



MILKYWAY IMAGE

Milkyway Image Holdings Limited

銀河映像控股有限公司

(incorporated in the Cayman Islands with limited liability)

Interim Report 2002

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This report, for which the directors of Milkyway Image Holdings Limited collectively and individually accept full responsibility, includes particulars given in compliance with the Rules Governing the Listing of Securities on the Growth Enterprise Market of The Stock Exchange of Hong Kong Limited for the purpose of giving information with regard to Milkyway Image Holdings Limited. The directors, having made all reasonable enquiries, confirm that, to the best of their knowledge and belief: 1. The information contained in this report is accurate and complete in all material respects and not misleading; 2. There are no other matters the omission of which would make any statement in this report misleading; and 3. All opinions expressed in this report have been arrived at after due and careful consideration and are founded on bases and assumptions that are fair and reasonable.

CONTENTS

	<i>Pages</i>
Highlights	3
Business Review and Prospect	4
Management's Discussion & Analysis	6
Unaudited Interim Results	13
Other Information	27

HIGHLIGHTS

1. The turnover of the Group during the six months ended 30 September, 2002 was approximately HK\$18.6 million representing a decrease of approximately 64% as compared with the corresponding period in 2001.
2. The net profit of the Group for the six months ended 30 September, 2002 was approximately HK\$1.07 million representing a decrease of approximately 85% as compared with the corresponding period in 2001.
3. Earnings per share of the Group was approximately HK cent 0.22 for the six months ended 30 September, 2002 (2001: HK cents 1.46).
4. The Board does not recommend the payment of any dividend for the six months ended 30 September, 2002 (2001:HK\$ Nil).

BUSINESS REVIEW AND PROSPECT

Business Review

For the six months ended 30 September, 2002, Milkyway Image Holdings Limited (the "Company") and its subsidiaries (together the "Group") recorded a turnover of HK\$18,575,000, representing a drop of approximately 64% over the corresponding period in 2001.

The decrease in turnover during the interim period mainly due to the economic downturn in the industry. As a result, the Group could only engage in one film production project whereas it did 4 projects in the corresponding period in 2001.

In addition, net profit attributable to shareholders for the six months ended 30 September, 2002 was approximately HK\$1.07 million, representing a decrease of approximately 85% over the same period in 2001. The significant decrease was partly due to the drop in turnover and partly due to an increase in administration expenses. Compared with the same period in 2001, administration expenses increased by HK\$3.5 million, i.e., increased to HK\$5.2 million from HK\$1.7 million. Salaries expenses of HK\$3.1 million (six months ended 30 September, 2001: HK\$0.6 million), rent, rates and management fees of HK\$0.89 million (six months ended 30 September, 2001: HK\$116,000) and depreciation of property, plant and equipment of HK\$204,000 (six months ended 30 September, 2001: HK\$94,000) were major components of administration expenses and they contributed to the increase in administration expenses for the six months ended 30 September, 2002. The increase in salaries expenses was due to increase in salaries of employees and the reallocation of a film director's fee in respect of a Director from production costs to salaries expenses of administration expenses. The increase in rent and rates was attributable to the increase in the office space required by the growing number of staff, in-house editing and sound mixing studio and the production crew.

Prospects

In spite of the film production business still being hindered by the overall economic recession in the foreseeable future, the directors of the Company (the "Directors") believe that the overall performance of the Group can rebound to record a growth in the near future. The Group has entered into a co-investment agreement for film production; the Group has contributed HK\$2 million, being 50% of the total investment cost of HK\$4 million and will then own 50% of the film rights and share 50% of the profit from all kinds of income arising from the film. It is expected that the Group will complete the film before 31 December, 2003. The Group intends to take advantage of the partial copyright ownership to generate recurring licensing income so as to broaden the revenue base.

In addition, the Group is diversifying its business by engaging in the provision of TV movie production services. During the interim period, the Group has completed the production of one TV movie which contributed HK\$5.5 million to the turnover of the Group in the interim period. The Directors believe that the demand of TV movies in the PRC market is increasing and it is a good stepping stone for the Group to penetrate its business into the PRC market. The Directors consider that resources, equipment and production skillset for film production are transferable to the production of TV movies. As such, the Group is not required to make any additional investment for this new business segment. No net proceeds from the Share Offer has been applied for the development of TV movie production. During the six months ended 30 September, 2002, the Group has signed a master production agreement with a TV movie company for the development and production of 10 TV movies.

