



Advanced Card Systems Holdings Limited

龍傑智能卡控股有限公司*

(incorporated in the Cayman Islands with limited liability)

(Stock Code: 8210)

ANNUAL RESULTS ANNOUNCEMENT FOR THE YEAR ENDED 31 DECEMBER 2006

CHARACTERISTICS OF THE GROWTH ENTERPRISE MARKET ("GEM") OF THE STOCK EXCHANGE OF HONG KONG LIMITED (THE "STOCK EXCHANGE")

GEM has been established as a market designed to accommodate companies to which a high investment risk may be attached. In particular, companies may list on GEM with neither a track record of profitability nor any obligation to forecast future profitability. Furthermore, there may be risks arising out of the emerging nature of companies listed on GEM and the business sectors or countries in which the companies operate. Prospective investors should be aware of the potential risks of investing in such companies and should make the decision to invest only after due and careful consideration. The greater risk profile and other characteristics of GEM mean that it is a market more suited to professional and other sophisticated investors.

Given the emerging nature of companies listed on GEM, there is a risk that securities traded on GEM may be more susceptible to high market volatility than securities traded on the Main Board and no assurance is given that there will be a liquid market in the securities traded on GEM.

The principal means of information dissemination on GEM is publication on the internet website operated by the Stock Exchange. Listed companies are not generally required to issue paid announcements in gazetted newspapers. Accordingly, prospective investors should note that they need to have access to the GEM website in order to obtain up-to-date information on GEM-listed issuers.

The Stock Exchange takes no responsibility for the contents of this announcement, makes no representation as to its accuracy or completeness and expressly disclaims any liability whatsoever for any loss howsoever arising from or in reliance upon the whole or any part of the contents of this announcement.

This announcement, for which the directors of Advanced Card Systems Holdings Limited (the "Company") collectively and individually accept full responsibility, includes particulars given in compliance with the Rules Governing the Listing of Securities on the GEM of the Stock Exchange for the purpose of giving information with regard to the Company. The directors, having made all reasonable enquires, confirm that, to the best of their knowledge and belief:- (i) the information contained in this announcement is accurate and complete in all material respects and not misleading; (ii) there are no other matters the omission of which would make any statement in this announcement misleading; and (iii) all opinions expressed in this announcement have been arrived at after due and careful consideration and are founded on bases and assumptions that are fair and reasonable.

* For identification only

HIGHLIGHTS

- The revenue of the Group for the year ended 31 December 2006 increased by 11% to HK\$43.2 million from the year ended 31 December 2005.
- The gross profit of the Group for the year ended 31 December 2006 increased to HK\$23.1 million from HK\$17.0 million in 2005 and the gross profit margin increased to 53% from 44%.
- The Group recorded net profit before income tax of HK\$3.8 million in 2006 and loss before income tax of HK\$2.1 million in 2005.
- The Group recorded net profit after income tax of HK\$2.6 million (after deducting income tax of HK\$1.2 million) in 2006 and net profit after income tax of HK\$0.2 million (after adding tax credit of HK\$2.3 million) in 2005.
- As at 31 December 2006, the cash at banks and on hand of the Group amounted to HK\$7.9 million (HK\$7.1 million as at 31 December 2005) and there was no borrowing.

CONSOLIDATED RESULTS

The Board of Directors of the Company are pleased to announce the audited consolidated results of the Company and its subsidiaries (the “Group”) for the year ended 31 December 2006 together with the comparative figures for the year ended 31 December 2005 as follows:

CONSOLIDATED INCOME STATEMENT

For the year ended 31 December 2006

	<i>Notes</i>	2006 <i>HK\$'000</i>	2005 <i>HK\$'000</i>
Revenue	3	43,165	38,853
Cost of sales		<u>(20,092)</u>	<u>(21,808)</u>
Gross profit		23,073	17,045
Other revenue	3	282	1,163
Other net loss	4	(196)	(153)
Selling and distribution costs		(3,014)	(4,080)
Administrative expenses		<u>(16,185)</u>	<u>(15,968)</u>
Operating profit/(loss)		3,960	(1,993)
Finance costs	6.1	<u>(206)</u>	<u>(149)</u>
Profit/(Loss) before income tax	6	3,754	(2,142)
Income tax (expense)/credit	7	<u>(1,190)</u>	<u>2,338</u>
Profit for the year		<u>2,564</u>	<u>196</u>
Earnings per share	9		
Basic		<u>HK0.91 cents</u>	<u>HK0.07 cents</u>
Diluted		<u>HK0.91 cents</u>	<u>N/A</u>

