Industry Review

China's economy continued to record strong growth in the first half of the year, with GDP having increased by around 10% year-on-year. Advertising spending as a whole continued to grow healthily in the first half of the year, as boosted by the 2006 FIFA World Cup in the second quarter of the year. This hugely-successful event, however, created a number of short-term fluctuations in the consumption patterns of consumers as well as advertisers' media mix strategies during the first half of 2006. Nevertheless, we expect that normal advertising spending patterns will gradually resume and that outdoor advertising spending will increase in the second half of the year.

Operations Review

The period under review marked eight and a half consecutive years of growth for Clear Media and another solid interim performance.

Core Bus Shelter Advertising Business

Our core bus shelter advertising business spanning across 30 key cities in China continued to perform well, despite the short-term fluctuations in the advertising spending due to the 2006 FIFA World Cup. Over the last six months, our nationwide network has generated HK$336 million in turnover, representing an 11% increase from the same period last year and accounting for 96% of the Group's total turnover (1H2005:99%). The average selling price increased by 15%. The price increment was partially offset by a 9% decrease in average occupancy rate to 53% (1H2005:62%), as our customers needed time to adapt to the new pricing.

We continued to expand our network in the first half of the year and added 1,347 new panels through organic development and acquisitions during the first six months of 2006, which included 634 panels acquired in Beijing in June this year. During the period under review, on a time-weighted basis, the number of 12-sheet equivalent panels increased from 22,699 to 24,736, or by 9%, as compared with the same period last year. Apart from increasing our assets, we have also commenced a project to enhance the returns on our assets, by converting all advertising panels in Shanghai to scrolling panels, allowing us to charge rates higher than those for static panels.

Key Cities

Guangzhou, Shanghai and Beijing continued to be the top three cities where we maintained leading positions in outdoor advertising, and these cities continued to contribute the most to our overall performance in the first half of 2006. Total sales of the three key cities grew by 13% in the first half of the year, which accounted for 54% of our total bus shelter advertising business, as compared with 53% in the corresponding period last year. We have also extended a majority of the concession contracts in Beijing to 2018. Bus shelters in these three key cities accounted for 41% of the Group's total number of bus shelter advertising panels during the period under review.

In Shanghai, sales rose by 17% due to the introduction of the new scrolling panels. The conversion process of bus shelters to scrolling panels has reduced the availability of some bus shelters and therefore sales were affected. We expect sales to improve in the second half when the conversion process is completed. In Beijing, sales increased by 13% and the average selling price grew by 10% while the occupancy rate dropped slightly to 56%. In Guangzhou, sales increased by 10% and the average selling price increased by 7% as compared to the same period last year, however, the occupancy rate dropped to 66%.

Mid-tier Cities

Performance in the mid-tier cities showed satisfactory growth in the first half. Sales increased by 9% and the average selling price showed a strong increase by 16%. The average occupancy rate however dropped to 50% (1H2005:60%) as the higher selling prices had caused some short-term switching by certain customers, but we expect that customers will gradually adjust to our new prices. Sales from mid-tier cities accounted for 46% of the Group's total sales in the first half of the year (1H2005:47%).

Other Advertising Formats

In the first half of the year, the Group's other advertising formats, including airport advertising, point-of-sale, unipoles and other advertising formats, generated a total of HK$12.4 million in sales revenue as compared to HK$3.6 million recorded in the first half of 2005.

Financial Review

Turnover

The Group's turnover increased by 14% to HK$349 million from HK$307 million during the period under review. Our core bus shelter advertising business remains the driver of this growth in the first half of 2006. Our entire turnover was derived from China. Total sales from bus shelter advertising increased by 11% to HK$336 million in the first half of 2006 (1H2005: HK$303 million) despite the short-term fluctuations in the advertising market in China in the first half of the year. The other advertising formats including airport, point-of-sale, unipoles and other advertising formats contributed a total of HK$12.4 million during the period under review (1H2005: HK$3.6 million).

