

Advanced Card Systems Holdings Limited

龍傑智能卡控股有限公司*

(Incorporated in the Cayman Islands with limited liability)



INTERIM REPORT 2004



* For identification only

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This document, 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 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 document 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 document misleading; and (iii) all opinions expressed in this document have been arrived at after due and careful consideration and are founded on bases and assumptions that are fair and reasonable.

As at the date of this document, the Board comprises 3 Executive Directors, namely Mr. Wong Yiu Chu, Denny, Mr. Pang Wang Kee, Laurence and Mr. Tan Keng Boon; 1 Non-executive Director, Mr. Wan Wab Tong, Thomas; and 2 Independent Non-executive Directors, Dr. Yip Chak Lam, Peter and Mr. Cheong Chung Chin.

HIGHLIGHTS

- Turnover and gross profit of the Group for the six months ended 30 June 2004 decreased by approximately 16% to approximately HK\$11.9 million and approximately 29% to approximately HK\$5.5 million respectively from the six months ended 30 June 2003.
- The Group recorded loss attributable to shareholders of approximately HK\$2.98 million for the six months ended 30 June 2004 as compared to profit attributable to shareholders of approximately HK\$3.1 million for the six months ended 30 June 2003.
- Financial position of the Group remained strong, with cash and cash equivalents of approximately HK\$17.6 million and no borrowings.

MANAGEMENT DISCUSSION AND ANALYSIS

The Board of Directors (the "Board") hereby announces the unaudited consolidated results of the Company and its subsidiaries (collectively, the "Group" or "ACS") for the six months ended 30 June 2004 (the "Review Period").

The first half of the financial year 2004 was a time to plant seeds for ACS. The Group worked on strengthening its workforce and recruited high caliber professionals, and at the same time actively participated in international trade shows to explore new business opportunities for its latest products. The effective marketing efforts had led the Group to discuss a number of new projects with potential customers and some of which were close to conclusion and were expected to generate revenue for the Group in the near future.

Financial Review

Turnover of the Group for the six months ended 30 June 2004 was approximately HK\$11.9 million, representing a decrease of approximately 16% over the same period last year. During the period under review, a number of projects had been delayed. Of all the projects on hand, a few were wrapped up while the details of a few others were still being ironed out. Since not all the returns from the projects were realized, the Group had recorded a decline in turnover in the period.

Gross profit of the Group amounted to approximately HK\$5.5 million (2003: approximately HK\$7.8 million), and gross profit margin decreased from approximately 55% to approximately 46% mainly due to the increase in the costs of raw materials. To capture emerging opportunities, the Group had beefed up its sales and marketing, and product design and development teams. Total headcount of the Group increased by approximately two-third from 25 at 30 June 2003 to 42 at 30 June 2004 leading to 62% increase in staff cost in the first half of 2004 as compared to the corresponding period in 2003. Loss attributable to shareholders thus amounted to approximately HK\$2.98 million. However, management believes the strengthened workforce will make significant contribution to the Group's business growth by boosting its core competitiveness.

PC linked readers remained as the Group's major income source, generating revenue of approximately HK\$5.8 million for the Group. During the period under review, the Group actively diversified its product scope and as a result, the percentage of revenue contribution of PC linked readers gradually decreased from 68% in the corresponding period last year to 49% this year.

Looking at the geographical breakdown, Europe, Africa and the Middle East was the Group's major market and accounted for approximately 66% (2003: approximately 32%) of the total turnover in the first half of 2004 while Asia and the Americas accounted for approximately 26% (2003: approximately 52%) and approximately 8% (2003: approximately 16%) respectively.

Dividend

To retain more resources for business development, the Board does not recommend the payment of an interim dividend for the six months ended 30 June 2004.

Business Review

During the period under review, the Group proactively carried out more marketing activities. The Group participated in certain trade shows including CeBIT 2004 in Germany, the International ICT Expo in Hong Kong, and other shows in the US and China. These trade shows provided the avenue for the Group to meet with existing and potential customers, and to launch its latest products. The Group's *ACR38T*, an upgraded version of its PC linked readers, was launched and the first shipment of this new product to customers was made during the period under review.

ACS' PC linked readers were qualified for various government projects around the world even though it might take longer for a big project to reach its full implementation stage. The Group continued to supply PC linked readers to government or public entities in the US, Serbia and Montenegro, Taiwan and Hong Kong. In addition to PC linked readers, the Group started the development of contactless smart card reader *ACR120* and smart card/finger print reader *BioTrustKey* and diversified the Group's product portfolio during the period under review.

The additional talents recruited during the period under review significantly strengthened the Group, with its sales and marketing team having the strongest personnel boost, allowing the Group to respond promptly to customers' requirement. During the period under review, the Group started to assign sales professionals to focus on specific geographical regions, identifying key customers in each region. The new service model added flexibility to the Group operations and allowed it to offer more comprehensive solutions to customers and capture more businesses.

