

ESF Educational Services Limited ('ESL') Accounts for year ended 31st August 2006

Explanatory Notes

These explanatory notes do not form part of the audited accounts and are provided to put the numbers into context with some background information. There are sections on the income and expenditure account, the balance sheet and cash flow.

Income and expenditure

	<u>2005/06</u>		<u>2004/05</u>		<u>2003/04</u>	
	\$M	% of total income	\$M	% of total income	\$M	% of total income
Income						
Course fees	31.6	35.5	29.8	37.2	28.9	37.2
Tuition fees	53.9	60.5	48.4	60.3	46.6	59.9
Others	3.6	4.0	2.1	2.5	2.2	2.9
	<u>89.1</u>	<u>100.0</u>	<u>80.3</u>	<u>100.0</u>	<u>77.7</u>	<u>100.0</u>
Expenditure						
Staff cost	63.8	71.6	55.5	69.1	56.1	72.1
Depreciation	4.5	5.1	2.4	3.0	2.5	3.2
Management and administrative expenses	1.8	2.0	1.8	2.2	1.6	2.1
Rent, rates and building management fees	9.1	10.2	7.5	9.3	7.6	9.8
Other expenses	15.2	17.1	9.3	11.6	9.8	12.6
	<u>94.4</u>	<u>106.0</u>	<u>76.5</u>	<u>95.2</u>	<u>77.6</u>	<u>99.8</u>
(Deficit)/Surplus	<u>(5.3)</u>	<u>(6.0)</u>	<u>3.8</u>	<u>4.8</u>	<u>0.2</u>	<u>0.2</u>
Average student enrolment						
Kindergartens	676		701		672	
Phoenix International	426		335		336	
Total enrolment	<u>1,102</u>		<u>1,036</u>		<u>1,008</u>	

Income:

1. Although the English course fees continuously decreased since 2003/04 and Phoenix International School summer courses were cancelled in 2005/06, the overall course

fees were higher than last two years due to the strong increase in Sports course fees (100% higher than 2003/04 actual), camps and educational visits.

2. The increase in school fees received over the last two years was due to higher enrolment in Phoenix International and tuition fees increment in kindergartens in 2005/06.
3. Included in \$3.6M other income for 2005/06 was \$2.1M income derived from renting of school premises to outsiders, \$0.8M registration fees of Renaissance College ('RCHK') and \$0.7M miscellaneous items.

Expenditure

1. \$8.3M increase in staff cost during 2005/06 was due to the increase in the number of staff employed to meet the growth in student enrolment and advancement of teachers' contracts commencement day to mid-August.
2. Depreciation expense was \$2.1M as a result of the change in leasehold improvement amortization policy as per HKAS16.
3. Rent paid to schools was higher by \$1.6M, resulting from the growth of school premises rental to outsiders.
4. Other expenses were \$5.9M higher due to \$2.6M increase in teaching materials and resources, \$0.5M increase in passage for new teachers and \$2.6M increase in office and general expenses for RCHK.

Business segment performance

ESL operating deficit in 2005/06 can be better explained by business segment. English section contributed \$1.5M surplus to ESL's bottomline, a low level of contribution compared with its past result. Sports section achieved a small surplus of \$0.1m while kindergartens lost \$2.1m mainly due to the adjustment of depreciation change policy in conformity HKAS16.

The main reason for ESL's deficit was from RCHK. 2005/06 was a year of preparation for RCHK to open in late August 2006. There was no income other than \$0.8m of admission fees. The teaching material costs to get the school ready and teaching staff costs for August month were booked in 2005/06. Overall, RCHK generated \$4.8m loss which was anticipated in its infancy.

Balance sheet

ESL's balance sheet shows:

	<u>2005/06</u>	<u>2004/05</u>	<u>2003/04</u>
	\$M	\$M	\$M
Assets employed			
Non-current assets	38.9	9.6	11.0
Current assets and other	4.6	11.1	4.7
	<u>43.5</u>	<u>20.7</u>	<u>15.7</u>
Less current liabilities	<u>(41.5)</u>	<u>(13.4)</u>	<u>(12.3)</u>
Net assets employed	<u><u>2.0</u></u>	<u><u>7.3</u></u>	<u><u>3.4</u></u>
Reserves			
Accumulated fund	1.7	7.0	3.1
Schools' donation fund	0.3	0.3	0.3
	<u>2.0</u>	<u>7.3</u>	<u>3.4</u>

The non-current assets of \$38.9M were mainly construction in progress for Discovery Bay Private Independent School ('DBPIS') project. As indicated in the balance sheet, these fixed assets were financed by a combination of (1) retained surplus built up by ESL over the years; and (2) the excess of current liabilities over other assets.

	<u>2005/06</u>		<u>2004/05</u>		<u>2003/04</u>	
	\$M	% of total	\$M	% of total	\$M	% of total
Reserves	2.0	5.1	7.3	76.0	3.4	30.9
Net current liabilities	<u>36.9</u>	<u>94.9</u>	<u>2.3</u>	<u>24.0</u>	<u>7.6</u>	<u>69.1</u>
	<u><u>38.9</u></u>		<u><u>9.6</u></u>		<u><u>11.0</u></u>	

Cashflow and capital commitments

	<u>2005/06</u>	<u>2004/2005</u>	<u>2003/04</u>
	<u>\$M</u>	<u>\$M</u>	<u>\$M</u>
Operating activities			
(Deficit)/Surplus for the year	(5.3)	3.8	0.2
Depreciation	4.5	2.4	2.5
Loss on sales of fixed assets	-	0.2	-
	<u>(0.8)</u>	<u>6.4</u>	<u>2.7</u>
Change in working capital	7.6	2.8	(2.9)
Cash generated from operations	<u>6.8</u>	<u>9.2</u>	<u>(0.2)</u>
Investing activities			
Capital expenditure	(15.1)	(1.1)	(0.3)
Other	-	(0.1)	-
	<u>(15.1)</u>	<u>(1.2)</u>	<u>(0.3)</u>
(Decrease)/Increase in cash	<u>(8.3)</u>	<u>8.0</u>	<u>(0.6)</u>

ESL's capital expenditure exceeded cash generated from operations by \$8.3M during the year. Its capital commitment as at 31st August 2006 was \$127.3M which relates to the DBPIS project.

The relationship between ESF and ESL

ESL was set up in 1994 to provide kindergarten, English language classes and extra curricula activities. It also runs the Private Independent Schools and has common management with ESF, but is not legally a subsidiary of ESF.

ESL is the qualified sponsoring body to run RCHK in Ma On Shan and DBPIS under the service agreement with Education and Manpower Bureau.

ESF and ESL have entered into a Development and Operating Agreement such that the top-up funds made available by ESF to build the RCHK and DBPIS school premises and provisions will be rewarded by fees basing on student enrolment. These fees income will provide a steady stream of revenue to ESF starting 2006/07.