007, the Board recommended a final dividend of RMB0.22 per share for Year 2006, amounting to RMB195.4 million. After the distribution of the above dividend declared, the reserve available for distribution as at December 31, 2006 would be approximately RMB592.5 million (2005: RMB423.6 million).

On March 28, 2007, the Board recommended a bonus issue of shares on the basis of the bonus share for every one share to the shareholders of the Company. The relevant proposal is subject to shareholders' and relevant regulatory approvals and should be in compliance with relevant laws and regulations.

A circular containing particulars regarding the proposed bonus issue of shares will be despatched to the shareholders of the Company as soon as practicable.

## LIQUIDITY AND CAPITAL STRUCTURE

The following table summarizes the cash flows of the Group for the years presented:

	For the year ended December 31	
	2006 <i>(RMB in million)</i>	2005 <i>(RMB in million)</i>
Net cash inflows from operating activities	<b>650.9</b>	402.5
Net cash used in investing activities	<b>(42.1)</b>	(1,656.7)
Net cash used in financing activities	<b>(217.3)</b>	(111.3)
Impact of change of exchange rates on cash and cash equivalents	<b>(15.2)</b>	(14.6)
Net increase (decrease) in cash and cash equivalents	<b>376.3</b>	(1,380.0)

The Group's working capital for Year 2006 mainly came from operating activities. Net cash inflow from operating activities amounted to RMB650.9 million.

In Year 2006, the Group had no short-term and long-term bank loans, and the Group did not use any financial instruments for hedging purposes.

As at December 31, 2006, cash and cash equivalents of the Group amounted to RMB1,233.2 million, of which approximately 86.4%, 8.9% and 4.5% were denominated in Renminbi, U.S. dollars and Hong Kong dollars, respectively.

## LONG-TERM INVESTMENT

As at December 31, 2006, the Group held RMB100 million treasury bonds of China with an interest rate of 3% per annum. The maturity date of the treasury bonds is on December 18, 2008.

## CHARGE ON ASSETS

As at December 31, 2006, the Group had no charge on its assets.

## CAPITAL EXPENDITURE

The capital expenditure of the Group amounted to approximately RMB159.3 million in Year 2006, representing a decrease of approximately RMB275.7 million as compared to that of approximately RMB435.0 million in Year 2005.

The capital expenditure of the Group in Year 2006 consisted principally of purchase of hardware, software and infrastructure in accordance with the Group's business strategies.

The Board estimates that the Group's planned capital expenditure for year 2007 will amount to approximately RMB494.7 million, which is mainly for development and gradual implementation of the new-generation civil traveler service system and other new businesses.

The sources of funding for the capital expenditure commitments will include internal cash flow generated from operations.

The Board estimates that the sources of funding of the Group in year 2007 will be sufficient for its capital expenditure commitments, daily operations and other purposes.

## EXCHANGE RISKS

The Group's foreign exchange risk arises from commercial transactions and recognised assets and liabilities. Fluctuation of the exchange rates of Renminbi against foreign currencies could affect the Group's results of operations.

## GEARING RATIO

As at December 31, 2006, the gearing ratio of the Group was approximately 10.3% (2005: 11.2%), which was computed by dividing the total amount of liabilities by the total assets of the Group as at December 31, 2006.

## CONTINGENT LIABILITIES

As at December 31, 2006, the Group had no material contingent liabilities.

## EMPLOYEES

As at December 31, 2006, the total number of employees of the Group was 2,388. Salary and bonus expenses amounted to approximately RMB181.6 million for Year 2006, representing approximately 16.6% of the total operating cost of the Group for Year 2006.

The remuneration of the employees of the Group (including Executive Directors and Staff Representative Supervisors) includes salaries, bonuses and other fringe benefits. The Group has different rates of remuneration for different employees (including Executive Directors and Staff Representative Supervisors), according to their performance, experience, position and other factors in compliance with the relevant PRC laws and regulations.

Currently, none of the Non-executive Directors receive any remuneration. Nevertheless, any reasonable expenses incurred by the Non-executive Directors during their service period will be borne by the Company. Independent Non-executive Directors do receive remuneration from the Company, which is determined by reference to the prevailing market price, and that any reasonable expenses incurred by Independent Non-executive Directors during their service period will be borne by the Company.

In Year 2006, the Group continued to provide its employees with opportunities to acquire skills in relation to the aviation and travel industry, computer technologies and business administration and provide training on the latest development in areas such as computer technologies, personal development, laws, regulations and economics.

## BASIC MEDICAL INSURANCE REGULATION

On February 20, 2001, the People's Government of the Municipality of Beijing in the PRC promulgated the "Basic Medical Insurance Regulation for the Municipality of Beijing" (the "Regulation"). Given the fact that relevant regulations concerning employees' medical insurance must be applied according to the policies applicable to the place in which a company is located, the head office of the Company in Beijing implemented the Regulation from September 1, 2002 onwards. For Year 2006, the Company incurred a total amount of RMB7,162,909 (a total amount of RMB5,504,730 was incurred in Year 2005) pursuant to the Regulation. The Board believes that by implementing the Regulation, the financial position of the Company has not been materially affected.