CONSOLIDATED BALANCE SHEET
As at 31 December 2006

	<i>Notes</i>	2006 <i>HK\$'000</i>	2005 <i>HK\$'000</i>
ASSETS AND LIABILITIES			
Non-current assets			
Plant and equipment		1,932	2,151
Development costs		9,393	8,148
Deferred tax assets	10.1	<u>2,762</u>	<u>3,952</u>
		<u>14,087</u>	<u>14,251</u>
Current assets			
Inventories		8,600	9,047
Trade and other receivables, deposits paid and prepayments	11	6,753	6,103
Held-to-maturity financial asset		17	—
Pledged bank deposits		2,691	691
Cash and cash equivalents		<u>5,240</u>	<u>6,390</u>
		<u>23,301</u>	<u>22,231</u>
Current liabilities			
Trade and other payables, deposits received and accruals	12	<u>4,472</u>	<u>6,130</u>
Net current assets		<u>18,829</u>	<u>16,101</u>
Net assets		<u>32,916</u>	<u>30,352</u>
EQUITY ATTRIBUTABLE TO COMPANY'S EQUITY HOLDERS			
Share capital		28,180	28,180
Reserves		<u>4,736</u>	<u>2,172</u>
Total equity		<u>32,916</u>	<u>30,352</u>

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
For the year ended 31 December 2006

	Share capital <i>HK\$'000</i>	Share premium <i>HK\$'000</i>	Merger reserve <i>HK\$'000</i>	Accumulated losses <i>HK\$'000</i>	Total <i>HK\$'000</i>
At 1 January 2005	28,180	24,333	4,496	(26,853)	30,156
Profit for the year	<u>—</u>	<u>—</u>	<u>—</u>	<u>196</u>	<u>196</u>
Total recognised income and expense for the year	<u>—</u>	<u>—</u>	<u>—</u>	<u>196</u>	<u>196</u>
At 31 December 2005 and 1 January 2006	28,180	24,333	4,496	(26,657)	30,352
Profit for the year	<u>—</u>	<u>—</u>	<u>—</u>	<u>2,564</u>	<u>2,564</u>
Total recognised income and expense for the year	<u>—</u>	<u>—</u>	<u>—</u>	<u>2,564</u>	<u>2,564</u>
At 31 December 2006	<u><u>28,180</u></u>	<u><u>24,333*</u></u>	<u><u>4,496*</u></u>	<u><u>(24,093)*</u></u>	<u><u>32,916</u></u>

* The aggregated amount of the above balances of HK\$4,736,000 (2005: HK\$2,172,000) represented the reserves in the consolidated balance sheet.

NOTES

1. GENERAL INFORMATION

The Company was incorporated in the Cayman Islands on 13 April 2000 as an exempted company with limited liability under the Companies Law (Revised) of the Cayman Islands. The address of its registered office is Ugland House, P.O. Box 309, George Town, Grand Cayman, Cayman Islands, British West Indies and its principal place of business is located at Unit 1008, 10th Floor, Hongkong International Trade and Exhibition Centre, 1 Trademart Drive, Kowloon Bay, Hong Kong. The Company's shares are listed on The Growth Enterprise Market ("GEM") of The Stock Exchange of Hong Kong Limited (the "Stock Exchange").

The principal activities of the Company and its subsidiaries (the "Group") include the development, sale and distribution of smart card products, software and hardware and the provision of smart card related services to its customers.

The financial statements have been prepared in accordance with Hong Kong Financial Reporting Standards ("HKFRSs") which collective term includes all applicable individual Hong Kong Financial Reporting Standards, Hong Kong Accounting Standards and Interpretations issued by the Hong Kong Institute of Certified Public Accountants, the disclosure requirements of the Hong Kong Companies Ordinance and the Rules Governing the Listing of Securities on the GEM of the Stock Exchange ("GEM Listing Rules").

The financial statements for the year ended 31 December 2006 were approved by the board of directors on 23 March 2007.

2. ADOPTION OF NEW OR AMENDED HKFRSs

From 1 January 2006, the Group has adopted all the new and amended HKFRSs which are first effective on 1 January 2006 and relevant to the Group. The adoption of these new and amended HKFRSs did not result in significant changes to the Group's accounting policies. The specific transitional provisions contained in some of these new or amended HKFRSs have been considered.

2.1 New or amended HKFRSs that have been issued but are not yet effective

The Group has not early adopted the following HKFRSs that have been issued but are not yet effective. The directors of the Company anticipate that the adoption of such HKFRSs will not result in material financial impact on the Group's financial statements.