Prospects

Leveraging its global exposure, ACS will adopt a more proactive approach in identifying key customers. The national identity card projects in Serbia and Montenegro and the project with eMedical ID are in progress, and the launch of the smart card based electronic identity card in Hong Kong is generating a steady demand for the Group's PC linked readers. With more governments adopting smart card based security solutions for information management and authentication of identity, ACS will be able to accumulate more experience in the provision of those solutions and in turn gain strength and flexibility in customizing solutions for potential customers including governments and public entities around the world.

Apart from PC linked readers, the Group is expanding the range of its products. It has successfully integrated its finger print authentication technology with smart card reader technology. Its latest finger print reader is receiving positive response from the market. The Group expects this new product will account for a bigger share of the Group's total turnover.

The Group sees opportunities in emerging countries like India, Indonesia and the Philippines. Therefore, in addition to the sales and marketing team in Hong Kong, it is completing the necessary legal procedures to set up an office in Manila. This move allows the Group to remain competitive in terms of price and services, and has contributed to its securing of more businesses in these emerging countries.

A few existing projects will be completed in the second half of the financial year 2004 and directly contribute to the Group's top line. The contribution from new customers will be reflected in the second half of the financial year.

Liquidity and Financial Resources

As at 30 June 2004, the Group's cash and cash equivalents amounted to approximately HK\$17.6 million (30 June 2003: approximately HK\$0.9 million). The Group continued to operate under a debt-free status with no outstanding net debt as at 30 June 2004.

The current ratio, being the ratio of current assets to current liabilities, was maintained at a strong level of 6.6 (30 June 2003: 2.3). Net asset value as at the end of the review period was approximately HK\$41.2 million (30 June 2003: approximately HK\$16.5 million). As at 30 June 2004, the Group did not have any borrowing and, accordingly, the gearing ratio was zero (30 June 2003: zero).

Capital Structure

The Group relies on internal resources and the net proceeds from the Placing referred to in its prospectus dated 31 October 2003 as its sources of funding. Most of its cash for use as working capital is kept in bank accounts in Hong Kong and United States dollars.

Investments

During the first six months, the Group did not hold any significant investments.

Acquisitions and Disposals of Subsidiaries and Affiliated Companies

The Group did not make any material acquisitions or disposals of subsidiaries and affiliated companies during the six months ended 30 June 2004.

Exposure to Exchange Rate Fluctuations

The assets, liabilities and transactions of the Group are primarily denominated in Hong Kong or United States dollars and the exchange rates of the currencies have been stable during the review period. Hence, there was no significant exposure to foreign exchange rate fluctuations. No hedging or other alternatives were implemented during the period.

Pledge of Assets

As at 30 June 2004, the Group did not pledge any of its assets.

Contingent Liabilities

The Group did not have any significant contingent liabilities as at 30 June 2004.

Employees and Remuneration Policies

As at 30 June 2004, the Group had 42 full-time employees compared to headcount of 25 as at 30 June 2003. Staff costs charged to the consolidated profit and loss account amounted to approximately HK\$4.2 million (2003: approximately HK\$2.6 million). Remuneration policies and packages for the Group's employees are based on individual qualification, performance, experience and prevalent practice in the industry. In addition, various training sessions are offered to employees to enhance their product and market knowledge.

The Group also adopts share option schemes under which employees with contributions to the Group may be granted share options.

REVIEW OF BUSINESS OBJECTIVES

Business Progress

The following is a comparison of the business objectives as set out in the prospectus dated 31 October 2003 and the actual business progress for the period from 1 January 2004 to 30 June 2004.

Business objectives as stated in the prospectus dated 31 October 2003

Enhancing the PC linked readers and developing new products

Strengthening and developing industry alliances

Enhancing the design of customised products with a view to developing more generic products

Expansion of the Group's sales network

Actual business progress for the period from 1 January 2004 to 30 June 2004

ACR38T, an upgraded version of the Group's PC linked readers, was launched to the market in April 2004.

Chip Card Interface Device ("CCID") reader will be enhanced to support Linux driver. The product development period will be lengthened by three months in order to have the above-mentioned enhanced function. The expected launch date will be subsequently extended to the fourth quarter of 2004.

The Group strengthened its relationship with an IT solution house in Indonesia to promote *ACOS2* cards and integrated finger print and reader scanners to bank in the country. Initial orders were secured.

The Group is adding a special feature to its PC linked reader *ACR38T* so that along with a smart card it can be used as a device for physical access (e.g. door access) control as well as for logical access (e.g. PC access) control.

