

Interim Report
2004-2005

CULTURECOM HOLDINGS LIMITED

(Incorporated in Bermuda with limited liability)

www.culturecom.com.hk

CULTURECOM

CHAIRMAN'S STATEMENT

Business Review

Foreword

Culturecom Group has been heading in the direction of development R&D of Chinese Linux technologies, including (1) Chinese Character Generating Engine (CCGE), (2) Chinese Voice Engine (CVE) and Conceptual Judgment System Technology and (3) the related Linux software technologies, such as Midori Linux embedded operating system and Red Office. Our efforts in the R&D of these three spheres have achieved significant results, which have found favor in the eyes of and are adopted by certain technological companies, like IBM, IT companies of the V-Dragon Industry Alliance and others. Based on this core technology, we have developed various Chinese IT products and applications and have marketed them all in succession. Besides, we have adopted the marketing strategy of "eTown (Digital web-town)" that targets the market of first-time computer users of 1.2 billion population in China to establish an eTown community.

Technological Business Development

The V-Dragon 3210 Processor, based on the Group's CCGE and IBM's PowerPC Technology, has completed its related mother-board design and accessory software development and has been marketed for use in the embedded system products. Among them, the designing plan for mother-board of Tax Terminal/POS Machine has passed China's technological examination and verification. Presently, the Chinese Government is implementing the tax terminal project nationwide, which has entered its tender invitation stage. As our mother-board design has been agreed to adopt by a number of manufacturers, it is believed that substantial income and profits will be crystallized in the near future.

The overall operation mode of eTown has been formed after the activation of the first eTown in Yun'an county, Guangdong province of China in July 2004. The Municipal Government of Yunfu City, Guangdong province will be scheduled to convene a district-wide eTown mobilization meeting in January 2005, and the installation of eTown for 4 counties and cities and 55 towns within the district is scheduled to be completed by the first quarter of next year. At the "17th Meeting of Mayors of Huaihai Economic Zone, the PRC" held in November this year, it was also duly resolved to adopt the Group's eTown solution to build a unified information management and development platform for a population of 120,000,000 within the Zone's 20 cities, 133 counties and 463 towns. Thereafter, with the active support of the Municipal Government of Xuzhou City, the Group has set about the construction of Xuzhou eTown Platform, the first eTown platform in this Zone. In this regard, Xuzhou Government has instructed Xuzhou Telecom Bureau to sign with the Group the "Bundled-Sales Cooperative Agreement in relation to Xuzhou Telecom Broadband Business, eTown Computer and eTown Services", thereby Xuzhou Telecom Bureau will be able to provide local governments, schools, hospitals, enterprises and families with the Group's Chinese Linux Computer and eTown Services. Subsequent to the activation of eTown in Xuzhou, Huaihai Economic Zone, the Group will, acting in the spirit of the "summary of minutes of the 17th Meeting of Mayors of Huaihai Economic Zone, the PRC", continue to co-operate with the governments of all tiers within the Zone to complete zone-wide coverage of eTown services within the next two years.

CHAIRMAN'S STATEMENT (Continued)

Technological Business Development (Continued)

On the other hand, the Group has been negotiating with key agency of China's central government to initiate nation-wide construction work of eTown, and the next planned districts will be the Three Provinces in Northeast, the northwest areas, the Central China Economic District, the Economic Districts of Fujian, Zhejiang, Hunan and Jiangxi and the Economic Districts of Sichuan, Shaanxi, Gansu, Ningxia and etc. The Group believes that the advancement of the eTown marketing strategy will bring a considerable income and profits for the Group itself.

Red Office developed by the Group launched its latest version in June this year and was well received and purchased by the Beijing Municipal Government and other local governments following the purchase bid one after another, such as Shanxi Provincial Government and Hunan Provincial Government. As the Chinese Government tends to use software that possesses self-owned copyright of intellectual properties and open source solution, the Group believes that Red Office will account for a notable share in the future purchases from the Chinese Government.

The Group also made use of the Chinese Character DNA technology to successfully complete the R&D of CVE by the end of this year, and planned to develop jointly with IBM the world's first new-generation "Chinese Smart Computer Chip" that has voice processing capability. Such smart chip features the function of having a computer endowed with the capability to "hear, speak, comprehend and judge", and to enable the user interacting with the computer itself by means of natural language, spurring on a trend of application R&D of new-generation domestic intelligent home appliances. On the occasion, man and machine may communicate with each other through natural conversation, breaking through the restrictions associated with the use of key-board, hand-writing pad and other input methods, and enabling a 'serving the people' application status of the computer.

Comic Business

Comic business has undergone 21% growth after economic recovery of both Hong Kong and Asian markets. However, the future growth momentum will rely on development of new business and new market. By the first half of year 2004/2005, comic department of the Group has signed content distributionship agreement with over 10 major mobile phone service providers (SPs) in China with their total registered members amounted to more than 500 million.

