

# Management Discussion and Analysis

## FINANCIAL REVIEW

### Overall Performance

The Group recorded a profit attributable to shareholders of HK\$424 million (2002: HK\$555 million), a decline of 24%. The steeper decline in profit was attributable mainly to the anticipated increase in depreciation and in-orbit insurance upon commissioning of AsiaSat 4, the decrease in turnover and an additional provision of deferred tax for prior years as a result of the increase in tax rate.

### Turnover

Turnover for the year fell by 6% to HK\$896 million (2002: HK\$951 million). This was due largely to slower than expected growth, loss of customers on contract renewals and continued pricing pressure both on new leases and renewals.

### Cost of Services

Cost of services was HK\$313 million (2002: HK\$243 million), an increase of HK\$70 million, or 29%. The increase arose largely from the depreciation and in-orbit insurance of AsiaSat 4.

### Other Operating Income

Other operating income amounted to HK\$0.9 million (2002: Nil), most of which arose from the provision of in-orbit service support.

### Interest Income

Interest of HK\$5 million (2002: HK\$6 million) was generated on short-term deposits from funds on hand.

### Administrative Expenses

Administrative expenses decreased to HK\$56 million (2002: HK\$77 million), a decrease of HK\$21 million or 27%. The decrease was due largely to a reduction in performance bonuses and reversal of provision for doubtful debts.

### Finance Costs

Finance costs amounted to HK\$3 million (2002: Nil), which arose from the loan facility arranged for AsiaSat 4. Prior to the commencement of commercial operation of AsiaSat 4, these finance costs were capitalised.

### Share of Results of Associates

The share of loss from an associate, including amortisation of goodwill, amounted to HK\$16 million (2002: HK\$14 million).

### Impairment Loss

Impairment loss recognised during the year amounting to HK\$2 million (2002: Nil) arose from the write off of the goodwill in an associate, SpeedCast Holdings Limited.

# Management Discussion and Analysis

## FINANCIAL REVIEW (CONTINUED)

### Taxation

The rate for Hong Kong Profits Tax for corporations was raised from 16% to 17.5% with effect from 1st April, 2003. As a result, the Company had to make an additional provision of HK\$17 million on deferred tax for prior years.

### Financial Results Analysis

The financial results are highlighted below:

		<b>2003</b>	2002	% Change
Turnover	HK\$M	<b>896</b>	951	-6
Profit attributable to shareholders	HK\$M	<b>424</b>	555	-24
Dividend (excluding special dividend)	HK\$M	<b>125</b>	98	+28
Capital and reserves	HK\$M	<b>3,568</b>	3,347	+7
Earnings per share	HK cents	<b>109</b>	142	-23
Dividend per share (excluding special dividend)	HK cents	<b>32</b>	25	+28
Dividend cover before special dividend	Times	<b>3</b>	6	-50
Special dividend per share	HK cents	<b>Nil</b>	25	N/A
Return on shareholders' funds	%	<b>12</b>	17	-29
Net assets per share - book value	HK cents	<b>914</b>	858	+7

## LIQUIDITY AND FINANCIAL RESOURCES

### Sources of Financing

The Group's principal use of capital during the year under review was the capital expenditure related to the construction of AsiaSat 4. In addition, the Group also made progress payments for the construction of the telemetry, tracking and control facilities at the Company's new Tai Po Earth Station. These payments were financed through cash flow generated from operating activities.

On 24th November, 2000, the Company and its subsidiary, AsiaSat, entered into an agreement with a consortium of banks to provide a secured term loan credit facility of US\$250 million (the "Loan Facility") with a grace period of three years for drawdown. Since no drawdown was made the Loan Facility automatically lapsed on 24th November, 2003. Cash flow generated from operating activities, was more than sufficient to meet the capital expenditure of AsiaSat 4 and other projects. At 31st December, 2003, there was no outstanding bank loan.

## Management Discussion and Analysis

### **CAPITAL STRUCTURE**

#### **Funding and Treasury Policy**

The Group adopts conservative treasury policies and exercises tight control over its cash and risk management. Cash is generally placed in short-term deposits denominated in U.S. Dollars to meet its payments. Hong Kong Dollar is pegged to U.S. Dollar at the exchange rate of HK\$7.80 to US\$1.00. The exchange movement has been kept within a narrow band. Therefore, the Group does not have any significant currency exposure.

#### **Financial Instruments for Hedging**

Since almost all the revenue of the Group is in U.S. Dollars there is no need to hedge its liabilities, which are also substantially denominated in U.S. Dollars.

#### **Foreign Currency Investment**

The Group does not have any material investment in currencies other than in U.S. Dollars or Hong Kong Dollars.

### **ORDER BOOK**

At 31st December, 2003, the value of contracts on hand amounted to HK\$3,720 million (2002: HK\$4,029 million), the majority of which will be realised over the next few years. Almost all the contracts are denominated in U.S. Dollars.