The Group participated in five trade shows in Germany, the United States, China (Shenzhen and Beijing) and Hong Kong. The Group continued to strengthen the sales network by employing additional six sales and marketing people in Hong Kong. The Group will also set up a sales team in the Manila office to serve the emerging countries like India, Pakistan, Indonesia and Africa in a cost effective manner.

The Group delayed the opening of the the office in Guangdong, China. The opening of the new office will depend on the bussiness expansion in China.

**Business objectives
as stated in the prospectus
dated 31 October 2003**

Enhancing research and development capacity

Exploring additional commercial applications

Building on new market opportunities

Catering to the needs of small and medium-sized customers

**Actual business progress
for the period from
1 January 2004 to 30 June 2004**

The Group recruited four new members to join the product design and development team in Hong Kong.

The new office in Manila, the Philippines will be opened in July 2004. This office will be engaged in developing smart card operating systems and smart card reader related software.

The Group finished the prototyping of the finger print module for access to safes by the touch of a finger.

The Group has strengthened its influence to the Middle East and South American market. Important customers there included a solution house in the United Arab Emirates and a bank ATM manufacturer in Brazil.

The Group finished the packaging of the software development kits ("SDK") for the smart card/finger print readers like *BioTrustKey* and *BioCardKey*.

Use of Proceeds

The net proceeds from the placing of shares upon the listing of the Company which remains unutilized as at 30 June 2004 amounted to approximately HK\$14.3 million.

For the period from 1 January 2004 to 30 June 2004:

	Budgeted <i>HK\$'million</i>	Actual <i>HK\$'million</i>
Product development (<i>Note 1</i>)	2.9	0.9
Sales and marketing	0.5	0.5
Patent copyright and trademark registration	0.1	0.0
Management information system (<i>Note 2</i>)	0.5	0.3
Human resources	0.1	0.1
Relocation of Hong Kong office	0.4	0.4
General working capital	0.4	0.0
	4.9	2.2
	4.9	2.2

Notes:

- The reduction in development cost is owing to the better utilization of the existing engineering resources than initially budgeted and to the delay of the development of *Cbina Tax Terminal*.
- Instead of acquiring a brand new Management Information System, the existing system was enhanced to accommodate the Group's business expansion at a lesser cost than the budgeted expenses as this enhanced system is considered to be adequate for a period of time.

UNAUDITED CONSOLIDATED PROFIT AND LOSS ACCOUNT

For the three months and six months ended 30 June 2004

	Note	Three months ended		Six months ended	
		30 June		30 June	
		2004	2003	2004	2003
		HK\$'000	HK\$'000	HK\$'000	HK\$'000
Turnover	2	4,571	9,639	11,894	14,190
Cost of sales		(2,495)	(4,383)	(6,404)	(6,432)
		<u>2,076</u>	<u>5,256</u>	<u>5,490</u>	<u>7,758</u>
Other revenue		23	20	49	28
Other net income / (loss)		5	2	(14)	10
Operating expenses					
Staff costs		(2,291)	(1,401)	(4,243)	(2,626)
Depreciation		(167)	(145)	(306)	(286)
Amortisation of development costs		(539)	(339)	(971)	(656)
Other operating expenses		(1,582)	(414)	(2,923)	(1,124)
		<u>(2,475)</u>	<u>2,979</u>	<u>(2,918)</u>	<u>3,104</u>
(Loss) / profit from operations					
Finance costs		(29)	(26)	(64)	(48)
		<u>(2,504)</u>	<u>2,953</u>	<u>(2,982)</u>	<u>3,056</u>
(Loss) / profit from ordinary activities before taxation					
Income tax	3	—	—	—	—
		<u>(2,504)</u>	<u>2,953</u>	<u>(2,982)</u>	<u>3,056</u>
(Loss) / profit from ordinary activities after taxation and attributable to shareholders					
(Loss) / earnings per share					
- Basic	5	<u>(0.891) cents</u>	<u>1.462 cents</u>	<u>(1.063) cents</u>	<u>1.513 cents</u>
- Diluted	5	<u>N/A</u>	<u>N/A</u>	<u>N/A</u>	<u>N/A</u>

CONSOLIDATED BALANCE SHEET

At 30 June 2004

Advanced Card Systems Holdings Limited

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	<i>Note</i>	Unaudited 30 June 2004 HK\$'000	Audited 31 December 2003 HK\$'000
Non-current assets			
Fixed assets	7	1,502	832
Development costs	8	10,165	9,098
Deferred tax assets		1,614	1,614
		<u>13,281</u>	<u>11,544</u>
Current assets			
Inventories		7,848	5,738
Accounts receivable	9	6,397	12,071
Other receivables, deposits and prepayments		1,012	1,290
Cash and cash equivalents		17,581	21,456
Total current assets		<u>32,838</u>	<u>40,555</u>
Current liabilities			
Accounts payable	10	3,282	5,665
Other payables, deposits and accruals		1,669	2,446
Total current liabilities		<u>4,951</u>	<u>8,111</u>
Net current assets		<u>27,887</u>	<u>32,444</u>
NET ASSETS		<u>41,168</u>	<u>43,988</u>
CAPITAL AND RESERVES			
Share capital	11	28,180	28,000
Reserves	12	12,988	15,988
		<u>41,168</u>	<u>43,988</u>