Building up comic content based value added service platform on mobile phone, PC and TV channel is the focus of the year. For the licensing business of multi-media products, we licensed our comic title "Chinese Hero" to TV producers to produce two series of TV opera in 2004 and 2005 respectively. Shooting of the first episode already started by October. In addition, "Dragon Tiger Hero" is licensed to produce movie and is scheduled to be on screen by summer of 2005. Besides, more than 20 comic titles have been licensed to be published in China by 2005 and 2006.

CHAIRMAN'S STATEMENT (Continued)

Prospects

Cuturecom Group will carry through the above development strategy, utilizing developed technologies while collaborating unceasingly with friendly enterprises for further co-operation and promotion, in order to produce more fore-front products that fit in with the emerging need of eTown community. Meantime, the Group will, in addition to consolidating its success in Yun'an and Yunfu District and Huaihai Economic Zone that accounts for 10% of the total population of China, proactively expand the Group's eTown project into other areas of China. The Group will focus on the new first time computer users market of 1.2 billion to build eTown information infrastructure and eTown community. We are much confident that the Group has entered its harvest period and our R&D fruits will dominate the market in the short run.

INTERIM RESULTS

The Board of Directors (the "Directors") of Culturecom Holdings Limited (the "Company") are pleased to announce the unaudited consolidated results of the Company and its subsidiaries (collectively referred to as the "Group") for the six months ended 30th September, 2004 together with the comparative figures for the corresponding period of 2003 are as follows :

CONDENSED CONSOLIDATED INCOME STATEMENT

For the six month ended 30th September, 2004

	Notes	Six months ended 30th September,	
		2004 HK\$'000 (unaudited)	2003 HK\$'000 (unaudited)
Turnover	3	22,755	19,838
Cost of sales		(17,575)	(15,363)
Gross profit		5,180	4,475
Other revenue		2,881	2,542
Administrative expenses		(36,561)	(30,491)
Unrealized (loss) gain on investments in securities		(38,882)	16,410
Amortization of development costs		(5,624)	(9,105)
Research and development expenditures		(384)	(402)
Loss from operations	4	(73,390)	(16,571)
Finance costs	5	(5)	(5)
Share of results of associates		(3,025)	(5,735)
Share of results of a jointly controlled entity		(924)	(805)
Impairment loss recognized in respect of goodwill reserve		(3,000)	–
Loss on deemed disposal of associates		–	(1,333)
Loss before taxation		(80,344)	(24,449)
Taxation	6	–	(1)
Loss for the period		(80,344)	(24,450)
Loss per share – basic and diluted	7	(2.41 cents)	(0.81 cents)

CONDENSED CONSOLIDATED BALANCE SHEET

At 30th September, 2004

		30th September, 2004	31st March, 2004
		HK\$'000	HK\$'000
	Notes	(unaudited)	(audited)
NON-CURRENT ASSETS			
Property, plant and equipment	8	68,500	70,989
Development costs	9	43,385	45,557
Interests in associates		95,030	86,274
Interests in a jointly controlled entity		4,833	5,757
Investments in securities		1,385	1,385
		213,133	209,962
CURRENT ASSETS			
Inventories		15,746	15,783
Trade debtors	10	12,329	10,979
Other debtors, deposits and prepayments		44,251	33,903
Amount due from related companies		7,955	7,668
Amount due from a jointly controlled entity		1,214	82
Investments in securities		26,020	65,948
Deposits with banks and other financial institutions		21,833	69,809
		129,348	204,172
CURRENT LIABILITIES			
Trade creditors	11	8,627	5,482
Other creditors and accrued charges		16,748	17,344
Amounts due to related companies		11	488
Obligation under a finance lease – amount due within one year	12	34	34
		25,420	23,348
NET CURRENT ASSETS		103,928	180,824
TOTAL ASSETS LESS LIABILITIES		317,061	390,786

CONDENSED CONSOLIDATED BALANCE SHEET (Continued)

At 30th September, 2004

		30th September, 2004	31st March, 2004
		HK\$'000	HK\$'000
	Notes	(unaudited)	(audited)
CAPITAL AND RESERVES			
Share capital	13	334,253	332,352
Reserves	15	(17,225)	58,384
TOTAL CAPITAL AND RESERVES		317,028	390,736
NON-CURRENT LIABILITIES			
Obligation under a finance lease – amount due after one year	12	33	50
		317,061	390,786

CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the period ended 30th September, 2004

	Six months ended 30th September,	
	2004	2003
	HK\$'000	HK\$'000
	(unaudited)	(unaudited)
Balance at beginning of the period	390,736	362,208
Exchange difference arising on translation of overseas operation	12	(39)
Loss for the period	(80,344)	(24,450)
Net proceeds from issue of warrants, net of expenses	–	23,818
Issue of shares upon exercise of share options, net of expenses	1,362	–
Issue of shares upon exercise of warrants	2,262	7,920
Impairment loss recognized in respect of goodwill reserve	3,000	–
	<u>317,028</u>	<u>369,457</u>
Balance at end of the period	<u>317,028</u>	<u>369,457</u>