### **SIGNIFICANT INVESTMENTS, THEIR PERFORMANCE AND FUTURE PROSPECTS**

The Group maintained its interest in SpeedCast Holdings Limited ("SpeedCast") at 45.3%. SpeedCast provides three major services: broadband, corporate broadcast and multimedia.

For the year 2003, SpeedCast increased its turnover to HK\$28 million (2002: HK\$12 million), an increase of 133%. However, the company still incurred a loss of HK\$40 million (2002: HK\$49 million), an improvement of 18%. With increase in turnover, the loss is expected to reduce in the years to come.

At 31st December, 2003, the book value of the investment in SpeedCast has been written down to zero.

### **MATERIAL ACQUISITIONS AND DISPOSALS OF SUBSIDIARIES AND ASSOCIATED COMPANIES**

During the year, there were neither material acquisitions nor disposals of subsidiaries and associated companies.

### **SEGMENT INFORMATION**

The turnover of the Group, analysed by location of customers, is disclosed in note 4 to the financial statements.

## Management Discussion and Analysis

### **EMPLOYEES AND REMUNERATION POLICIES**

At 31st December, 2003, the Group had 83 permanent staff (2002: 83).

The Group considers its human resources as one of its most valuable assets. The talent pool that the Group draws from overlaps with the telecommunications, information technology and some high-tech equipment vendor industries.

The Group has established a performance based appraisal system. The present remuneration package consists of salaries, housing benefits (applicable to certain grades of employees), performance bonuses, share options (again applicable to certain grades of employees) and fringe benefits that are compatible with the market.

Pursuant to the Company's new share option scheme adopted on 25th January, 2002 (the "Share Option Scheme"), the Board of Directors of the Company may grant options to any employees (including officers and directors) of the Company or any of its subsidiaries to subscribe for shares in the Company. The subscription price shall be such a price as the Board of Directors of the Company may in its absolute discretion determine at the time of grant but the subscription price shall not be less than whichever is the higher of (i) the closing price of the shares as stated in The Hong Kong Stock Exchange Limited's (the "Stock Exchange") daily quotations sheet on the date of grant; (ii) the average closing price of the shares as stated in the Stock Exchange's daily quotation sheets for the five business days immediately preceding the date of the grant; or (iii) the nominal value of a share.

The Group does not operate an in-house regular training programme. However, the Group does provide ad hoc training on new developments/facilities and sponsors employees to attend external vocational training that is relevant to their jobs and their career progression.

### **CHARGES ON GROUP ASSETS**

With the lapse of the US\$250 million loan facility on 24th November, 2003, the securities that were pledged to the banks are being released. There are no other charges on any of the Group's assets.

### **CAPITAL COMMITMENTS**

Details of the capital commitments of the Group are set out in note 25 to the financial statements.

At 31st December, 2003, the Group had total capital commitments of HK\$49 million (2002: HK\$286 million), of which HK\$21 million (2002: HK\$219 million) was contracted for but not provided in the financial statements, and the remaining HK\$28 million (2002 HK\$67 million) was authorised by the Board but not yet contracted.

### **GEARING RATIO**

At 31st December, 2003, the Company had no debt. Hence, the gearing ratio was zero.

## Management Discussion and Analysis

### EXCHANGE RATES AND ANY RELATED HEDGES

During the year, almost all of the Group's revenues, premiums for satellite insurance coverage and debt service, and substantially all capital expenditure were denominated in U.S. Dollars. The Group's remaining expenses were primarily denominated in Hong Kong Dollars. At 31st December, 2003, almost all the Group's transponder utilisation agreements, transponder purchase agreements, borrowings, obligations to construct and launch satellites, and to purchase telemetry, tracking and control equipment were denominated in U.S. Dollars. Hence, the Group does not have any significant currency exposure and does not need to hedge.

### CONTINGENT LIABILITIES

At 31st December, 2003, the Group had significant contingencies as follows:

Under Indian tax regulations, the Group may be subject to Indian income tax on revenues received by the Group in respect of income from provision of satellite transponder capacity to the Group's customers for purposes of those customers carrying on business in India or earning income from any source in India.

The Indian tax authorities assessed the Group (including interest as of 21st March, 2001) for income tax of approximately HK\$21 million (INR131 million) for the assessment year 1997-1998 and approximately HK\$23 million (INR141 million) for the assessment year 1998-1999. No assessment has yet been made for the 1999-2000, 2000-2001, 2001-2002, 2002-2003 or 2003-2004 assessment years.

The Group filed appeals for each of the assessment years 1997-1998 and 1998-1999. The Indian tax authorities initiated tax recovery measures against the Group in January 2002. In order to expedite the legal proceeding in India and obtain a stay of the recovery measures, the Group made a tax payment totalling approximately HK\$19 million (INR120 million) to the Government of India.