Amendment to HKAS 1	Presentation of Financial Statements - Capital Disclosures ¹
HKFRS 7	Financial Instruments: Disclosures ¹
HKFRS 8	Operating Segments ²
HK(IFRIC) Interpretation 7	Applying the Restatement Approach under HKAS 29 Financial Reporting in Hyperinflationary Economies ³
HK(IFRIC) Interpretation 8	Scope of HKFRS 2 ⁴
HK(IFRIC) Interpretation 9	Reassessment of Embedded Derivatives ⁵
HK(IFRIC) Interpretation 10	Interim Financial Reporting and Impairment ⁶
HK(IFRIC) Interpretation 11	Group and Treasury Share Transactions ⁷
HK(IFRIC) Interpretation 12	Service Concession Arrangements ⁸

¹ Effective for annual periods beginning on or after 1 January 2007

² Effective for annual periods beginning on or after 1 January 2009

³ Effective for annual periods beginning on or after 1 March 2006

⁴ Effective for annual periods beginning on or after 1 May 2006

⁵ Effective for annual periods beginning on or after 1 June 2006

⁶ Effective for annual periods beginning on or after 1 November 2006

⁷ Effective for annual periods beginning on or after 1 March 2007

⁸ Effective for annual periods beginning on or after 1 January 2008

3. REVENUE AND OTHER REVENUE

Revenue, which is also the Group's turnover, represents total invoiced value of goods supplied and income from provision of services rendered. Revenue and other revenue recognised during the year are as follows:

	2006 <i>HK\$'000</i>	2005 <i>HK\$'000</i>
Revenue		
Sale of smart card products, software and hardware	41,123	38,125
Smart card related services	<u>2,042</u>	<u>728</u>
	<u>43,165</u>	<u>38,853</u>

	2006 <i>HK\$'000</i>	2005 <i>HK\$'000</i>
Other revenue		
Forfeiture of deposits	—	211
Government grants received	—	707
Interest income	230	231
Sundry income	<u>52</u>	<u>14</u>
	<u>282</u>	<u>1,163</u>

4. OTHER NET LOSS

	2006 <i>HK\$'000</i>	2005 <i>HK\$'000</i>
Net foreign exchange loss	196	120
Loss on disposal of plant and equipment	<u>—</u>	<u>33</u>
	<u>196</u>	<u>153</u>

5. SEGMENT INFORMATION

Primary reporting format - business segments

During the year, the Group was principally engaged in the development, sale and distribution of smart card products, software and hardware and the provision of smart card related services to its customers.

Year ended 31 December 2006

	Development, sale and distribution of smart card products, software and hardware <i>HK\$'000</i>	Provision of smart card related services <i>HK\$'000</i>	Total <i>HK\$'000</i>
Revenue	<u>41,123</u>	<u>2,042</u>	<u>43,165</u>
Segment result and operating profit	2,541	1,419	3,960
Finance costs			<u>(206)</u>
Segment result and profit before income tax			3,754
Income tax expense			<u>(1,190)</u>
Profit for the year			<u>2,564</u>
Capital expenditure	3,209	—	3,209
Depreciation and amortisation	2,307	—	2,307
Reversal of impairment loss on development costs	(124)	—	(124)
Non-cash expenses other than depreciation and amortisation	<u>11</u>	<u>—</u>	<u>11</u>

Year ended 31 December 2005

	Development, sale and distribution of smart card products, software and hardware <i>HK\$'000</i>	Provision of smart card related services <i>HK\$'000</i>	Total <i>HK\$'000</i>
Revenue	<u>38,125</u>	<u>728</u>	<u>38,853</u>
Segment result and operating (loss)/profit	(2,472)	479	(1,993)
Finance costs			<u>(149)</u>
Segment result and loss before income tax			(2,142)
Income tax credit			<u>2,338</u>
Profit for the year			<u>196</u>
Capital expenditure	4,977	—	4,977
Depreciation and amortisation	2,058	—	2,058
Impairment loss on development costs	409	—	409
Non-cash expenses other than depreciation and amortisation	<u>488</u>	<u>—</u>	<u>488</u>

Over 90% of the segment assets and liabilities are attributable to the segment of “Development, sale and distribution of smart card products, software and hardware” and, accordingly, no segmental analysis of the Group’s assets, liabilities and capital expenditure is presented.

Secondary reporting format - geographical segments

The Group’s operations are located in Hong Kong. The following table provides an analysis of the Group’s revenue by geographical market irrespective of the origin of the goods and services.

Sales revenue by geographical markets:

	2006 <i>HK\$'000</i>	2005 <i>HK\$'000</i>
The Americas	5,545	4,433
Asia Pacific	16,644	15,424
Europe, Middle East and Africa	<u>20,976</u>	<u>18,996</u>
	<u>43,165</u>	<u>38,853</u>

Over 90% of the total assets and liabilities of the Group at the respective balance sheet dates were physically located in Hong Kong and substantially employed in Hong Kong. Accordingly, no geographical segmental analysis of the Group’s assets and liabilities and capital expenditure is presented.