CONDENSED CONSOLIDATED CASH FLOW STATEMENT

For the period ended 30th September, 2004

	Six months ended 30th September,	
	2004	2003
	HK\$'000	HK\$'000
	(unaudited)	(unaudited)
Net cash outflow from operating activities	(34,250)	(3,659)
Net cash outflow from investing activities	(17,340)	(4,125)
Net cash inflow from financing activities	3,602	31,738
(Decrease) increase in cash and cash equivalents	(47,988)	23,954
Effect of foreign exchange rate change	12	(39)
Cash and cash equivalents at beginning of the period	69,809	15,835
Cash and cash equivalents at end of the period	<u>21,833</u>	<u>39,750</u>

NOTES TO THE FINANCIAL STATEMENTS

1. BASIS OF PREPARATION

The condensed financial statements have been prepared in accordance with Statement of Standard Accounting Practice ("SSAP") No. 25 "Interim Financial Reporting" issued by the Hong Kong Institute of Certified Public Accountants and with the disclosure requirements of Appendix 16 to the Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong Limited.

The condensed consolidated interim financial statements should be read in conjunction with the 2003/2004 annual financial statements.

2. PRINCIPAL ACCOUNTING POLICIES

The accounting policies and basis of preparation used in the preparation of the interim financial statements are the same as those used in the annual financial statements for the year ended 31st March 2004.

3. BUSINESS AND GEOGRAPHICAL SEGMENTS

Business segments

Income statement for the period ended 30th September

	Publishing and related business	Chinese information infrastructure	Investment holding	Consolidated
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
2004				
Turnover	<u>22,581</u>	<u>174</u>	<u>–</u>	<u>22,755</u>
Segment results	<u>2,584</u>	<u>(17,633)</u>	<u>(40,272)</u>	(55,321)
Unallocated corporate expenses				<u>(18,069)</u>
Loss from operations				(73,390)
Finance costs				(5)
Share of result of associates	–	(3,025)	–	(3,025)
Share of result of a jointly controlled entity	–	(924)	–	(924)
Impairment loss in respect of goodwill reserve	–	(3,000)	–	<u>(3,000)</u>
Loss before tax				(80,344)
Taxation				<u>–</u>
Net loss for the period				<u>(80,344)</u>

NOTES TO THE FINANCIAL STATEMENTS (Continued)

3. BUSINESS AND GEOGRAPHICAL SEGMENTS (Continued)

Business segments (Continued)

	Publishing and related business HK\$'000	Chinese information infrastructure HK\$'000	Investment holding HK\$'000	Consolidated HK\$'000
2003				
Turnover	<u>18,596</u>	<u>1,242</u>	<u>–</u>	<u>19,838</u>
Segment results	<u>1,801</u>	<u>(13,510)</u>	<u>10,376</u>	<u>(1,333)</u>
Unallocated corporate expenses				<u>(15,238)</u>
Loss from operations				(16,571)
Finance costs				(5)
Share of result of associates	–	(5,735)	–	(5,735)
Share of result of a jointly controlled entity	–	(805)	–	(805)
Loss on deemed disposal of associates	–	(1,333)	–	<u>(1,333)</u>
Loss before tax				(24,449)
Taxation				<u>(1)</u>
Net loss for the period				<u>(24,450)</u>

Geographical segments

The Group's operations are located in Hong Kong and other regions in the People's Republic of China (the "PRC").

The following table provides an analysis of the Group's turnover and loss to operations by location of markets, irrespective of the origin of the goods/services:

	Turnover		Loss from operation	
	2004 HK\$'000	2003 HK\$'000	2004 HK\$'000	2003 HK\$'000
Hong Kong	<u>22,631</u>	<u>19,687</u>	<u>(67,473)</u>	<u>(10,925)</u>
PRC	<u>124</u>	<u>151</u>	<u>(5,917)</u>	<u>(5,646)</u>
	<u>22,755</u>	<u>19,838</u>	<u>(73,390)</u>	<u>(16,571)</u>

NOTES TO THE FINANCIAL STATEMENTS (Continued)

4. LOSS FROM OPERATIONS

	Six months ended 30th September,	
	2004	2003
	<u>HK\$'000</u>	<u>HK\$'000</u>
Loss from operations has been arrived at after charging (crediting):		
Depreciation and amortisation of property, plant and equipment	4,107	4,711
Bank interest income	<u>(165)</u>	<u>(202)</u>

5. FINANCE COSTS

The amount represents interest on bank borrowings wholly repayable within five years.

6. TAXATION

Hong Kong profits tax has been provided at the rate of 17.5% (2003 : 17.5%) on the estimated assessable profit for the period.

7. LOSS PER SHARE

The calculation of the basic loss per share is based on the net loss for the period of approximately HK\$80,344,000 (2003: HK\$24,450,000) and the weighted average number of 3,333,928,137 (2003: 3,027,233,959) ordinary shares in issue during the period.

The computation of diluted loss per share for the periods ended 30th September, 2004 and 2003 does not assume the exercise of the Company's outstanding share options and warrants since their exercise would reduce net loss per share.

Dilutive loss per share for the period is not shown because the exercise of outstanding share options granted and warrants issued by the Company would have an anti-dilutive effect on the loss per share for the period.

8. ADDITIONS TO PROPERTY, PLANT AND EQUIPMENT

During the period, the Group acquired equipment amounting to approximately HK\$1,618,000 (2003 : HK\$2,173,000).

