
BUSINESS OF THE GROUP

INTRODUCTION

The Group is principally engaged in the provision of enterprise solutions with a focus on online payment and logistics. The Group's enterprise solutions are principally provided to enterprises in the PRC to enable them to conduct online payment and logistics processes. The Group had registered the software copyright of its proprietary software systems for Internet payment service with the relevant PRC authority in August 2001. The Directors believe that its enterprise solutions with a focus on online payment and logistics can effectively assist enterprises in tackling the issues arising from payment and logistics requirements for their e-commerce operations and therefore could form a critical part of their e-commerce strategy.

Combining its technical and application expertise together with the software components developed on its own and other third parties' products, the Group provides enterprise solutions with a focus on online payment and logistics. The third parties' products used in providing the Group's enterprise solutions comprise mainly software packages. The Group's services in this regard include consulting, system design, system integration, implementation and maintenance. In April 2001, the Group entered into agreements with two software developers, namely SLI and EXE, to act as the exclusive value-added reseller of the logistics software in the Greater China Region of SLI and as a non-exclusive value-added reseller in the PRC (and to the clients worldwide to whom iLogistics China provides services) of EXE respectively. Being a value-added reseller, the Group uses the software packages of SLI or EXE as components to build logistics solutions and provide the solution, together with value-added services such as system design, implementation and maintenance, to its clients.

The Directors believe that the Internet as an interface between buyers, sellers and various service providers has changed the competitive landscape of the commercial world. Whilst the Internet has, to a large extent, resolved the problem of information flow, the task of facilitating efficient fund flow and merchandise flow remains an obstacle to the development of e-commerce. To solve the fund flow problem, the role of traditional financial institutions will remain important. At the same time, the Directors foresee a high demand for technical support to handle the business volume generated by e-commerce operations. The Directors believe that payment and logistics solution providers with the necessary technical expertise would be able to capitalise on the opportunity by providing online payment and logistics related services.

The Group has built a professional R&D team with expertise and experience in e-commerce related areas. Most of the R&D staff are university graduates and have years of experience relating to e-commerce solutions. In addition, the Group utilises external resources to efficiently enhance its R&D capabilities. The Group has engaged Shanghai Jiao Tong University in the PRC, Professor Cheng Yurong of Tsinghua University in the PRC and Mr. Li Ye, an e-commerce consultant, to conduct research on the regulatory, market and technological environment of online payment and logistics business in the PRC. Each of the engagement with Shanghai Jiao Tong University, Professor Cheng Yurong and Mr. Li Ye has a term of one year up to 24th March, 2002, 31st October, 2002 and 22nd March, 2002 respectively.

MISSION

The mission of the Company is *“to provide online payment and logistics enterprise solutions to enable clients to increase operating efficiency and to extend coverage of services via the Internet”*.