6. PROFIT/(LOSS) BEFORE INCOME TAX

	2006 <i>HK\$'000</i>	2005 <i>HK\$'000</i>
Profit/(Loss) before income tax is arrived at after charging/(crediting):		
6.1 Finance costs:		
Interests on bank borrowings wholly repayable within five years	45	—
Bank charges	<u>161</u>	<u>149</u>
	<u>206</u>	<u>149</u>
6.2 Other items:		
Amortisation of development costs	1,339	1,189
Auditors' remuneration	264	267
Cost of inventories recognised as expense	19,765	20,601
Depreciation	968	869
Impairment loss on development costs	—	409
Impairment of trade receivables	9	46
Reversal of impairment loss on development costs	(124)	—
Reversal of write-down of inventories	(540)	—
Write-back of impairment of trade receivables	(134)	(164)
Write-down of inventories to net realisable value	—	355
Write-off of bad debts	1	87
Operating lease charges on land and buildings	1,318	1,890
Less: Amount included in research and development costs	<u>(112)</u>	<u>(226)</u>
	<u>1,206</u>	<u>1,664</u>

6.3 Research and development costs:

Research and development costs amounting to HK\$4,049,000 (2005: HK\$4,821,000) for the year have been calculated to the extent that staff costs and direct overheads can be allocated by management on a reasonable basis to research and development activities. Included in the total costs of HK\$4,049,000 (2005: HK\$4,821,000) were amounts of HK\$2,460,000 (2005: HK\$3,526,000) capitalised during the year.

Other costs such as depreciation of plant and equipment and indirect overheads have not been included within research and development costs.

7. INCOME TAX (EXPENSE)/CREDIT

No provision for Hong Kong profits tax has been made in the financial statements as a subsidiary of the Group has losses brought forward from previous years to offset against its current year's assessable profits and the Company and other subsidiaries sustained losses for taxation purposes for the years ended 31 December 2005 and 2006.

No provision for overseas taxation has been made as no assessable profits arose from the operations in the PRC, Philippines and Canada during the year ended 31 December 2006 (2005: Nil).

	2006 <i>HK\$'000</i>	2005 <i>HK\$'000</i>
Deferred tax		
Current year	<u>1,190</u>	<u>(2,338)</u>
Income tax expense/(credit)	<u>1,190</u>	<u>(2,338)</u>

8. DIVIDENDS

The Company had not declared or paid any dividends during the year ended 31 December 2006 (2005: Nil).

9. EARNINGS PER SHARE

The calculations of the basic and diluted earnings per share is based on the following data:

	2006 <i>HK\$'000</i>	2005 <i>HK\$'000</i>
Profit for the year for the purposes of calculating basic and diluted earnings per share	<u>2,564</u>	<u>196</u>
	'000	'000
Number of shares		
Weighted average number of ordinary shares for the purposes of calculating basic earnings per share	<u>281,800</u>	<u>281,800</u>
Effect of dilutive potential ordinary shares relating to outstanding share options	<u>129</u>	
Weighted average number of ordinary shares for the purposes of calculating diluted earnings per share	<u>281,929</u>	

Diluted earnings per share for the year ended 31 December 2005 was not presented because the exercise prices of the outstanding options exceeded the average market price of the Company's ordinary shares during the year and, accordingly, there was no dilutive effect on the basic earnings per share.

10. DEFERRED TAX ASSETS

10.1 Deferred tax assets and liabilities recognised

Deferred taxation is calculated in full on temporary differences under the liability method using a principal taxation rate of 17.5% (2005: 17.5%).

The components of deferred tax assets and liabilities recognised in the consolidated balance sheet and the movements during the year are as follows:

	Accelerated tax depreciation <i>HK\$'000</i>	Tax losses <i>HK\$'000</i>	Total <i>HK\$'000</i>
At 1 January 2005	(109)	1,723	1,614
(Charged)/Credited to the income statement	<u>(102)</u>	<u>2,440</u>	<u>2,338</u>
At 31 December 2005 and 1 January 2006	(211)	4,163	3,952
Credited/(Charged) to the income statement	<u>33</u>	<u>(1,223)</u>	<u>(1,190)</u>
At 31 December 2006	<u>(178)</u>	<u>2,940</u>	<u>2,762</u>

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when the deferred income taxes relate to the same tax authority. The offset amounts are as follows:

	2006 <i>HK\$'000</i>	2005 <i>HK\$'000</i>
Deferred tax assets	2,940	4,163
Deferred tax liabilities	<u>(178)</u>	<u>(211)</u>
Deferred tax assets recognised in the consolidated balance sheet	<u>2,762</u>	<u>3,952</u>

Deferred tax assets are recognised for tax losses carried forward to the extent that realisation of the related tax benefit through the future taxable profits is probable. As at 31 December 2006, the Group recognised deferred tax assets arising from the future benefit of tax losses in the amount of HK\$2,940,000 (2005: HK\$4,163,000).

10.2 Deferred tax assets and liabilities unrecognised

Unrecognised deferred tax assets, representing the future benefit of tax losses to the extent that the directors do not consider it probable that sufficient taxable profits will be available in the foreseeable future, amounted to HK\$215,000 (2005: HK\$505,000). The tax losses do not expire under current tax legislation. There were no unrecognised deferred tax liabilities.