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the six months ended 30 June 2004

	<i>Note</i>	Unaudited	
		Six months ended 30 June	
		2004	2003
		<i>HK\$'000</i>	<i>HK\$'000</i>
Shareholders' equity at 1 January		<u>43,988</u>	<u>13,422</u>
(Loss) / profit for the period	12	<u>(2,982)</u>	<u>3,056</u>
Shares issued upon conversion of share options:			
Share capital	11	180	—
Share premium	12	<u>(18)</u>	<u>—</u>
Net increase in shareholders' equity arising from conversion of share options		<u>162</u>	<u>—</u>
Shareholders' equity at 30 June		<u><u>41,168</u></u>	<u><u>16,478</u></u>

CONDENSED CONSOLIDATED CASH FLOW STATEMENT
For the six months ended 30 June 2004

	Unaudited	
	Six months ended 30 June	
	2004	2003
	HK\$'000	HK\$'000
Net cash (used in) / generated from operating activities	(928)	825
Net cash used in investing activities	(3,045)	(2,020)
Net cash generated from / (used in) financing activities	98	(48)
	<hr/>	<hr/>
Net decrease in cash and cash equivalents	(3,875)	(1,243)
Cash and cash equivalents at 1 January	21,456	2,119
	<hr/>	<hr/>
Cash and cash equivalents at 30 June	17,581	876
	<hr/> <hr/>	<hr/> <hr/>

NOTES ON THE CONDENSED INTERIM FINANCIAL STATEMENTS

1 Basis of Preparation of the Condensed Interim Financial Statements

The unaudited condensed interim financial statements have been prepared in accordance with Statement of Standard Accounting Practice 25 "Interim Financial Reporting" issued by the Hong Kong Society of Accountants, and the applicable disclosure provisions of the Rules Governing the Listing of Securities on the Growth Enterprise Market of The Stock Exchange of Hong Kong Limited. The condensed interim financial statements should be read in conjunction with the 2003 annual financial statements.

The same accounting policies adopted in the 2003 annual financial statements have been applied to the condensed interim financial statements.

The condensed interim financial statements are unaudited but have been reviewed by the audit committee of the Company.

2 Turnover

Turnover represents the invoiced value of sales to customers less discounts and returns during the period.

	Three months ended		Six months ended	
	30 June		30 June	
	2004	2003	2004	2003
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Sales of smart card products, software and hardware	4,482	9,046	10,531	13,222
Smart card related services	89	593	1,363	968
	<u>4,571</u>	<u>9,639</u>	<u>11,894</u>	<u>14,190</u>

3 Income Tax

No provision for Hong Kong Profits Tax has been made as there were no assessable profits during the three months and six months ended 30 June 2004.

4 Dividends

The Company had not declared or paid any dividend during the three months and six months ended 30 June 2004 (2003: HK\$Nil).

5 (Loss) / Earnings Per Share

The calculation of basic (loss) / earnings per share for the three months and six months ended 30 June 2004 is based on the respective unaudited loss attributable to shareholders of HK\$2,504,000 and HK\$2,982,000 (2003: unaudited profit attributable to shareholders of HK\$2,953,000 and HK\$3,056,000) and the weighted average of 280,890,236 and 280,445,118 (2003: 202,000,000 and 202,000,000) ordinary shares outstanding after the issuance of shares prior to the Listing as if those shares had been outstanding from 1 January 2003.

No diluted (loss) / earnings per share is presented for the three months and six months ended 30 June 2004 and 30 June 2003 as there were no dilutive potential ordinary shares during these periods.

6 Segment Information

Segment information is presented in respect of the Group's business and geographical segments. Business segment information is chosen as the primary reporting format because this is more relevant to the Group in making operating and financial decisions.

(a) Business segments

During the period, 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 customers.

Six months ended 30 June 2004

	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>
Turnover	10,531	1,363	11,894
Other revenue - unallocated			49
			<u>11,943</u>
Segment results and loss from operations			(2,918)
Finance costs			(64)
			<u>(2,982)</u>
Loss from ordinary activities before taxation			(2,982)
Taxation			—
			<u>(2,982)</u>
Loss from ordinary activities after taxation			(2,982)
Depreciation and amortisation	1,277	—	1,277
	<u>1,277</u>	<u>—</u>	<u>1,277</u>

	Development, sale and distribution of smart card products, software and hardware	Provision of smart card related services	Total
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Turnover	13,222	968	14,190
Other revenue - unallocated			28
			<u>14,218</u>
Segment results and profit from operations			3,104
Finance costs			(48)
Profit from ordinary activities before taxation			3,056
Taxation			—
Profit from ordinary activities after taxation			<u>3,056</u>
Depreciation and amortisation	942	—	942

All 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.