ENTERPRISE SOLUTIONS

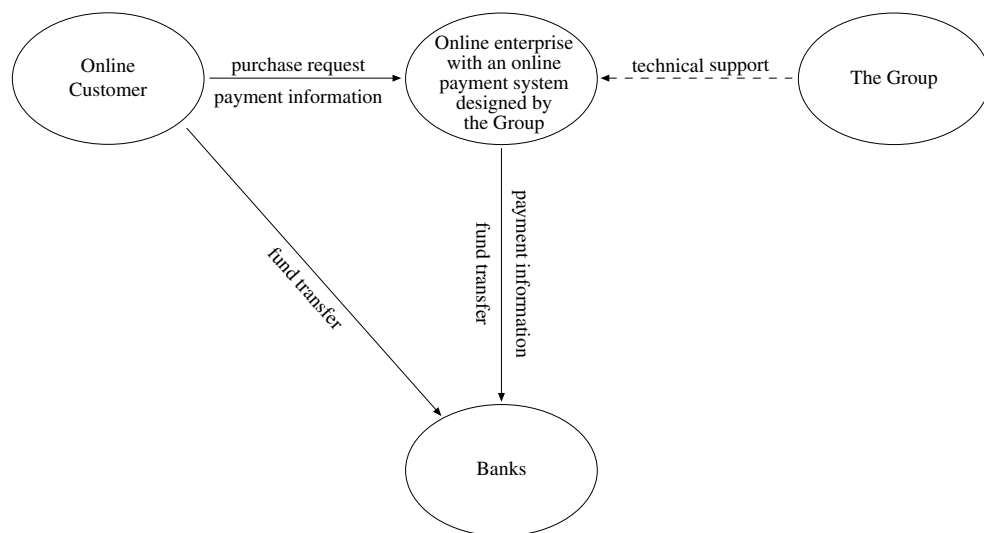
Online Payment Solutions

The Company, through iPayment China, provides online payment enterprise solutions. Typically, the payment process of the client involves receiving payment instructions via the Internet, processing and verifying the relevant instructions and data and effecting fund transfer from the bank account of online customers to the online enterprises. Depending on the requirements of the online enterprise, the fund transfer can be conducted on a real time basis or by batch. Such services of the Group are primarily for enterprises with operations that process payment instructions online. The clients may choose banks and payment services providers such as Visa and MasterCard, through which payment by its customers is allowed. The Group then designs and implements the required system for processing payment requests and settlement procedures based on IPRS and IPSVAS. The Group also assists the client to liaise and establish the necessary interface with relevant bank. Project income for designing, licensing and implementing the online payment system is determined according to the time and material required to complete the project, its complexity, and resources available to the Group during the time of implementation, and is payable at pre-agreed stages of implementation. Typically, these pre-agreed stages of implementation include analysis on the needs of the clients, completion of technical proposals, development of the enterprise solutions and acceptance by the clients.

The Group also provides ongoing technical support services to its clients who use the Group's online payment enterprise solutions. Currently, clients using the Group's online payment enterprise solution are engaged in a variety of businesses including trading, customs application and raw material purchasing. Such ongoing technical support services include maintaining and providing configuration on the servers and payment system; constructing and managing the database; upgrading the payment software system; monitoring security; training the technical staff members of the clients; and any other relevant technical support requested by the clients. The fee is typically calculated based on usage of the related system and a fixed unit charge per transaction. The charge per transaction is determined with reference to the nature and volume of the online operation of the client and on a case by case basis. As part of its services, the Group monitors the payment system and its transaction record on an ongoing basis by way of accessing its server and database. At the same time, the Group can ensure that the fees payable to the Group for the ongoing technical support services are consistent with the transactions actually performed via the system.

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The following diagram illustrates a typical payment mechanism for a transaction using a customised online payment enterprise solution as an online payment platform.



As at the Latest Practicable Date, the Group was executing one online payment enterprise solution project.

Logistics Enterprise Solutions

The Group also provides logistics enterprise solutions to enable enterprises to enhance their operating efficiency in the PRC. The Group usually builds logistics and related system solutions for its clients based on iwareZ, the software packages developed by the Group. The iwareZ package provides a simplified Chinese interface. Currently, the iwareZ product suite comprises seven applications specifically designed to enhance logistics and the related ERP capability of an enterprise. The functions of the applications comprising the iwareZ series include warehouse management, integrated ERP management, sales management, MRP management, purchase management, and financial and human resources management. The Group also uses products of other third parties for developing logistics enterprise solutions. Products of third parties used by the Group comprise mainly software packages developed by other software developers. Project income for designing and implementing the system is determined according to the time and material required to complete the project, its complexity, and resources available to the Group during the time of implementation, and is payable at pre-agreed stages of implementation. Typically, these pre-agreed stages of implementation include analysis on the needs of the clients, completion of technical proposals, development of the enterprise solutions and acceptance by the clients.

As at the Latest Practicable Date, the Group was executing one logistics enterprise solution project.

Business partners

It is the Group's strategy to form alliances with overseas logistics solution providers. The Group has entered into agreements with SLI and EXE to act as their value-added reseller in the Greater China Region and the PRC (and to the clients worldwide to whom iLogistics China provides services) respectively. Being a value-added reseller, the Group uses the software packages of SLI or EXE as components to build logistics solutions and provide the solution, together with value-added services such as system design, implementation and maintenance, to its clients.

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Pursuant to the agreement entered into by the Group and SLI on 17th April, 2001, the Group was granted the exclusive rights to act as value-added reseller to market and supply the SLI software products together with the Group's value-added services such as system design, implementation and maintenance in the Greater China Region, for a term of one year starting from the date of the agreement. This agreement is renewable automatically for additional periods of one year at the time of each anniversary. Under the agreement, the Group shall pay SLI a license fee for each unit of the software products sold and distributed by the Group and the Group will be entitled to the selling price net of license fee payable to SLI. Such selling price is inclusive of the project fees charged by the Group for the provision of logistics solution. SLI is a logistics solutions provider in South Korea. Established in 1997, SLI is principally engaged in the consultancy and provision of logistics information system and third party logistics. SLI developed logistics solution with the assistance of the Ministry of Information & Telecom of South Korea in 1998. SLI was identified as a business partner of the Group for its logistics software business due to SLI's expertise in developing logistics software packages and its existing products, which can be modified for sales in the PRC market.