11. TRADE AND OTHER RECEIVABLES, DEPOSITS PAID AND PREPAYMENTS

	2006 <i>HK\$'000</i>	2005 <i>HK\$'000</i>
Trade receivables	6,440	6,239
Less: Impairment of receivables	<u>(1,072)</u>	<u>(1,197)</u>
Trade receivables — net	5,368	5,042
Other receivables	117	120
Deposits paid	529	467
Prepayments	<u>739</u>	<u>474</u>
	<u>6,753</u>	<u>6,103</u>

As at 31 December 2006, the amount of other receivables, deposits paid and prepayments expected to be recovered after more than one year is HK\$109,000 (2005: HK\$383,000).

Customers are generally granted credit terms of 30 to 60 days. As at 31 December 2006, the ageing analysis of net trade receivables was as follows:

	2006 <i>HK\$'000</i>	2005 <i>HK\$'000</i>
0 - 30 days	2,993	4,577
31 - 60 days	777	143
61 - 90 days	36	37
Over 90 days	<u>1,562</u>	<u>285</u>
	<u>5,368</u>	<u>5,042</u>

The Group has recognised a loss of HK\$9,000 (2005: HK\$46,000) for the impairment of its trade receivables during the year ended 31 December 2006. The loss has been included in “Administrative expenses” in the consolidated income statement.

12. TRADE AND OTHER PAYABLES, DEPOSITS RECEIVED AND ACCRUALS

	2006 <i>HK\$'000</i>	2005 <i>HK\$'000</i>
Trade payables	1,871	3,449
Deposits received	922	1,413
Accruals	<u>1,679</u>	<u>1,268</u>
	<u>4,472</u>	<u>6,130</u>

All of the deposits received and accruals are expected to be settled within one year of the balance sheet date.

At 31 December 2006, the ageing analysis of trade payables was as follows:

	2006 <i>HK\$'000</i>	2005 <i>HK\$'000</i>
0 — 30 days	1,833	2,856
31 — 60 days	38	393
61 — 90 days	—	114
Over 90 days	<u>—</u>	<u>86</u>
	<u>1,871</u>	<u>3,449</u>

SCOPE OF WORK OF GRANT THORNTON

The figures in respect of the Annual Results Announcement (“Announcement”) of the Company for the year ended 31 December 2006 have been agreed by the Company’s auditors, Grant Thornton, to the amounts set out in the Company’s consolidated financial statements for the year. The work performed by Grant Thornton in this respect did not constitute an assurance engagement in accordance with Hong Kong Standards on Auditing, Hong Kong Standards on Review Engagements or Hong Kong Standards on Assurance Engagements issued by the Hong Kong Institute of Certified Public Accountants and consequently no assurance has been expressed by Grant Thornton on the Announcement.

MANAGEMENT DISCUSSION AND ANALYSIS

The following discussion and analysis should be read along side with the Group's audited financial statement for the year ended 31 December 2006.

FINANCIAL REVIEW

The total sales of the Group increased 11% to HK\$43.2 million in the year ended 31 December 2006 from HK\$38.9 million in the previous year. The sales of PC linked reader in quantity remained to be about the same in 2006 as in 2005 but the dollar amount dropped by 17% owing to decrease in the selling price. The product line of PC linked readers has been the cash cow and the profits generated from it have funded the development of new products. The growth in the sales of smart cards and other products, respectively at 41% and 68% reflected the successful introduction of new products, such as ACOS5 PKI cards.

	For the year ended 31 December		Change
	2006 <i>HK\$' million</i>	2005 <i>HK\$' million</i>	
Smart cards	7.6	5.4	+41%
PC linked readers	21.1	25.3	-17%
Other products	<u>12.4</u>	<u>7.4</u>	+68%
	41.1	38.1	
Smart card related services	<u>2.1</u>	<u>0.8</u>	+163%
	<u>43.2</u>	<u>38.9</u>	

The Group managed to expand its sales in all the three regions, "Europe, Middle East and Africa", "Asia Pacific" and "The Americas". "The Americas" still remain to be the smallest region in term of the Group's sales figures. The Group had some successes in penetrating into the Latin American market such as the Brazilian and the Costa Rican markets. The biggest American market is in USA, mainly for smart card products used by the government departments. The Group is endeavouring to have its products customized to fit the requirements of the USA government.

	For the year ended 31 December		Change
	2006 <i>HK\$' million</i>	2005 <i>HK\$' million</i>	
Europe, Middle East and Africa	21.0	19.0	+11%
Asia Pacific	16.6	15.4	+8%
The Americas	<u>5.6</u>	<u>4.5</u>	+24%
	<u>43.2</u>	<u>38.9</u>	

Owing mainly to the introduction of innovative new products, the Group increased its gross profit margins to 53% in 2006 from 44% in 2005.