(b) *Geographical segments*

The Group's operations are located in Hong Kong. In presenting information on the basis of geographical segments, segment revenue is based on the geographical location of its customers who are principally located in the Americas, Asia, Europe, Africa and the Middle East. Segment information relating to these geographical markets is presented below:

	Turnover	
	Six months ended 30 June	
	2004	2003
	<i>HK\$'000</i>	<i>HK\$'000</i>
The Americas	934	2,230
Asia	3,153	7,446
Europe, Africa and the Middle East	7,807	4,514
	<u>11,894</u>	<u>14,190</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.

7 Fixed Assets

	Leasehold improvements HK\$'000	Computer and office equipment HK\$'000	Furniture and fixtures HK\$'000	Moulds HK\$'000	Total HK\$'000
<i>Cost:</i>					
At 1 January 2004	98	1,958	337	790	3,183
Additions	358	530	51	68	1,007
Disposals	(98)	(295)	(155)	—	(548)
At 30 June 2004	<u>358</u>	<u>2,193</u>	<u>233</u>	<u>858</u>	<u>3,642</u>
<i>Accumulated depreciation:</i>					
At 1 January 2004	74	1,633	208	436	2,351
Charge for the period	86	121	22	77	306
Written back on disposals	(76)	(288)	(153)	—	(517)
At 30 June 2004	<u>84</u>	<u>1,466</u>	<u>77</u>	<u>513</u>	<u>2,140</u>
<i>Net book value:</i>					
At 30 June 2004	<u>274</u>	<u>727</u>	<u>156</u>	<u>345</u>	<u>1,502</u>
At 31 December 2003	<u>24</u>	<u>325</u>	<u>129</u>	<u>354</u>	<u>832</u>

8 Development Costs

	2004 HK\$'000	2003 HK\$'000
<i>Cost:</i>		
At beginning of the period / year	11,762	8,128
Additions through internal development during the period / year	<u>2,038</u>	<u>3,634</u>
At the end of the period / year	<u>13,800</u>	<u>11,762</u>
<i>Accumulated amortisation:</i>		
At beginning of the period / year	2,664	1,166
Charge for the period / year	<u>971</u>	<u>1,498</u>
At the end of the period / year	<u>3,635</u>	<u>2,664</u>
<i>Net book value:</i>		
At the end of the period / year	<u>10,165</u>	<u>9,098</u>

9 Accounts Receivable

Customers are generally granted credit terms of 30 to 60 days. An ageing analysis of accounts receivable (net of provisions for bad and doubtful debtors) is as follows:

	30 June 2004 HK\$'000	31 December 2003 HK\$'000
Current	883	7,308
Aged over 1 month but less than 2 months	510	1,293
Aged over 2 months but less than 3 months	44	1,377
Aged over 3 months	4,960	2,093
	<u>6,397</u>	<u>12,071</u>

10 Accounts Payable

An ageing analysis of accounts payable is as follows:

	30 June 2004 HK\$'000	31 December 2003 HK\$'000
Current	2,358	3,903
Aged over 1 month but less than 2 months	140	1,381
Aged over 2 months but less than 3 months	110	152
Aged over 3 months	674	229
	<u>3,282</u>	<u>5,665</u>

11 Share Capital

	<i>Note</i>	Number of shares	Amount HK\$'000
Authorised:			
At 31 December 2003 and			
30 June 2004, ordinary shares			
of HK\$0.10 each		1,000,000,000	100,000
Issued and fully paid:			
At 1 January 2004			
Shares issued upon conversion		280,000,000	28,000
of share options	(i)	1,800,255	180
At 30 June 2004		<u>281,800,255</u>	<u>28,180</u>

Note:

- (i) On 17 May 2004, the Company issued a total of 1,800,255 ordinary shares of HK\$0.10 each as a result of the exercise of share options issued on 27 October 2003 to subscribe for shares at HK\$0.09 per share.

	Share premium HK\$'000	Merger reserves HK\$'000	Revenue reserves HK\$'000	Total HK\$'000
At 1 January 2003	15,863	4,496	(24,612)	(4,253)
Profit for the period	—	—	3,056	3,056
At 30 June 2003	<u>15,863</u>	<u>4,496</u>	<u>(21,556)</u>	<u>(1,197)</u>
At 1 January 2004	24,351	4,496	(12,859)	15,988
Shares issued upon exercise of the share options	(18)	—	—	(18)
Loss for the period	—	—	(2,982)	(2,982)
At 30 June 2004	<u>24,333</u>	<u>4,496</u>	<u>(15,841)</u>	<u>12,988</u>

Merger reserves of the Group represent reserves of the subsidiary that have been capitalised as a result of a share-for-share exchange.