NOTES TO THE FINANCIAL STATEMENTS (Continued)

9. DEVELOPMENT COSTS

	30th September, 2004	31st March, 2004
	HK\$'000	HK\$'000
COST		
Balance at the beginning of the period	95,045	86,288
Additions	3,452	8,757
Balance at the end of the period	<u>98,497</u>	<u>95,045</u>
AMORTIZATION AND ACCUMULATED IMPAIRMENT LOSS		
Balance at the beginning of the period	49,488	30,782
Charged for the period	5,624	18,706
Balance at the end of the period	<u>55,112</u>	<u>49,488</u>
NET BOOK VALUE	<u>43,385</u>	<u>45,557</u>

Development costs represent expenditure incurred for the development of the Chinese information infrastructure. Such development costs are deferred and amortised over its estimated useful life range from two to five years from the date of commencement of commercial operations.

10. TRADE DEBTORS

The Group allows an average credit period of 60 days to its trade customers. The following is an aged analysis of trade debtors at the balance sheet date:

	30th September, 2004	31st March, 2004
	HK\$'000	HK\$'000
0 – 60 days	7,899	5,979
61 – 90 days	2,872	582
Over 90 days	1,558	4,418
	<u>12,329</u>	<u>10,979</u>

NOTES TO THE FINANCIAL STATEMENTS (Continued)

11. TRADE CREDITORS

The following is an aged analysis of trade creditors at the balance sheet date:

	30th September, 2004 HK\$'000	31st March, 2004 HK\$'000
0 – 60 days	7,682	4,475
61 – 90 days	98	166
Over 90 days	847	841
	<u>8,627</u>	<u>5,482</u>

12. OBLIGATIONS UNDER A FINANCE LEASE

	Minimum lease payments HK\$'000	Present value of minimum lease payments HK\$'000
Amounts payable under a finance leases:		
Within one year	42	34
In the second to fifth years inclusive	42	33
	84	67
Less : future finance charges	(17)	–
Present value of lease obligation	<u>67</u>	67
Less : amount due from settlement within one year shown under current liabilities		<u>(34)</u>
Amount due after one year		<u>33</u>

The lease term in respect of the furniture and equipment under the finance lease is 5 years.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

13. SHARE CAPITAL

	Number of shares		Share capital	
	30th September, 2004 '000	31st March, 2004 '000	30th September, 2004 HK\$'000	31st March, 2004 HK\$'000
Ordinary shares of HK\$0.10 each, Authorized:	<u>6,000,000</u>	<u>4,000,000</u>	<u>600,000</u>	<u>400,000</u>
Issued and fully paid :				
At the beginning of the period	3,323,520	3,014,000	332,352	301,400
Exercise of share options	5,300	199,800	530	19,980
Exercise of warrants	<u>13,710</u>	<u>109,720</u>	<u>1,371</u>	<u>10,972</u>
At the end of the period	<u>3,342,530</u>	<u>3,323,520</u>	<u>334,253</u>	<u>332,352</u>

14. WARRANTS

On 6th June, 2003, the Company entered into a placing and underwriting agreement with a placing agent in relation to the private placing of 430,000,000 warrants ("2005 Warrants") conferring rights to subscribe up to HK\$70,950,000 in aggregate in cash for shares of HK\$0.10 each in the share capital of the Company at an initial subscription price of HK\$0.165 per share during the period from 8 July 2003 to 7 July 2005, both days inclusive. The placing of 2005 Warrants was completed on 4th July, 2003.

The net proceeds of the placing of approximately HK\$24 million was intended to be used for general working capital of the Group.

On 30th September, 2004, the Company had 306,570,000 outstanding 2005 Warrants conferring rights to subscribe up to approximately HK\$50,584,050 in cash for shares of HK\$0.10 cash in the Company. Exercise in full of those outstanding warrants would, under the present share capital structure of the Company as of 30th September, 2004, result in the issue of 306,570,000 additional shares of HK\$0.10 each in the Company.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

15. RESERVES

	Share premium	Contribution surplus	Goodwill reserve	Other reserve	Capital redemption reserve	Translation reserve	Deficit	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 1st April, 2003	630,013	171,671	(62,948)	1,500	446	(307)	(679,567)	60,808
Exchange loss on translation of overseas operations not recognized in the income statement	-	-	-	-	-	170	-	170
Proceeds from issue of warrants, net of expenses	-	-	-	23,774	-	-	-	23,774
Exercise of warrants	7,132	-	-	-	-	-	-	7,132
Transfer from other reserve to share premium due to exercise of warrants	6,066	-	-	(6,066)	-	-	-	-
Exercise of share options	32,967	-	-	-	-	-	-	32,967
Impairment loss recognized (<i>note</i>)	-	-	6,000	-	-	-	-	6,000
Net loss for the year	-	-	-	-	-	-	(72,467)	(72,467)
At 31st March, 2004	676,178	171,671	(56,948)	19,208	446	(137)	(752,034)	58,384
Exchange loss on translation of overseas operations not recognized in the income statement	-	-	-	-	-	12	-	12
Exercise of warrants	891	-	-	-	-	-	-	891
Transfer from other reserve to share premium due to exercise of warrants	758	-	-	(758)	-	-	-	-
Exercise of share options	832	-	-	-	-	-	-	832
Impairment loss recognized (<i>note</i>)	-	-	3,000	-	-	-	-	3,000
Net loss for the period	-	-	-	-	-	-	(80,344)	(80,344)
At 30th September, 2004	678,659	171,671	(53,948)	18,450	446	(125)	(832,378)	(17,225)