The total operating expenses and finance costs for 2006 amounted to HK\$19.4 million compared with HK\$20.2 million in 2005. Staff costs increased in 2006 by HK\$1.2 million. Such an increase was compensated by the reduction in office rental expenses and legal and professional expenses. As a result, the total operating expenses and finance costs did not increase.

DIVIDEND

The board of directors (the “Board”) does not recommend the payment of a final dividend in respect of the year ended 31 December 2006. The declaration, payment and amount of future dividends will be at the discretion of the Board and will depend upon, among other things, the Group’s results of operations, capital requirements, cash flows, general financial conditions and such other factors as the Board may deem relevant.

BUSINESS REVIEW

In 2006, the Group took various measures to grow its business profitably, to manage its cash flow and to enhance its infrastructure in order to ensure its long-termed viability and prosperity in the smart card industry.

New products launched

Three main products were launched to the market in 2006. They are:

- (1) ACR88, the portable PIN-pad smart card reader with display and with optional finger print scanner and optional contactless reader. There is a wide range of applications of this device, notably for national health card schemes and ID card schemes. The Hong Kong Immigration is the first customer of this product and they use the device to read the Hong Kong Identity Cards.
- (2) the ACR100, a flash drive integrated with a PC linked reader. The device has the full functions of the popular flash drive and additionally provides security function and payment function by virtue of the SIM-sized smart card inserted in it. Before the product was launched, a mobile phone operator in Asia ordered ten thousand units for their pilot project to enable subscribers to use their special VoIP services.
- (3) ACOS5 card, a PKI (Public Key Infrastructure) smart card. Such cards are used in high security applications, e.g. for access to the Internet for home banking, on-line transactions, e-government services, etc.

Even though the sales of these products did not account for a significant percent of the total sales of the Group in 2006, these products were warmly accepted in the market and they created good potential of substantial sales in year 2007 and beyond.

Development of new products started in 2006

In 2006, the Group started to develop a few new products. They are:

- (1) CryptoMate, a USB PKI token with an embedded smart card chip for extra convenience and security in access control to the Internet and PC networks. It combines the simplicity of a USB device with the capabilities of a cryptographic smart card and an integrated reader. It is ideal for applications such as enterprise banking, e-Commerce, Internet access, computer access control, etc.
- (2) APG82, a dynamic password generator which generates one time password to provide a means of authentication in non face-to-face transactions, both online and offline.
- (3) eH880, a multi-function smart reader using a 32-bit microprocessor. The eH880 is a secure and feature-rich smart card terminal and is used for various purposes with the initial target use in the German national health card project. This innovative device is capable of facilitating secure mutual authentications (e.g. between a doctor's and patient's card), displaying detailed multi-layered information from one or both cards based on embedded access rights, and facilitating various online and offline transactions through both private and public network infrastructures.

Smart card and security projects in the world using the Group's products

In 2006, the Group secured business on a world-wide basis for a variety of projects with examples mentioned below:

Developing specialized smart card reader for a global company

In 2006, the Group succeeded in concluding an agreement with a global company to develop, manufacture and provide support, for a smart card reader accepting contactless smart card and finger print for physical access control, after the global company evaluated prototypes of the device the Group developed for them. This global company is among the world's leading providers of full access control systems. The Group is completing the product development while the customer is building the system software. Once the device is fully commercialized, substantial income can be expected.

Belgium National ID cards using smart card readers, ACR38 from the Group

The Group continued to supply its PC linked readers, ACR38, to ZETES SA, the prime contractor for the Belgian National Identity Cards using smart cards. The Group has supplied a substantial volume of readers to them in 2005 and 2006 and their requirement of readers has been extended to 2007.

VoIP applications for a GSM mobile phone operator using the Group ACR100, flash drive integrated with a PC linked reader

The Group delivered 10,000 units of ACR100 to a GSM mobile phone operator in a Southeast Asian country which provides the device to their subscribers for making long distance calls using specialized programs stored securely in the flash by virtue of the SIM-sized smart card inserted into ACR100. The subscribers will pay a fee on the use of services for making phone calls or using PC in public areas. If the operator is successful with their pilot runs using 10,000 units of ACR100, the Group can expect bigger volume of purchase from them.

Customer loyalty program in Kenya

In 2006, the Group received an order of 100,000 units of ACOS5 cards for multi-function loyalty programs for a supermarket store chain in Kenya. The project will be rolled out in East and Central Africa. The Group supplied 20,000 cards to them in the first quarter of 2007 and will continue to supply the cards in the rest of 2007. The project represents a new market penetration into this African country better known for its rich wildlife.

Contactless smart card reader for Internet café in Korea

The Group supplied over one thousand units of ACR120, contactless smart card reader and over ten thousand units of contactless cards to a system integrator in Korea for the management of payment in Internet café. The world consumption of contactless smart card readers in quantity is still small compared with that of contact smart card readers but it is rapidly increasing.