Pursuant to the agreement entered into by the Group and EXE on 18th April, 2001, the Group was granted the non-exclusive rights to act as value-added reseller to market and supply the EXE software products together with the Group's value-added services such as system design, implementation and maintenance in the PRC and to the clients worldwide to whom iLogistics China provides services, for a term of two years commencing from the date of the agreement. This agreement is renewable automatically for additional periods of one year at the time of each anniversary. Under the agreement, the Group shall pay EXE a license fee for each unit of the software products sold and distributed by the Group. Such selling price is inclusive of the project fees charged by the Group for the provision of logistics solution. EXE is a logistics solutions provider based in Korea, and it is a wholly owned subsidiary of EXE Technologies Inc., whose shares are listed on Nasdaq. EXE's logistics software products allow companies to efficiently manage and control the flow of inventory throughout the supply chain using the Internet and traditional communication methods.

Implementation of Online Payment and Logistics Enterprise Solutions

Upon the request of a potential client, both the Group's marketing and technical staff first assesses the requirements and the client's needs and produces a proposal to the clients. The Group then liaises with the client to refine the proposal. After the terms and scope of the services have been agreed, the technical department produces a more specific technical proposal and implements the required system in accordance with the agreed time schedule. The design and implementation stages usually take between two to seven months. After completing the implementation, a user acceptance test is undertaken before concluding the project. Typically, the client is required to pay 10% of the contract sum within 15 days after the signing of the contract. Balance of the payment for the system solution and related services typically falls due within two months after the completion of user acceptance test. Clients are also usually given a credit period of 30 days. The Group also provides training to its clients to ensure smooth operation of the system installed.

As far as logistics enterprise solutions are concerned, the Group provides system maintenances services during the first year from the installation based on the original contract with a maintenance fee representing a percentage of the contract sum. After the first year, maintenance services can be provided at the clients' option with a fee also representing a percentage of the original contract sum.

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As for online payment enterprise solutions, ongoing technical support is provided to the client for a technical support fee, which is calculated depending on the usage of the system implemented by the Group and are payable to the Group on a monthly basis. The after sales services typically include user training, technical support via phone and diagnosis via the Internet. Other technical support such as upgrade of the software package can be provided by the Company, if required.

MARKETING

The Company believes that the overall image of the Group will be crucial for its further development and that aggressive marketing and promotional programs are necessary to build the Group's brandname. Such marketing and promotional activities may include public educational seminars, advertisements, the provision of a demonstration version of online payment and logistics software system and participation in industry or technology related exhibitions.

Major Group marketing activities mainly comprise:

Direct Marketing – One of the most important marketing efforts of the Group in direct marketing is to target prospective clients in the PRC when the Group carries out on-site demonstrations of functions of the Group's solutions and services. To this end, the Group has held numerous meetings with banks and with enterprises in the PRC having online operations and it will continue to do so.

Joint marketing program – The Group entered into memoranda of understanding with three software developers, namely 深圳時代飛揚軟件有限公司 (Shenzhen Infoage Software Co., Ltd.), 深圳市峰杰數字網絡技術有限公司 (Shenzhen Feng Jie Digital Network Technology Co., Ltd.) and Qiva Inc., on 27th February, 2001, 15th March, 2001 and 18th July, 2001 respectively and a telecommunication services provider, namely 上海潤訊通信發展有限公司 (Shanghai China Motion Telecommunication Development Co., Ltd.), on 29th March, 2001 in the PRC in order to take advantage of the existing joint marketing and cross referral opportunities.

Press promotion – The Group places advertisements in the press from time to time.

www.ilogistics.com.cn and *www.ipayment.com.cn* – The Group's web-sites, *www.ipayment.com.cn* and *www.ilogistics.com.cn*, are designed to promote its enterprise solutions and related services.

Industry/technology exhibition – Participation in industry/technology exhibitions is regarded as another effective channel to promote the Group's brand name and image among prospective users and industry practitioners and to make initial introductions of its services. For example, the Group participated in "Comdex China 2001" in Beijing in April 2001 and the CeBIT Asia 2001 exhibition held in Shanghai in August 2001.