Note: Due to continuous losses incurred by an associate, the directors recognized an impairment loss of HK\$3,000,000 in current period, while it was HK\$6,000,000 for the year ended 31st March 2004.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

16. CONTINGENT LIABILITIES

- (a) At 30th September, 2004, the Company was cited as defendant in a court case in respect of claims amounting to approximately HK\$11,967,000 (2003: HK\$11,967,000) in relation to a guarantee given to the plaintiff. Based on the advice of its legal adviser, the directors are of the view that the Company has reasonable grounds to defense. Accordingly, no provision for this amount has been provided in the financial statements.
- (b) During the period, the Company and eForce Holdings Limited (“eForce”), on a joint and several basis, provided a guarantee to Transmeta Corporation (“Transmeta”) in respect of the payment obligations of service fees of China Ever Limited, a wholly-owned subsidiary of Chinese 2 Limited (Holdings) Limited, the associate of the Group. Pursuant to the agreement between the Company, eForce, China Ever Limited and Transmeta, China Ever Limited shall pay a service fee of US\$66,000 per month to Transmeta for a term of 20 months from 22nd November, 2003.

17. DISPUTE

In May 2003, Winway H.K. Investments Limited (“Winway”), a wholly owned subsidiary of the Company, has placed 300,000,000 shares (the “shares”) of Q9 Technology Holdings Limited (“Q9 Technology”) with TKR Finance Limited (“TKR Finance”) for safe custody and to facilitate management of such shares. In June 2004, Winway was informed by Q9 Technology that it had received a copy of the disclosure of interests form filed pursuant to the Securities and Futures Ordinance by the provisional liquidator of TKR Finance claiming security interests in the shares, of which Winway had no prior knowledge nor given any consent thereto. Upon receipt of such information, Winway had sought legal advice and had notified the provisional liquidator about its title in the shares and demanded the return of the shares from TKR Finance. Currently, Winway is positively seeking a feasible resolution and negotiating with the relevant parties to reclaim the shares. As at 30th September, 2004, the market value of the shares was approximately HK\$12.6 million.

18. CAPITAL COMMITMENTS

At the balance sheet date, the Company has no significant capital commitments.

MANAGEMENT DISCUSSION AND ANALYSIS

Financial Results

The Group's overall turnover for the period ended 30th September, 2004 increased approximately by 15% to approximately HK\$22,755,000 over last period, of which approximately HK\$22,581,000 and HK\$174,000 (2003: HK\$18,596,000 and HK\$1,242,000) were attributable to our business of comics publication and Chinese information infrastructure respectively.

For the period ended 30th September, 2004, the Group's consolidated net loss attributable to shareholders increased to approximately HK\$80,344,000 as compared to that of the last period. The loss per share for the period was HK2.41 cents (2003: HK0.81 cents). The increase in loss for the period was due to that:

- (i) marketing and promotional expenses for the group's information technology products were increased by approximately HK\$3,900,000 over the previous period;
- (ii) an unrealized loss on investment in securities of approximately HK\$38,882,000 while it was an unrealized gain of approximately HK\$16,410,000 in previous period; and
- (iii) due to continuous losses incurred by an associated company, an impairment loss of goodwill reserve of HK\$3,000,000 was recognized in current period.

The Directors believe that the loss for the consecutive financial periods will be improved once when the sales revenue in respect of V-Dragon products and eTown computers is recognized upon the delivery of products in the coming year.

At 30th September, 2004, the Group's net asset value was HK\$317,028,000 and net asset value per weighted average number of 3,333,928,137 shares of the Company was approximately HK\$0.10 (2003: HK\$0.12).

Liquidity and Financial Resources

As at 30th September, 2004, the Group had bank and cash balances in aggregate of approximately HK\$21,833,000 and short-term listed securities of approximately HK\$26,020,000. The Group has no significant exposure to foreign exchange rate fluctuation.

As at 30th September, 2004, the Group's total liabilities amounted to approximately HK\$25,453,000, representing approximately 8% (2003: 8%) to the shareholders' equity. There was no outstanding bank loan as at 30th September, 2004.

The Directors believe that the Group currently has sufficient liquidity to finance its daily operation, and the net proceeds from the exercise of the remaining warrants in the future would further strengthen the financial position of the Group.

MANAGEMENT DISCUSSION AND ANALYSIS (Continued)

Development Costs of I.T. Projects

As at 30th September, 2004, accumulated costs incurred for the development of Chinese language computer operating system, Chinese single chip system, Chinese electronic books and other related application software less accumulated amortization amounted approximately to HK\$43,385,000 (2003: HK\$52,545,000). These development costs are deferred and written off over its estimated useful life range from two to five years from the date of commencement of commercial operations. For the period ended 30th September, 2004, the amortization of development cost amounted to HK\$5,624,000 (2003: HK\$9,105,000). In addition, research and development expenditures incurred directly as expenses during the period amounted to HK\$384,000 (2003: HK\$402,000).