Promotion

In 2006, the Group continued to participate in various smart card and security trade shows in the world as it had done in the previous years. These shows were:

- March: “CeBIT Hannover 2006” in Germany;
- April: “The 8th international Smart card Technology, Application Conference & Products Exhibition, 2006” in Shenzhen;
- April: “Hong Kong Electronics (Spring Edition)” in Hong Kong;
- May: “CardTech/SecureTech 2006” in the USA;
- May: “The 9th International fair of smart card, China (SCC) 2006” in Beijing;
- July: “CardEx Asia 2006” in Malaysia;
- November: “Cartes & IT Security” in France;
- November: “The 15th Annual Governmentware 2006” in Singapore; and
- December: “2006 China (Guangzhou) Card Expo And Summit of Card Industry” in Guangzhou.

The Group will continue to take part in trade shows in the world in order to secure new customers and meet existing customers spread out all over the world.

Industry awards

In July 2006, the Group won the D'ucoty's "Product Innovation Award in Telecommunications" as a recognition by the smart card industry of its development and launching of the innovative product ACR100 which integrates a flash drive with a PC linked reader. The awards were established by the publisher of the magazine "CardsNow!Asia" and the organizer of the trade show "CardEX Asia". The purpose of the awards is to recognize individuals and companies that demonstrated outstanding performance in the smart card industry throughout the Asia Pacific region. The Group received in September 2006, Frost & Sullivan's "World Business Development Strategy Leadership" award as a recognition of the Group's success in spreading its PC linked readers to over 80 countries in the world for a big variety of applications.

Canadian subsidiary established

In 2006, the Group established a wholly owned subsidiary in Canada named "Advanced Card Systems (Canada) Limited". With the establishment of a subsidiary in Canada, it is expected that more sales can be made in Canada, an important market in "The Americas" region.

PROSPECTS

Since the establishment of the business in 1995, the mission of the management of the Group has been to turn the Group into a respectable global player in the smart card industry. Financial resources have always been a major constraint in the Group's attempt to attain an economy of scale. The Group has not reached this scale yet but has moved big steps in the direction toward this goal through several measures.

Staff costs represent some two-thirds of the total operating expenses of the Group. Therefore the Group emphasizes on managing the human resources expenses by (1) increasing the ratio of junior staff to senior staff and providing them, especially the junior staff members good training and (2) to make the best use of the strengths of the staff teams in the three locations of Hong Kong, Manila and Shenzhen. To allow staff members in different locations to work simultaneously on the same project (e.g. developing, testing and producing a sophisticated product), efficient communication methods and a good IT system are required. The Group has made good progress in its attempt to increase its communication effectiveness and to build a powerful web-based IT system.

Through eleven years of hard work and determination to succeed by dedicated staff members since the establishment of the business in 1995, the Group has built a base of satisfied customers, core competence in smart card readers and has figured out a business strategy. It has proven to be able to secure business from high-profiled projects including nation-wide projects usually initiated by governments despite keen competitions from the strongest global players.

The world market of the types of products in the Group's product portfolio is increasing as smart card systems provide convenience to citizens and protect the physical and intangible assets of people. Many applications of smart cards are getting popular in the world. Examples are (1) using contactless smart cards for the payment of fare (2) using smart cards to go through immigration check-point by verification of finger print stored in the smart cards (3) waving a contactless smart card to enter a building (4) using a contact smart card for accessing the Internet network for banking services, for micro-payments or for on-line

commercial transactions and (5) using a smart card, a dynamic password generator or a finger print scanner to authenticate a person for accessing a web-server for confidential or valuable information, just to mention a few. The Group will definitely reap the benefits from the growth of the industry.

Within the constraint of limited financial resources to compete in the world market for smart card products, the Group's priority has to achieve profitability and to attain a positive cash flow. The Group managed to make a small net profit after income tax in 2006 and increased slightly its cash position at 31 December 2006 compared with the position a year ago.

Once the Group reaches its economy of scale, the growth of sales and profitability will accelerate.

LIQUIDITY AND FINANCIAL RESOURCES

As at 31 December 2006, the Group's cash at banks and on hand amounted to HK\$7.9 million (2005: HK\$7.1 million) which included the pledged bank deposits of HK\$2.7 million (2005: HK\$0.7 million). Out of the HK\$2.7 million pledged bank deposits, HK\$0.7 million was pledged for a performance bond issued by a bank to a customer who gave the Group a prepayment for ordering the Group's products being developed. The balance of HK\$2.0 million was to secure bank credit lines. At 31 December 2006, no credit line has been utilized (2005: Nil).

The current ratio, being the ratio of current assets to current liabilities, was kept at 5.2 (2005: 3.6). Net asset value as at the year end date was HK\$32.9 million (2005: HK\$30.4 million). As at 31 December 2006, the Group did not have any borrowings and, accordingly, the gearing ratio was zero (2005: zero).