Strong support services for users – Complementary to its aggressive promotion activities, strong customer support for its clients is necessary to encourage online enterprises to use the Group's services. The following services and support programmes are provided by the Company to all online enterprises:

- Technical staff to answer questions regarding technical functions relating to the Group's enterprise solutions during implementation.

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- Training for new clients to cover the installation and explanation of the functions of the Group's enterprise solutions.
- A system for receiving comments from online enterprises, and a carefully-planned internal follow-up to provide rapid responses.
- Continuous R&D of the Group's enterprise solutions.

As at the Latest Practicable Date, the Group has 15 marketing professionals based in Shanghai to carry out marketing functions, whilst the marketing activities took place mainly in Shanghai, Beijing and Shenzhen.

For the year ended 31st March, 2000, no marketing cost was incurred by the Group. For the year ended 31st March, 2001, the Group incurred marketing costs of approximately HK\$22,000.

CLIENTELE

Currently, the Group's clients are enterprises in the PRC using the Group's online payment and logistics solutions. During the year ended 31st March, 2001, all clients of the Group were PRC companies and all payments to the Group were made in Renminbi. During the year ended 31st March, 2000, all clients of the Group were in Hong Kong and all payments to the Group were made in Hong Kong dollars. The five largest clients, who were independent third parties, accounted for approximately 65.8% and 57.1% respectively of the Group's turnover for each of the two years ended 31st March, 2001. The largest clients accounted for approximately 19.6% and 25% respectively of the Group's turnover for each of the two years ended 31st March, 2001. Sales to the five largest clients for each of the two years ended 31st March, 2001 were related to Internet related enterprise solutions in Hong Kong and trading of computer hardware in the PRC respectively. For the year ended 31st March, 2000, the Group had 27 projects relating to Internet related enterprise solutions in Hong Kong. For the year ended 31st March, 2001, the Group had 5 projects relating to online payment and logistics enterprise solutions in the PRC. None of the Directors, nor any shareholder of the Company who will be interested in more than 5% of the issued share capital of the Company immediately following the Capitalisation Issue and the Placing (but taking no account of any Shares which may be allotted and issued upon the exercise of the Over-allotment Option, and any options granted or which may be granted under the Pre-IPO Share Option Schemes and the Share Option Scheme) or their respective associates has had any interest in any of the Group's five largest customers during the two years ended 31st March, 2001.

The Group generally provides credit terms of 30 days to its clients using its enterprise solutions and delivers hardware on a cash on delivery basis. The credit terms and limits for each client have to be reviewed and approved by a director. As at the Latest Practicable Date, the Group had encountered no debt collection problems and has, therefore, not been required to make any provision for bad and doubtful debts.

SUPPLIERS

Since August 2001, the Group purchases logistics software packages supplied by SLI and EXE. Other than the agreements with SLI and EXE, the Company has entered into no long term contracts with any of its suppliers and all purchases of software packages are made on an order by order basis according to the needs of the Company's clients. In view of the supply and diversity of the software offered in the market and the software component development capacity of the Group, the Directors believe that even without the supplies from SLI and EXE, the Group will have no difficulty in meeting its clients' demands for software solutions. The Group has experienced no major difficulties in obtaining an adequate supply of products to meet its own needs.

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Purchases from the five largest suppliers, who were independent third parties, accounted for approximately 91.1% and 96.5% respectively of the Group's purchases for each of the two years ended 31st March, 2001. The largest supplier accounted for approximately 40.7% and 52.5% respectively of the Group's purchases for each of the two years ended 31st March, 2001. Settlements to the five largest suppliers for each of the two years ended 31st March, 2001 were made in Hong Kong dollars and Renminbi respectively and either by letter of credits or on cash-on-delivery basis. None of the Directors, nor any shareholder of the Company who will be interested in more than 5% of the issued share capital of the Company immediately following the Capitalisation Issue and the Placing (but taking no account of any Shares which may be allotted and issued upon the exercise of the Over-allotment Option, and any options granted or which may be granted under the Pre-IPO Share Option Schemes and the Share Option Scheme) nor any of their respective associates has had any interest in any of the Group's five largest suppliers during the two years ended 31st March, 2001.