The Group had a net reserves of HK\$12,988,000 at 30 June 2004 (2003: deficit of HK\$1,197,000) analysed as follows:

	Six months ended 30 June	
	2004	2003
	HK\$'000	HK\$'000
Company	23,037	15,717
Subsidiaries	(14,545)	(21,410)
Merger reserves	<u>4,496</u>	<u>4,496</u>
Group	<u>12,988</u>	<u>(1,197)</u>

13 Operating Lease Commitments

At 30 June 2004, the total future minimum lease payments under non-cancellable operating leases for property rental were payable as follows:

	30 June 2004 HK\$'000	31 December 2003 HK\$'000
Within 1 year	1,133	1,124
After 1 year but within 5 years	<u>609</u>	<u>1,156</u>
	<u>1,742</u>	<u>2,280</u>

The Group leases a number of properties under operating leases. The leases typically run for an initial period of one to two years, with an option to renew the lease upon expiry when all terms are renegotiated. None of these leases include contingent rentals.

The following represents a summary of material and significant related party transactions during the period between the Group and related parties identified by the directors:

	<i>Note</i>	Six months ended 30 June	
		2004	2003
		HK\$'000	HK\$'000
Consultancy fees payable	(i)	90	294
Rentals payable	(ii)	—	48
Salaries payable to a related party	(iii)	300	240
		=====	=====
Sale of smart card products	(iv)	—	327
		=====	=====

Notes:

- (i) The subsidiary has entered into agreements with Mr. Tan Keng Boon and Mr. Tong Kam Hung for the provision of consultancy services. The terms of the consultancy fees are determined based on services provided with reference to market rates.

Mr. Tan Keng Boon (who was a full time consultant of the subsidiary for the period from October 1999 to April 2003) and Mr. Tong Kam Hung (who has been a part-time consultant of the subsidiary since April 1998) were interested in the agreements as shareholders of the Company.

- (ii) On 1 January 2002, the subsidiary of the Company renewed a rental agreement with United Animal Exchange Limited ("UAEL"), whereby the subsidiary paid a monthly rental of \$24,000 to UAEL which approximated the market rate for a term of one year commencing from 1 January 2002 which was extended for a further two months for the period from 1 January 2003 to 28 February 2003 on the same terms.

Mr. Wong Yiu Chu, Denny was interested in the agreement as a director of the Company and a director and shareholder of UAEL.

- (iii) The subsidiary paid salaries to Ms. Tsui Kam Ling, for her role as vice president, operations of the subsidiary. Ms. Tsui Kam Ling is a shareholder of the ultimate holding company and the spouse of Mr. Wong Yiu Chu, Denny, a director of the Company.

- (iv) The subsidiary sold smart card products to external customers during last period where T & C Technologies (Pte) Limited acted as a sales agent on behalf of the subsidiary.

Mr. Tan Keng Boon was interested in these transactions as a major shareholder of T & C Technologies (Pte) Limited and a full time consultant of the subsidiary during the period from October 1999 to April 2003. Mr. Tan Keng Boon ceased to be a consultant of the subsidiary in May 2003 and was appointed as a chief technical officer of the Group in May 2003. Mr. Tan Keng Boon ceased to be a shareholder of T & C Technologies (Pte) Limited in May 2003.

The terms of the above transactions are mutually agreed between the respective related parties and the subsidiary.

The directors of the Company are of the opinion that the above transactions with related parties were conducted on normal commercial terms and in the ordinary course of business.

DIRECTORS' AND CHIEF EXECUTIVE'S INTERESTS AND SHORT POSITIONS IN SHARES, UNDERLYING SHARES AND DEBENTURES

At 30 June 2004, the interests and short positions of the directors and chief executive of the Company in the shares, underlying shares and debentures of the Company or any of its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance (the "SFO")), which were 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 they are taken or deemed to have under such provisions of the SFO), or which were required, pursuant to Section 352 of the SFO, to be entered in the register referred to therein, or which were required to be notified to the Company and the Stock Exchange pursuant to the required standard of dealings by directors as referred to in Rule 5.46 of the Rules Governing the Listing of Securities on GEM of the Stock Exchange (the "GEM Listing Rules") were as follows:

(i) *Interests in issued shares*

Name of director	Ordinary shares of HK\$0.10 each				Total number of shares held	Percentage of the Company's issued share capital as at 30 June 2004
	Personal interests (Note 1)	Family interests	Corporate interests	Other interests		
Mr. Wong Yiu Chu, Denny (Note 2)	6,773,831	2,882,481	105,706,210	—	115,362,522	40.94%
Mr. Pang Wang Kee, Lawrence (Note 3)	6,863,052	—	—	—	6,863,052	2.44%
Mr. Tan Keng Boon	6,845,893	—	—	—	6,845,893	2.43%
Mr. Wan Wah Tong, Thomas (Note 4)	2,402,068	—	17,615,162	—	20,017,230	7.10%

Notes:

- The shares are registered under the names of the directors who are the beneficial owners.
- Of these shares, 105,706,210 shares are held by D&A Holdings Limited (a company which is owned as to 70% by Mr. Denny Wong and as to 30% by his wife, Ms. Tsui Kam Ling, Alice) and 2,882,481 shares are held by Ms. Tsui Kam Ling, Alice personally. Mr. Denny Wong is taken to be interested in these shares under the SFO.
- The interest disclosed herein does not include the 1,601,378 shares subject to the options granted to him pursuant to the Pre-IPO Share Option Plan.
- Of these shares, 17,615,162 shares are held by Thomrose Holdings (BVI) Limited (a company which is wholly-owned by Mr. Thomas Wan). Mr. Thomas Wan is taken to be interested in these shares under the SFO.

(ii) *Interests in underlying shares*

The directors and chief executive of the Company have been granted options under the share option schemes, details of which are set out in the section "Share option schemes" below.

SHARE OPTION SCHEMES

(i) Pre-IPO Share Option Plan

At 30 June 2004, the directors, consultants and employees of the Company had the following interests in options to subscribe for shares of the Company (market value per share at 30 June 2004 was HK\$0.18) with an exercise price of HK\$0.09 or HK\$0.24 per share under the Pre-IPO Share Option Plan (the "Plan") of the Company. The options are unlisted. Each option gives the holder the right to subscribe for one ordinary share of HK\$0.10 each of the Company.

Grantees	Date granted	Balance as at 1 January 2004	Number of share options			Balance as at 30 June 2004	Period during which the options are exercisable	Exercise price per share	Percentage of the Company's issued share capital as at 30 June 2004
			Granted during the period	Exercised during the period	Lapsed during the period				
1 director	27 October 2003	1,601,378	–	–	–	1,601,378 (Note 1)	10 November 2004 to 2 December 2011	HK\$0.24	0.57%
2 consultants	27 October 2003	1,361,172	–	–	–	1,361,172	10 May 2004 to 24 July 2010	HK\$0.09	0.48%
13 employees	27 October 2003	1,441,241	–	1,280,668 (Note 2)	–	160,573	10 May 2004 to 24 July 2010	HK\$0.09	0.06%
	27 October 2003	520,449	–	519,587 (Note 2)	–	862	10 May 2004 to 27 December 2010	HK\$0.09	0.01%
	27 October 2003	1,411,218	–	–	–	1,411,218 (Note 3)	10 May 2004 to 20 January 2013	HK\$0.24	0.50%
	27 October 2003	200,173	–	–	200,173 (Note 4)	–	31 December 2004 to 20 January 2013	HK\$0.24	–
		<u>6,535,631</u>	<u>–</u>	<u>1,800,255</u>	<u>200,173</u>	<u>4,535,203</u>			

Notes:

- 1 The 1,601,378 share options were granted to a director, Mr. Pang Wang Kee, Lawrence. All other options were granted to employees and consultants of the Group.
- 2 1,800,255 share options at an exercise price of HK\$0.09 each have been exercised by 3 employees during the period ended 30 June 2004. The closing price of the shares immediately before the date on which the options were exercised was HK\$0.243.
- 3 The options will vest and be exercisable in three tranches as follows:
 - (a) one-third of the options have vested and be exercisable on 10 May 2004;
 - (b) a further one-third of the options will vest and be exercisable on 31 December 2004; and
 - (c) the remaining one-third of the options will vest and be exercisable on 31 December 2005.
- 4 The options lapsed upon the resignation of the participant from the Group.

(ii) *Share Option Scheme*

Pursuant to the resolution of the shareholders of the Company dated 27 October 2003, the Company adopted a Share Option Scheme (the "Scheme"). As at the date of this report, no options had been granted under the Scheme.

Save as disclosed above, to the best knowledge of the directors of the Company, as at 30 June 2004, none of the directors or their associates had any personal, family, corporate or other interest or short positions in any shares, underlying shares or debentures of the Company or any of its associated corporations (within the meaning of Part XV of the SFO) which would have 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 they are taken or deemed to have under such provisions of the SFO), or which were required, pursuant to Section 352 of the SFO, to be entered in the register referred to therein, or which were required, pursuant to the required standard of dealings by directors as referred to in Rule 5.46 of the GEM Listing Rules, to be notified to the Company and the Stock Exchange.