Expenses

Expenses in relation to core bus shelter advertising accounted for the main part of Clear Media's expenses. Direct operating costs, which included electricity, rental, maintenance costs and sales and cultural levy increased from HK$125 million last year to HK$140 million in the first half of 2006. Despite the higher rental expenses, direct costs represented about 40% of sales as compared with 41% in the same period last year. The impact, brought about by the higher rental expenses, was offset by the reversal of the over-provision of sales taxes created in the previous year.

Selling, general and administrative expenses increased by 25% in the first half of the year to HK$76.9 million (1H2005: HK$61.3 million) and as a percentage of sales, these expenses increased by 2% to 22%. This was largely due to the increased staff salary which accounted for 11% of sales in the first half of the year (1H2005:10%), following Clear Media's recent internal restructuring to ensure that our high caliber staff are appropriately remunerated and incentivised.

The expansion of our bus shelter network, including the acquisitions in Beijing, our build-out in other cities and the conversion of advertising panels to scrolling advertising panels in Shanghai this year have resulted in a higher charge for the amortization of concession rights which increased by 13% to HK$73.6 million (1H2005:HK$65.2 million). As a percentage of sales, amortization remained at 21% for both periods.

EBITDA

Our total earnings before interest, tax, depreciation and amortization (EBITDA) increased by 8% to HK$133 million in the first half of the year, from HK$123 million in the same period of 2005. Clear Media's EBITDA margin has decreased by 2% to 38% as a result of higher staff costs.

EBIT

Our total earnings before interest and tax (EBIT) improved by 2% from HK$55 million to HK$56 million for the period under review.

Net Profit

Our net profit increased by 19% to HK$42 million for the six months ended 30 June 2006 as compared with the corresponding period last year. Income tax payable for 2006 is lower as we started sponsoring advertising campaigns for charitable organizations which resulted in some tax benefits. In addition, the Group has also started to utilize tax losses carried forward. The net profit margin remained flat at 12% (1H2005: 12%).

Liquidity and Financial Resources

The Group financed its operations and investment activities with internally-generated cash flow, balanced with proceeds from the prior issue of convertible bonds.

Cashflow

Net cash inflow generated from our operations in the interim period reached HK$112 million, as compared with HK$108 million in the same period last year. Cash from investment activities amounted to an outflow of approximately HK$241 million as compared with HK$94 million for the same period last year. The increase was mainly due to increasing expenditures on building and acquiring bus shelter advertising panels. The major acquisition of bus shelter advertising panels during the period has resulted in a negative free cash flow of HK$120 million (1H2005: positive free cash flow of HK$16.5 million). Free cash flow is defined as EBITDA before share compensation expense less cash outflow on capital expenditure, less income tax and net interest expense.

Trade Receivables

The Group's accounts receivable balance due from third parties was HK$280 million for the period under review, as compared to HK$236 million as at 31 December 2005. Cash collection during the first half of the year is typically lower and the average accounts receivable outstanding days were 149 days, on a time-weighted basis, as at 30 June 2006, as compared to 145 days of the same period last year. In addition, there were also some delays in payment from certain major customers and this has resulted in an increase in the balances owing for more than 180 days as compared with last year. As at 30 June 2006, the provision for doubtful debts increased by HK$5 million to HK$15.5 million to cover balances for which the Group has initiated legal proceedings and to cover other contingencies. Clear Media will continuously monitor the level of trade receivables and apply measures to reduce the trade receivables level. As at 30 June 2006, the amount due from Guangdong White Horse Advertising Company Limited was HK$27 million, as compared to HK$27 million as at 31 December 2005.

Prepayments, Deposits and Other Receivables

The Group's total prepayments, deposits and other receivables as at 30 June 2006 were HK$308 million as compared to HK$265 million as at 31 December 2005. The increase in total prepayments, deposits and other receivables was due to the placement of certain performance deposits and higher prepaid rental in accordance with the payment scheme.