Employment and Remuneration Policies

As at 30th September, 2004, the Group had a total of 128 employees of which 73 are based in Hong Kong, 52 in Macau and 3 in the PRC. Total staff costs incurred during the period amounted to approximately HK\$11,420,000 (2003: HK\$13,216,000). Remuneration packages are maintained at competitive level and reviewed by the management on a periodical basis. Discretionary bonuses and incentive share options are awarded to certain directors and employees according to the assessment of individual merit and performance.

INTERIM DIVIDEND

The Board of Directors of the Company has resolved not to declare an interim dividend for the six months ended 30th September, 2004 (2003: nil).

REPURCHASE, SALE OR REDEMPTION OF LISTED SECURITIES

Neither the Company nor its subsidiaries have purchased, sold or redeemed any of the listed securities in the Company during the six months ended 30th September, 2004.

SHARE OPTION SCHEME

The Company has terminated its share option scheme adopted on 15th June, 1993 (the “1993 Scheme”) and adopted a new share option scheme (the “2002 Scheme”) on its 2002 Annual General Meeting held on 21st August, 2002.

Subsequent to the termination of the 1993 Scheme, no further share options can be granted thereunder but in all other respects, the provisions of the 1993 Scheme shall remain in force and all share options granted prior to such termination shall continue to be valid and exercisable in accordance therewith.

Details of the movement of the share options granted to the Directors and employees of the Company under the 1993 Scheme during the six months ended 30th September, 2004 are as follows:

	Date of Grant	At 1st April, 2004	Number of share options		At 30th September, 2004	Exercise price per share HK\$	Exercisable Period	Price of the
			Exercised during the period	Granted/ Lapsed/ Cancelled during the period				Company's shares immediately preceding the exercise date of share options (note)
								HK\$
(a) Directors								
Mr. Cheung Wai Tung	3rd March, 2000	4,565,000	-	-	4,565,000	1.680	3rd March, 2000 to 2nd March, 2010	N/A
Mr. Chu Bong Foo	(i) 27th August, 1999	10,000,000	-	-	10,000,000	0.264	27th August, 1999 to 26th August, 2009	N/A
	(ii) 3rd March, 2000	2,000,000	-	-	2,000,000	1.680	3rd March, 2000 to 2nd March, 2010	N/A
Mr. Cheung Kam Shing, Terry	3rd March, 2000	3,000,000	-	-	3,000,000	1.680	3rd March, 2000 to 2nd March, 2010	N/A
Mr. Henry Chang Manayan	(i) 27th August, 1999	2,000,000	(1,000,000)	-	1,000,000	0.264	27th August, 1999 to 26th August, 2009	0.55
	(ii) 3rd March, 2000	500,000	-	-	500,000	1.680	3rd March, 2000 to 2nd March, 2010	N/A
Mr. Wan Xiaolin	3rd March, 2000	1,000,000	-	-	1,000,000	1.680	3rd March, 2000 to 2nd March, 2010	N/A
(b) Employees								
	3rd March, 2000	25,035,000	-	-	25,035,000	1.680	3rd March, 2000 to 2nd March, 2010	N/A

Note: The price of the Company's shares disclosed as at immediately preceding the date of exercise of the share options is the Stock Exchange closing price on the trading day immediately prior to the date of the exercise of the share options.

SHARE OPTION SCHEME (Continued)

Details of the movement of the share options granted under the 2002 Scheme during the six months ended 30th September, 2004 are as follows:

	Date of Grant	At 1st April, 2004	Number of share options			At 30th September, 2004	Exercise price per share <i>HK\$</i>	Exercisable Period	Price of the
			Exercised during the period	Granted/ Lapsed/ Cancelled during the period					Company's shares immediately preceding the exercise date of share options <i>(note)</i> <i>HK\$</i>
(a) Directors									
Mr. Cheung Wai Tung	19th December, 2003	4,000,000	-	-	4,000,000	0.265	19th December, 2003 to 18th December, 2013	N/A	
Mr. Cheung Kam Shing, Terry	19th December, 2003	3,000,000	-	-	3,000,000	0.265	19th December, 2003 to 18th December, 2013	N/A	
Mr. Henry Chang Manayan	19th December, 2003	1,000,000	-	-	1,000,000	0.265	19th December, 2003 to 18th December, 2013	N/A	
Mr. Wan Xiaolin	19th December, 2003	3,000,000	-	-	3,000,000	0.265	19th December, 2003 to 18th December, 2013	N/A	
(b) Employees	19th December, 2003	48,200,000	(3,300,000)	-	44,900,000	0.265	19th December, 2003 to 18th December, 2013	0.525	
(c) Others	19th December, 2003	41,000,000	(1,000,000)	-	40,000,000	0.265	19th December, 2003 to 18th December, 2013	0.525	

Note: The price of the Company's shares disclosed as at immediately preceding the date of the exercise of the share options is the weighted average of the Stock Exchange closing prices over all of the exercises of share options prior to their respective exercise dates within the disclosure line.