CAPITAL STRUCTURE

The Group relies on internal resources and the net proceeds from the Placing as a source of funding. The Group keeps most of its cash in Hong Kong dollars and United States dollars in bank accounts as working capital for the Group.

INVESTMENTS

During the year, the Group did not hold any significant investments.

ACQUISITIONS AND DISPOSALS OF SUBSIDIARIES AND AFFILIATED COMPANIES

The Group did not have any material acquisitions or disposals of subsidiaries and affiliated companies during the year ended 31 December 2006.

EXPOSURE TO EXCHANGE RATE FLUCTUATIONS

The assets, liabilities and transactions of the Group are primarily denominated in Hong Kong dollars or United States dollars and the exchange rates between such currencies have been stable during the year. There is no significant exposure to foreign exchange rate fluctuations. No hedging or other alternatives have been implemented during the year.

PLEDGE OF ASSETS

As at 31 December 2006, the Group pledged a deposit of US\$88,000 to a bank for the bank to issue a performance bond to a customer. This customer paid the Group US\$88,000 as partial advanced payment when they placed the Group an order of 10,000 units of ACR100 (the flash drive integrated with a smart card reader) before the product was developed. In addition, the Group pledged deposits of US\$257,000 to two banks for banking facilities. Save as disclosed herein, the Group did not pledge any of its assets.

CONTINGENT LIABILITIES

As at 31 December 2006, the Company executed corporate guarantee of HK\$4 million (together with accrued interest thereon) to two banks in respect of banking facilities granted to a subsidiary. Save as disclosed herein, the Group did not have any significant contingent liabilities.

EMPLOYEES AND REMUNERATION POLICIES

As at 31 December 2006, the Group had 70 full time employees. Staff costs amounted to HK\$12.1 million (2005: HK\$10.9 million). Remuneration policies and packages for the Group's employees are based on individual qualifications, performance, experience and conditions prevailing in the industry. In addition, various training sessions are offered to employees to enhance their product and market knowledge.

The Group has also adopted share option schemes under which the employees of the Group may be granted share options to subscribe for shares in the Company for the purposes of recognising their contributions to the Group.

DIRECTORS' INTERESTS IN COMPETING BUSINESS

Based on the information available to the Company and within the knowledge and belief of the directors of the Company, none of the directors or the management shareholders of the Company (as defined under the GEM Listing Rules) have any interests in a business which competes or may compete with the business of the Group during the year.

PURCHASE, SALE OR REDEMPTION OF THE COMPANY'S LISTED SECURITIES

During the year, neither the Company nor its subsidiaries purchased, sold or redeemed any of the Company's listed shares.

THE CODE ON CORPORATE GOVERNANCE PRACTICES

During the year, the Company has applied the principles of the Code on Corporate Governance Practices as set out in Appendix 15 of the Rules Governing the Listing of Securities on the Growth Enterprise Market of the Stock Exchange of Hong Kong Limited (the “Code ”). The Company has complied with the requirements of the Code except for the provision A.2 of the Code. A.2 of the Code provides that the roles of chairman and chief executive officer should be separate and should not be performed by the same individual. Upon the resignation of Mr. Mak Chi Him as the chief executive officer of the Company effective on 3 May 2006, Mr. Wong Yiu Chu, Denny was then appointed as the chief executive officer and he is also the chairman of the Company. The roles of chairman and chief executive officer were not separated. The Board considers that this structure does not impair the balance of power and authority between the Board and the management of the Company. The Board also believes that his appointment being both the chairman and chief executive officer is beneficial to the business prospects of the Company.

AUDIT COMMITTEE

The Company has established an audit committee with written terms of reference in compliance with Rules 5.28 to 5.33 of the GEM Listing Rules. The audit committee comprises three independent non-executive directors namely, Mr. Yu Man Woon (being the chairman of the audit committee), Dr. Yip Chak Lam, Peter and Mr. Wong Yick Man, Francis and reports to the board of directors. The primary duties are to carry out the duties of reviewing and supervising the financial reporting process and internal control system of the Group. The audit committee met once with the external auditors to review the effectiveness of the internal control systems and the Group’s audited results for the year ended 31 December 2006.

By order of the Board of
Advanced Card Systems Holdings Limited
WONG Yiu Chu, Denny
Chairman

Hong Kong, 23 March 2007

As at the date of this announcement, the Board comprises 3 executive directors, namely Mr. Wong Yiu Chu, Denny, Mr. Tan Keng Boon and Ms. Tsui Kam Ling, Alice; and 3 independent non-executive directors, Dr. Yip Chak Lam, Peter, Mr. Yu Man Woon and Mr. Wong Yick Man, Francis.

This announcement will remain on the GEM website at <http://www.hkgem.com> on the “Latest Company Announcements” page for at least 7 days from the day of its posting.