Other Payables and Accruals

The Group's total payables and accruals for the interim period of 2006 were HK$207 million as compared to HK$175 million as at 31 December 2005. The increase was due mainly to the increase of capital expenditure payable. It would be inappropriate to give turnover days against sales as the payable is more closely related to capital expenditure incurred in relation to bus shelters.

Borrowings and Gearing

As at 30 June 2006, the Group had nil bank loans (2005: Nil) as we repaid all bank loans. The debt to equity ratio of the Group, defined as a percentage of net interest bearing borrowings over shareholders' funds, was at 19% as at 30 June 2006 (31 December 2005: 20%). As at 30 June 2006, the Group's total cash and bank balances amounted to HK$216 million (31 December 2005: HK$303 million).

Capital Expenditure

To strengthen the Group's leading position in China's outdoor media industry, the Group actively acquired concession rights and built bus shelters to expand its network of bus shelter advertising space. For the six months ended 30 June 2006, HK$212 million was spent on obtaining bus shelter concession rights and HK$3 million on fixed assets, as compared to HK$41 million and HK$2 million respectively for the same period last year.

Share Capital and Shareholder's Funds

During the six months ended 30 June 2006, the subscription rights attached to 15,987,000 share options were exercised at subscription prices ranging between HK$3.51 and HK$5.89 per share, resulting in the issue of 15,987,000 shares of HK$0.10 each for a total consideration, before expenses, of HK$81,634,000. As a result, Clear Media's issued and fully paid share capital increased slightly to 517,595,500 shares (1H2005: 501,608,500 shares). Equity attributable to equity holders of the parent as at 30 June 2006 increased by 9% to HK$1,683 million from HK$1,540 million as at 31 December 2005. During the six months under review, there was no share repurchase undertaken by Clear Media.

Material Acquisitions and Disposals

During the period under review, there were no material acquisitions or disposals of any subsidiary, associate or joint venture of the Group.

Exposure to Foreign Exchange Risk

Our only investment in China is the Group's operating vehicle, Hainan White Horse Advertising Media Investment Company Limited (the "WHA Joint Venture"), which conducts business only within China. Most of our turnover, capital investment and expenses are denominated in Renminbi, except for interest payable, repayment of foreign currency loans obtained to finance our operating vehicle's operations and any potential future dividend to be declared by our operating vehicle to shareholders. To date, we have not experienced any difficulties in obtaining governmental approvals for foreign exchange purposes when required. No financial instruments for hedging purposes were issued in the six months ended 30 June 2006.

Regarding the recent Renminbi appreciation, as we mentioned above, our turnover and costs are largely denominated in Renminbi, which will largely offset each other. However, as our net profit is denominated in Hong Kong Dollars, there will be some translation gain as a result of the Renminbi appreciation.

Employment, Training and Development

As at 30 June 2006, the Group had a total of 428 employees, an increase of 9% over the same period in 2005. The increase was largely due to the sales and marketing staff recruited to strengthen our sales capabilities to cultivate new clients and enhance existing client support. Total staff costs were approximately 11% of turnover, which increased by 23% compared to the same period last year, in order to retain and further incentivise our staff. As a matter of policy, employees are remunerated based on their performance, experience and the prevailing industry practices, with compensation policies and packages reviewed on a regular basis. Bonuses are linked to both the performance of the Group and to individual performance as recognition of value creation. Share options are also granted to senior management in an effort to align individual interests with the Group's.

Charge of Group Assets

During the period, Clear Media made certain arrangements to enable the provision of guarantees for the benefit of a third party in the ordinary course of business, amounting to HK$40 million (31 December 2005: Nil) as part of an acquisition. In connection with the arrangement, Clear Media pledged a fixed deposit of HK$40 million.

In addition, during the period, Clear Media had pledged time deposits of RMB30 million (approximately HK$29 million) as securities for bills payable of RMB20 million (approximately HK$19 million).