DIRECTORS' RIGHTS TO ACQUIRE SHARES

Save as disclosed under the paragraphs headed "Directors' and chief executive's interests and short positions in shares, underlying shares and debentures" and "Share option schemes" above, at no time during the period were rights to acquire benefits by means of the acquisition of shares in or debentures of the Company granted to any directors or their respective spouse or children under 18 years of age, or were any such rights exercised by them, or was the Company, its holding company, or any of its subsidiaries and fellow subsidiaries a party to any arrangement to enable the directors to acquire such rights in any other body corporate.

SUBSTANTIAL SHAREHOLDERS' AND OTHER PERSONS' INTERESTS AND SHORT POSITIONS IN SHARES AND UNDERLYING SHARES

In addition to the interests disclosed under the section "Directors' and chief executive's interests and short positions in shares, underlying shares and debentures" above, the Company has been notified of the following interests in the Company's issued shares at 30 June 2004 which as recorded in the register of interests required to be kept by the Company pursuant to Section 336 of the SFO:

	Capacity	Total number of ordinary shares held	Percentage of the Company's issued share capital as at 30 June 2004
D & A Holdings Limited	Beneficial owner	105,706,210 shares (L)	37.51%
Ms. Tsui Kam Ling, Alice (<i>Note 2</i>)	Personal	2,882,481 shares (L)	40.94%
	Family	112,480,041 shares (L)	
Proway Investment Limited (<i>Note 3</i>)	Beneficial owner	31,740,305 shares (L)	11.26%
Morningside CyberVentures Holdings Limited (<i>Note 3</i>)	Other	31,740,305 shares (L)	11.26%
Verrall Limited (<i>Note 3</i>)	Other	31,740,305 shares (L)	11.26%
Madam Chan Tan Ching Fen (<i>Note 3</i>)	Other	31,740,305 shares (L)	11.26%
Thomrose Holdings (BVI) Limited	Beneficial owner	17,615,162 shares (L)	6.25%

Notes:

- 1 The letter "L" stands for the shareholders' long position (within the meaning stated in the form for notification specified pursuant to the SFO) in shares.
- 2 105,706,210 shares are held by D&A Holdings Limited, 2,882,481 shares are held by Ms. Tsui Kam Ling, Alice personally and 6,773,831 shares are held by her husband, Mr. Denny Wong personally. Ms. Tsui Kam Ling, Alice is taken to be interested in the shares held by Mr. Denny Wong and D&A Holdings Limited under the SFO.
- 3 Proway Investment Limited is wholly owned by Morningside CyberVentures Holdings Limited. Morningside CyberVentures Holdings Limited is wholly owned by Verrall Limited in its capacity as trustee of a family trust established by Madam Chan Tan Ching Fen. Madam Chan Tan Ching Fen is taken to be interested in the shares disclosed herein in her capacity as founder of the trust (as that term is defined in the SFO).

Save as disclosed above, as at 30 June 2004 and to the best knowledge of the directors, there was no person (other than the directors and chief executive of the Company) whose interests are set out in the paragraph "Directors' and chief executive's interests and short positions in shares, underlying shares and debentures" above, had an interest or short position in the shares or underlying shares of the Company as recorded in the register to be kept under Section 336 of the SFO.

DIRECTORS' INTERESTS IN COMPETING BUSINESS

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.

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

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

SPONSOR'S INTERESTS

Neither the Company's sponsor, Anglo Chinese Corporate Finance, Limited (the "Sponsor"), nor its directors, employees or associates had any interests in any class of securities of the Company or any other company in the Group (including options or the right to subscribe for such securities) as at 30 June 2004 pursuant to Rule 6.35 of the GEM Listing Rules.

Pursuant to the sponsor agreement dated 30 October 2003 entered into between the Company and the Sponsor, the Sponsor receives a fee for acting as the Company's retained sponsor for the period from 10 November 2003 to 31 December 2005.

COMPLIANCE WITH THE BOARD PRACTICES AND PROCEDURES

The Company has complied with the Board Practices and Procedures requirements as set out in Rules 5.34 to 5.45 of the GEM Listing Rules throughout the period.

AUDIT COMMITTEE

The Company has established an audit committee with written terms of reference. The audit committee comprises two Independent Non-executive Directors namely, Dr. Yip Chak Lam, Peter (being the chairman of the audit committee) and Mr. Cheong Chung Chin and one Executive Director, Mr. Wong Yiu Chu, Denny 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 has reviewed the Group's unaudited results for the six months ended 30 June 2004.

By order of the Board
WONG Yiu Chu, Denny
Chairman

Hong Kong, 2 August 2004