RESEARCH AND DEVELOPMENT

The Group positioned itself as an online payment and logistics enterprise solutions provider. Accordingly, the R&D efforts of the Group concentrate on these two areas. The Group's R&D strategies are:-

- (1) **development of software components for online payment and logistics enterprise solutions.** These components are designed to have core functions but may be modified for integration into various existing IT system or systems under development. By using these modules, the Group can shorten the development time for its clients' desired system and maintain a high quality for these systems.
- (2) **development of services platform for value-added services.** As stated in the section headed "Future plan and prospects", the Directors believe that the Group will be in an advantageous position to provide other e-commerce enabling services. Building on IPRS and IPSVAS, the Group intends to provide value-added services in the future including provision of e-marketplace, provision of services to support usage of e-cash, e-cheque and e-cert.

As at the Latest Practicable Date, the R&D team comprises 13 technical staff members, with 9 focusing on online payment enterprise solutions and 4 focusing on logistics enterprise solutions. The team is led by Mr. Liu Yun, who has over six years of experience in the areas of Internet, software and computer systems, Mr. Liu graduated from Chongqing University in the PRC with professional qualifications in Computer Science. The remaining 12 members of the R&D team are also experienced in the areas of Internet and e-commerce.

The Group has been utilising external sources of R&D expertise in developing its own capabilities. In March 2001, the Group engaged Shanghai Jiao Tong University to carry out in-depth research in various research topics relating to logistics and IT systems security. The research team is currently looking into the following areas:-

- Encryption methodology
- Internet security analysis
- Firewall and anti-hacking technology
- Real time monitoring of and alarm system for Internet traffic
- Applications for e-commerce
- Market for the provision of logistics solutions in the PRC
- Localisation of foreign logistics software packages and user interface
- Implementation of logistics solutions

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Pursuant to the agreement with Shanghai Jiao Tong University, the Group is required to pay Shanghai Jiao Tong University a fee of Rmb1,000,000 by installments for its research. The agreement is for a term of one year from 25th March, 2001 to 24th March, 2002.

In addition, the Group has engaged Professor Cheng Yurong from the Centre for Software Technology of Tsinghua University in the PRC and Mr. Li Ye, an e-commerce consultant, as consultants to advise the Group on market conditions and technical aspects of IT systems security and logistics solutions. Pursuant to the agreements with Professor Cheng Yurong and Mr. Li Ye, the Group is required to pay to each of them a fixed fee for their services. The agreements are from 1st November, 2000 to 31st October, 2002 for Professor Cheng Yurong and from 23rd March, 2001 to 22nd March, 2002 for Mr. Li Ye.

Based on the best estimation of the Directors, for each of the two years ended 31st March, 2001, the costs incurred for R&D activities amounted to approximately HK\$229,000 and approximately HK\$366,000 respectively. All R&D expenses of the Group have been expensed as incurred.

COMPETITION

As for the business of the provision of online payment enterprise solutions, the Directors believe that the Group's competitive strengths are its technical expertise and its relationships with various banks. The Directors believe that there are a number of IT companies providing customised enterprise solutions in all the major cities of the PRC. However, the Directors believe that there are only a limited number of IT companies in the PRC which specialise in online payment solutions. Therefore, the Directors consider that direct competition with the Group's online payment solutions are not intense currently. Although the Group does not enter into contracts with the banks for the operation of the payment system of its clients, the Group has developed working relationships with these banks through the provision of marketing and technical support to the Group's clients using its online payment enterprise solutions. On assisting clients to connect to the payment system of banks for facilitating fund transfer, the Group is actively involved in the discussion between the client and its bankers as technical advisors. The Directors consider that, because of its relationship with the banks, the Group is in a position to assist its clients to negotiate with the banks to establish a direct interface between prospective client and the banks concerned.

As for the business of providing of logistics enterprise solutions, the Directors believe that a number of international and local consultancy firms and software houses already exist which provide logistics solutions in the PRC with a wide range of solutions of different levels of complexity and accordingly with different pricing levels. The Directors believe that one of the competitive advantages of the Group lies in its existing online payment and logistics software components developed and based on a local application environment. The Directors believe that together with the software package developed by the Group and the localised version of products of SLI and EXE, the dedication and expertise of its management and staff, the Group is well positioned to provide logistics solutions to its clients.

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INTELLECTUAL PROPERTY RIGHTS

Software library

Since its establishment, the Group has been developing a software library comprising software solutions for various types of applications. The Group utilises its software library to create system solutions to meet the needs of its clients. The Directors believe that as the Group continues to build up its software library, it will be able to reduce the cost of designing and implementing new solutions and improve the quality of the Group's solutions and its delivery times.