Capital Commitments

As at the balance sheet date for this interim period, the Group had capital commitments contracted but not provided for in relation to the construction of bus shelters amounting to HK$18 million, as compared to HK$45 million as at 31 December 2005.

Contingent Liabilities

On 10 August 1999, Advertasia Street Furniture Limited (“Advertasia”), an independent third party, commenced an action against China Outdoor Media Investment (Hong Kong) Company Limited (“China Outdoor Media (HK)”) (an indirect wholly owned subsidiary of Clear Media) in the High Court of Hong Kong pursuant to an agreement dated 21 April 1999 entered into by them for the sale of the entire issued share capital of four Hong Kong private companies by Advertasia to China Outdoor Media (HK) for the sum of HK$68 million (the “Agreement”). Advertasia alleged that China Outdoor Media (HK) had wrongfully, and in breach of the Agreement, refused to purchase the shares held by Advertasia in the four private companies and/or failed to tender a payment of HK$50 million in relation to the Agreement. On 28 November 2001, (i) Outdoor Media China, Inc. (“OMC”), a company incorporated under the laws of Western Samoa with limited liability and a substantial shareholder with a 3% interest in Clear Media, (ii) Han Zi Jing, one of the directors of Clear Media, (iii) Clear Channel Outdoor, Inc. (“CCO”), one of the substantial shareholders of Clear Media, (iv) China Outdoor Media (HK) and (v) Clear Media, entered into a Deed of Indemnity (as amended, the “Deed of Indemnity”). Under the terms of the Deed of Indemnity, OMC and CCO have covenanted and undertaken to indemnify Clear Media and the Group against all claims (including this claim), whether or not successful, compromised or otherwise settled, and any actions, damages, penalties, liabilities, legal fees, enforcement costs and expenses incurred by Clear Media and the Group in respect of the claims. On 8 October 2004, the High Court, acting as a court of first instance, made an order in favour of Advertasia. Clear Media made an appeal against the judgment of the High Court.

In January 2005, China Outdoor Media (HK) paid to the High Court the sum of HK$100 million in respect of the aforementioned Advertasia claim, and this amount of money will remain at the High Court until the final result of the appeals to the courts. The Group is still entitled to the deposit and will receive interest at market deposit rates during the period. Moreover, under a Deed of Indemnity between Clear Media, Outdoor Media China Inc., Han Zi Jing, Clear Channel Outdoor, Inc. and China Outdoor Media (HK), Clear Media and China Outdoor Media (HK) will be fully indemnified against all damages, penalties, liabilities, legal fees, enforcement costs and expenses incurred by them in respect of this claim.

A judgment of the Court of Appeal was made on 7 October 2005 and the appeal was dismissed. A Notice of Appeal was filed by China Outdoor Media (HK) on 8 December 2005 with the Court of Final Appeal, and the case was filed with the Court of Final Appeal on 16 February 2006.

Outlook

Looking ahead, we expect consumer spending and the advertising market in China to improve gradually. If current circumstances remain unchanged, we expect our core bus shelter advertising business to continue to improve in the latter half of the year based on the order book on hand. The second half is traditionally the peak advertising season and we believe that our year-end results will reflect this industry trend. We expect to continue to grow profitably in volume from major advertisers as well as aggressively pitch to small/medium advertisers via all our nine sales centers nationwide. With the completion of the bus shelter conversion in Shanghai, we expect that these new scrolling panels will contribute to the Group's sales revenue in the second half of the year. We will continue to integrate the advertising panels acquired in Beijing and focus on enhancing their returns to a level comparable to our existing network. We will also continue to set up more sales centers in mid-tier cities to enhance our customer support as well as to strengthen our sales presence on a regional basis to cater to the various needs of our new and existing clients.

We are also in the process of finalising our multi-year Olympic sales packages, which we intend to launch in the second half of the year in order to capture the advertising opportunities arising from the 2008 Beijing Olympics Games.