DISCLOSURE OF INTERESTS

(a) Interests of the Directors

As at 30th September, 2004, the interests and short positions of each Director and chief executive of the Company in the shares, underlying shares or debentures of the Company and its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance (the "SFO")) which are required (a) to be notified to the Company and The Stock Exchange of Hong Kong Limited (the "Stock Exchange") pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests or short positions which he/she is taken or deemed to have under such provisions of the SFO); or (b) pursuant to section 352 of the SFO, to be entered in the register referred to therein; or (c) pursuant to the Model Code for Securities Transactions by Directors of Listed Companies to be notified to the Company and the Stock Exchange:

Interests in the shares of the Company

Name of Director	Capacity	Nature of interests	Number of shares held	Approximate percentage of issued share capital
Mr. Cheung Wai Tung	Beneficial owner	Personal interest	10,000,000	0.30%
Mr. Chu Bong Foo	(i) Beneficial owner (ii) Interest of a controlled corporation	Personal interest Corporate interest	220,180,000 122,872,000 (note 1)	10.26%
Mr. Henry Chang Manayan	Beneficial owner	Personal interest	2,000,000	0.06%
Mr. Wan Xiaolin	Beneficial owner	Personal interest	500,000	0.01%

Note:

- 122,872,000 shares are held by Bay-Club Enterprises Inc., the entire issued share capital of which is beneficially owned by Mr. Chu Bong Foo.

All interests stated above represent long positions.

DISCLOSURE OF INTERESTS (Continued)

Interests in the share option of the Company

Name of Director	Capacity	Nature of interests	Number of share options	Exercise price per share HK\$	Exercisable period	Approximate percentage of issued share capital
Mr. Cheung Wai Tung	(i)	Beneficial owner	Personal interest 4,565,000 <i>(note 1)</i>	1.680	3rd March, 2000 to 2nd March, 2010	0.26%
	(ii)	Beneficial owner	Personal interest 4,000,000 <i>(note 1)</i>	0.265	19th December, 2003 to 18th December, 2013	
Mr. Chu Bong Foo	(i)	Beneficial owner	Personal interest 10,000,000 <i>(note 2)</i>	0.264	27th August, 1999 to 26th August, 2009	0.36%
	(ii)	Beneficial owner	Personal interest 2,000,000 <i>(note 2)</i>	1.680	3rd March, 2000 to 2nd March, 2010	
Mr. Cheung Kam Shing, Terry	(i)	Beneficial owner	Personal interest 3,000,000 <i>(note 3)</i>	1.680	3rd March, 2000 to 2nd March, 2010	0.18%
	(ii)	Beneficial owner	Personal interest 3,000,000 <i>(note 3)</i>	0.265	19th December, 2003 to 18th December, 2013	
Mr. Henry Chang Manayan	(i)	Beneficial owner	Personal interest 1,000,000 <i>(note 4)</i>	0.264	27th August, 1999 to 26th August, 2009	0.07%
	(ii)	Beneficial owner	Personal interest 500,000 <i>(note 4)</i>	1.680	3rd March, 2000 to 2nd March, 2010	
	(iii)	Beneficial owner	Personal interest 1,000,000 <i>(note 4)</i>	0.265	19th December, 2003 to 18th December, 2013	
Mr. Wan Xiaolin	(i)	Beneficial owner	Personal interest 1,000,000 <i>(note 5)</i>	1.680	3rd March, 2000 to 2nd March, 2010	0.12%
	(ii)	Beneficial owner	Personal interest 3,000,000 <i>(note 5)</i>	0.265	19th December, 2003 to 18th December, 2013	

DISCLOSURE OF INTERESTS (Continued)

Notes:

1. Pursuant to the 1993 Scheme, Mr. Cheung Wai Tung was granted share options by the Company on 3rd March, 2000 to subscribe for 4,565,000 shares at the exercise price of HK\$1.680 per share for the exercisable period from 3rd March, 2000 to 2nd March, 2010. On 19th December, 2003, Mr. Cheung was further granted share options by the Company to subscribe for 4,000,000 shares at the exercise price of HK\$0.265 for the exercisable period from 19th December, 2003 to 18th December, 2013 under the 2002 Scheme.
2. Pursuant to the 1993 Scheme, Mr. Chu Bong Foo was granted share options by the Company (i) on 27th August, 1999 to subscribe for 10,000,000 shares at the exercise price of HK\$0.264 per share for the exercisable period from 27th August, 1999 to 26th August, 2009; and (ii) on 3rd March, 2000 to subscribe for 2,000,000 shares at the exercise price of HK\$1.680 per share for the exercisable period from 3rd March, 2000 to 2nd March, 2010.
3. Pursuant to the 1993 Scheme, Mr. Cheung Kam Shing, Terry was granted share options by the Company to subscribe for 3,000,000 shares at the exercise price of HK\$1.680 per share for the exercisable period from 3rd March, 2000 to 2nd March, 2010 upon his appointment as Managing Director of the Company on 1st April, 2000. On 19th December, 2003, Mr. Cheung was further granted share options by the Company to subscribe for 3,000,000 shares at the exercise price of HK\$0.265 for the exercisable period from 19th December, 2003 to 18th December, 2013 under the 2002 Scheme.
4. Pursuant to the 1993 Scheme, Mr. Henry Chang Manayan was granted share options by the Company (i) on 27th August, 1999 to subscribe for 3,000,000 shares at the exercise price of HK\$0.264 per share for the exercisable period from 27th August, 1999 to 26th August, 2009; and (ii) on 3rd March, 2000 to subscribe for 500,000 shares at the exercise price of HK\$1.680 per share for the exercisable period from 3rd March, 2000 to 2nd March, 2010. Mr. Henry Chang Manayan exercised his share options to subscribe for the aggregate of 2,000,000 shares at the exercise price of HK\$0.264 on 18th February, 2000 and 6th April, 2004 respectively. On 19th December, 2003, he was further granted share options by the Company to subscribe for 1,000,000 shares at the exercise price of HK\$0.265 for the exercisable period from 19th December, 2003 to 18th December, 2013 under the 2002 Scheme.
5. Pursuant to the 1993 Scheme, Mr. Wan Xiaolin was granted share options by the Company on 3rd March, 2000 to subscribe for 1,000,000 shares at the exercise price of HK\$1.680 per share for the exercisable period from 3rd March, 2000 to 2nd March, 2010. On 19th December, 2003, Mr. Wan was further granted share options by the Company to subscribe for 3,000,000 shares at the exercise price of HK\$0.265 for the exercisable period from 19th December, 2003 to 18th December, 2013 under the 2002 Scheme.

All interests stated above represent long positions.

DISCLOSURE OF INTERESTS (Continued)

Save as disclosed above, as at 30th September, 2004, none of the Directors nor chief executive of the Company had interests or short positions in any securities of the Company or any of its associated corporations (within the meaning of Part XV of the SFO) which are required (a) to be notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests or short positions which he/she is taken or deemed to have under such provisions of the SFO); or (b) pursuant to section 352 of the SFO, to be entered in the register referred to therein; or (c) pursuant to the Model Code for Securities Transactions by Directors of Listed Companies to be notified to the Company and the Stock Exchange.

(b) Interests of Substantial Shareholders

As at 30th September, 2004, so far as is known to any Director or chief executive of the Company, the following person has an interest or short position in the shares or underlying shares of the Company which would fall to be disclosed to the Company under the provisions of Divisions 2 and 3 of Part XV of the SFO, or which were recorded in the register to be kept by the Company under Section 336 of the SFO:

Interests in the shares of the Company

Name	Capacity	Nature of interests	Number of shares held	Approximate percentage of issued share capital
Mr. Chu Bong Foo	(i) Beneficial owner	Personal interest	220,180,000	10.26%
	(ii) Interest of a controlled corporation	Corporate interest	122,872,000 (note 1)	

Note:

- 122,872,000 shares are held by Bay-Club Enterprises Inc., the entire issued share capital of which is beneficially owned by Mr. Chu Bong Foo.

All interests stated above represent long positions.

DISCLOSURE OF INTERESTS (Continued)

Interest in share options of the Company

Name of Director	Capacity	Nature of interest	Number of share options	Approximate percentage of issued share capital
Mr. Chu Bong Foo	Beneficial owner	Personal interest	12,000,000	0.36%

The interest stated above represents long position.

Save as disclosed above, as at 30th September, 2004, the Directors and the chief executive of the Company were not aware of any person who had an interest or short position in the shares or underlying shares of the Company which would fall to be disclosed to the Company under the provisions of Divisions 2 and 3 of Part XV of the SFO, or which were recorded in the register to be kept by the Company under Section 336 of the SFO.

AUDIT COMMITTEE

The Audit Committee comprises three independent non-executive Directors, namely Mr. Lai Man To, Mr. Wang Tiao Chun and Mr. Joseph Lee Chennault. The Committee has reviewed with the management the accounting principles and practices adopted by the Group and discussed the internal control and financial reporting matters including the review of the unaudited interim results for the six months ended 30th September, 2004.

CODE OF BEST PRACTICE

The Company has complied throughout the six months ended 30th September, 2004 with those paragraphs of the Code of Best Practice as set out in Appendix 14 of the Rules Governing the Listing of Securities on the Stock Exchange except that the Independent Non-Executive Directors of the Company were appointed without specific term as they were subject to retirement by rotation in accordance with the Bye-laws of the Company.

DIRECTORS

As at the date of this report, the Board comprises of Mr. Cheung Wai Tung, Mr. Chu Bong Foo, Mr. Cheung Kam Shing, Terry, Mr. Henry Chang Manayan, Mr. Wan Xiaolin (all being executive Directors); and Mr. Lai Man To, Mr. Wang Tiao Chun, Mr. Joseph Lee Chennault (all being independent non-executive Directors).

By Order of the Board
Cheung Wai Tung
 Chairman

Hong Kong, 17th December, 2004