Protection of proprietary rights

The Group seeks to protect its proprietary rights through registration and contractual protection such as non-disclosure agreements with its suppliers, clients, industry players and employment contracts including confidentiality terms for its employees. However, the Group cannot guarantee that the steps it has taken so far to protect its proprietary rights will be adequate to deter misappropriation of the Group's interests. Furthermore the Group may not be able to detect any unauthorised use and so take appropriate steps to enforce fully its proprietary rights.

iPayment China has also registered its proprietary software systems for Internet payment service with the National Copyright Administration of the People's Republic of China as the copyright owner.

Patents

The Group has not applied for any patents for any of its solutions. The Directors consider that the agreements with confidentiality clauses between the Group and its clients should provide a reasonable level of protection for the Group's intellectual property rights.

Trademarks

The Group has registered and applied for the registration of its trademarks, details of which are referred to in the paragraph headed "Intellectual property rights of the Group" in Appendix V to this prospectus.

EXEMPTED CONNECTED TRANSACTION

On 7th September, 2001, iPayment China and Ecommerce China entered into a services contract for the provision of an online payment enterprise solution and ongoing technical support services to Ecommerce China for its operation of its own online payment services. Pursuant to the Service Agreement, the Group provides ongoing technical support services to Ecommerce China for its offering of online payment services for a monthly fee to be calculated by applying fixed charge per transaction conducted on the payment system of Ecommerce China designed by the Group. The ongoing technical support services to be provided by the Group include maintaining the configuration of the servers for the payment system; managing the database; upgrading the payment software system; monitoring security; and training of technical staff. The payment system used by Ecommerce China includes an interface for banks, online enterprises and online customers to facilitate their payment processes on the Internet. It is designed to allow online enterprises and online customers to use their bank accounts in the banks or accounts supported by card payment services providers such as VISA and MasterCard to effect payment denominated in Renminbi or other currency.

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As at the Latest Practicable Date, the online payment system of Ecommerce China was connected to 13 banks in the PRC such that the online customers could use the bank cards issued by these banks to effect payment. As at the Latest Practicable Date, the payment system used by Ecommerce China was able to effect payment with accounts in the following banks:

China Merchants Bank (All branches) 招商銀行 (所有分行)
China Construction Bank Shanghai and Guangdong Branches 中國建設銀行上海分行及廣東省分行
Industrial and Commercial Bank of China Shanghai and Guangzhou Branches 中國工商銀行上海分行及廣州分行
Bank of Communications (All branches) 交通銀行 (所有分行)
Agricultural Bank of China Guangzhou and Guangdong Branches 中國農業銀行廣州分行及廣東省分行
Guangdong Development Bank (All branches) 廣東發展銀行 (所有分行)
Bank of China (All branches) 中國銀行 (所有分行)
China State Post Bureau (Guangzhou) 中國廣東省郵政儲匯局
Huaxia Bank Guangzhou Branch 華夏銀行廣州分行
Everbright Bank of China Guangzhou Branch 中國光大銀行廣州分行
Citic Development Bank Guangzhou Branch 中信實業銀行廣州分行
Shenzhen Development Bank Co., Ltd. Guangzhou Branch 深圳發展銀行廣州分行
China Minsheng Banking Corporation Limited Guangzhou Branch 民生銀行廣州分行

Ecommerce China is owned as to 51% by Mr. Liu and 49% by the Shanghai Gao Yuan Group. Mr. Liu is the brother of Mr. Y.S. Lau. Accordingly, Ecommerce China is deemed to be a connected person of the Company and the ongoing technical support services to be provided by the Group will constitute ongoing connected transactions of the Company. The Directors believe that the fee receivable from Ecommerce China from the date of listing of the Company to 31st March, 2002 (being the end of the current financial year) will be less than HK\$1,000,000. Therefore, the transactions would fall within the de minimis rules of the GEM Listing Rules and would not be subject to any disclosure or approval requirements. If the aggregate value of the transactions in any financial year exceed the higher of HK\$1,000,000; and 0.03% of the net tangible assets of the Group, the Company will notify the Stock Exchange as soon as practicable and will comply with the relevant requirements of the GEM Listing Rules.

INTEREST IN COMPETING BUSINESS

None of the Initial Management Shareholders has any interests in a business that is competing or is likely to compete with the Group.