The Income Tax Appellate Tribunal (the "Tribunal") in the appeal filed for the assessment year 1997-1998 held that the Group is liable for Indian income tax under certain circumstances. The Tribunal directed the Indian tax authorities to make a fresh computation of the taxable income. Pursuant to the order of the Tribunal, the tax authorities have prepared a revised computation of tax due on 30th May, 2003. The revised assessment is approximately HK\$20 million (INR115 million). The Group does not believe that it is liable for the Indian income tax as held by the Tribunal and has filed an appeal against the Tribunal's decision. The tax authorities have also filed an appeal against the Tribunal's decision. Both the appeals have been admitted by the High Court.

In order to obtain a stay of recovery proceedings, the Group has made a further payment of approximately HK\$5 million (INR30 million). An additional payment of approximately HK\$1.3 million (INR7.5 million) was made subsequent to the balance sheet date.

### **CONTINGENT LIABILITIES (CONTINUED)**

In addition, based on the general principles set forth by the Tribunal, the amount of income taxable in India depends on the payments made by the Group's customers to the Group for the purpose of those customers carrying on business in India or earning income from any source in India. As such information is proprietary in nature and has not been provided by the Group's customers, the Group cannot reasonably estimate the taxable income. Furthermore, as stated above, the Group has filed an appeal against the Tribunal's decision. The appeal has been admitted by the High Court and is pending before the Court. Accordingly, no provision has been recognised for Indian income tax in the Group's consolidated financial statements.

### **CRITICAL ACCOUNTING POLICIES**

The Company's consolidated financial statements are prepared in accordance with Hong Kong GAAP. The preparation of these consolidated financial statements requires the Company to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses as well as the disclosure of contingent assets and liabilities. The Company continually evaluates these estimates and judgments, including those related to estimated useful lives of satellites, impairment losses on satellites, allowance for doubtful accounts, and contingent liabilities related to tax assessments from Indian tax authorities. The Company bases these estimates and judgments on its historical experience and other factors that it believes to be reasonable under the circumstances. Actual results may differ from these estimates under different assumptions or conditions. The Company has identified below the accounting policies that are the most critical to its consolidated financial statements.

#### **Useful lives of in-orbit satellites**

The Company's operations are capital intensive and it has significant investments in satellites. The carrying value of the Company's in-orbit satellites (AsiaSat 2, AsiaSat 3S and AsiaSat 4) represented 72% of its total assets as of 31st December, 2003 (31st December, 2002: 39%). The Company estimates the useful lives of satellites in order to determine the amount of depreciation expense to be recorded during the reported period. The useful lives are estimated at the time satellites are put into orbit and are based on historical experience with other satellites as well as the anticipated technological evolution or other environmental changes. If technological changes were to occur more rapidly than anticipated or in a different form than anticipated, the useful lives assigned to these satellites may need to be shortened, resulting in the recognition of increased depreciation in a future period. Similarly, if the actual lives of satellites are longer than the Company has estimated, the Company would have a smaller depreciation expense. As a result, if the Company's estimations of the useful lives of its satellites are not accurate or are required to be changed in the future, the Company's net income in future periods would be affected.

### **CRITICAL ACCOUNTING POLICIES (CONTINUED)**

#### **Realisability of the carrying amounts of long-lived assets**

The Company is required to evaluate at each balance sheet date whether there is any indication that the carrying amounts of long-lived assets (primarily its satellites) may be impaired. If any such indication exists, the Company should estimate the recoverable amount of the long-lived assets. An impairment loss is recognised for the excess of the carrying amount of such long-lived assets over their recoverable amounts. The value in use is the discounted present value of the cash flows expected to arise from the continuing use of long-lived assets and cash arising from its disposal at the end of its useful life. The estimates of the cash flows are based on the terms and period of existing transponder utilisation agreements (“Existing Agreements”).

Modifications to the terms of the Existing Agreements that result in shorter utilisation periods than previously agreed and/or those that result in the reduction in agreed rates will result in a lower recoverable amount (if the discount rate used is not changed); which may, in turn, result in a situation wherein the recoverable amounts are less than the carrying amounts (therefore, an impairment loss would need to be recognised).

#### **Allowance for doubtful accounts**

The Company maintains allowance for doubtful accounts, and for estimated losses that result from the inability of its customers to make the required payments. The Company bases its allowances on the likelihood of recoverability of account receivables based on past experience and current collection trends that are expected to continue. The Company’s evaluation also includes the length of time the receivables are past due and the general business environment.

If changes in these factors occur, or the historical data the Company uses to calculate the allowance for doubtful accounts as of 31st December, 2003 does not reflect the future ability to collect outstanding receivables, additional provisions for doubtful accounts may be needed and the Company’s future results of operations could be adversely affected.

#### **Contingency related to Indian tax assessments**

The issue of Indian tax was covered under Contingent Liabilities above.