Regarding the film projects signed with One Hundred Years of Films Company Limited, Golden Harvest Film Productions Limited and Teamwork Motion Pictures Limited as disclosed in the prospectus dated 13 August, 2002 issued by the Company (the "Prospectus"), the Group has already signed a supplementary agreement for one film on 15 October, 2002 and has been in advanced discussion about another supplementary agreement for another film with One Hundred Years of Films Company Limited. One film is scheduled to be screened in the coming Lunar New Year.

In addition, the Group has entered another co-investment agreement for film production on 2 October, 2002; similarly, the Group has contributed HK\$2 million, being 50% of the total investment cost of HK\$4 million, and will own 50% of the film right and share 50% of the profit from all kinds of income from the film. Such film will be completed by 31 December, 2003.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Segment information

During the six months ended 30 September, 2002, the Group has started to generate revenue from the production of TV movies. All of the Group's revenue for the six months ended 30 September, 2002 was derived in Hong Kong.

For the six months ended 30 September, 2002, the gross profit margin of the film production segment was 18%, being higher than 15% for the same period in 2001. Such increase was due to the reallocation of a film director's fee in respect of a Director from production costs to salaries expenses of administration expenses. It is now the Group's accounting policy to treat the film director's fee of the Director as salaries expenses.

Liquidity, financial resources and Treasury Policy

The Group has been in good financial position and there was no borrowings or issues of capital market instruments other than the Share Offer during the six months ended 30 September, 2002.

As at 30 June, 2002, the Group had cash and cash equivalent of approximately HK\$3 million. Following the listing of the Company's Shares on GEM of the Stock Exchange on 26 August, 2002, the Group had received net proceeds of approximately HK\$17 million. The Group had applied the proceeds in the manner as stated in the Prospectus. As at 30 September, 2002, the Group had cash and cash equivalent of approximately HK\$12 million. The Group generally financed its operations and investing activities with internally generally cash flows and balance of proceeds from the Share Offer. Given the continuous inflow of advanced receipts and profits generated from the film companies and TV movie companies based on the master agreements and the supplementary agreements concluded, the Group did not anticipate any liquidity problem as at the report date.

The Group adopts a conservative treasury policy in cash and financial management . The Group does not have any committed borrowing facilities except for certain finance lease payables. Surplus funding not immediately applied is maintained with banks in Hong Kong. All the Group's sales transaction for the six months ended 30 September, 2002 was denominated in Hong Kong Dollars. All bank deposits are also made in Hong Kong Dollars, thus the Group does not expose to any foreign exchange risks.

Sales and Marketing

The Directors believe that participation in film festivals is still one of the most effective ways to promote and market the films produced by the Group, particularly those by invitation participations that incur minimal expenses. During the six months ended 30 September, 2002, awards attained to the films produced by the Group are as follows:

Name of Films	Film Festivals	Awards
<i>My Left Eye Sees Ghosts</i> (我左眼見到鬼)	2002 Taipei Golden Horse Award	Best Actress Nomination – Sammi Cheng
<i>Fat Choi Spirit</i> (嚟咕嚟咕新年財)	2002 Udineincontri Cinema Far East Film	Official Selection
<i>Running Out of Time 2</i> (暗戰2)	2002 Seattle International Film Festival	Official Selection – U.S. Premier
	2002 Philadelphia Festival of World Cinema	“Danger After Dark” Official Selection – International Premier
	2002 Taipei Golden Horse Award	Best Visual Effects Nomination Best Cinematography Nomination Best Action Choreography Nomination Best Sound Nomination Best Editing

Name of Films	Film Festivals	Awards
<i>Fulltime Killer (全職殺手)</i>	2002 New York Asian International Film Festival 2002 San Francisco Film Festival	Official Selection (HK Kickoff Night) Official Selection
<i>Love on a diet (瘦身男女)</i>	2002 Udineincontri Cinema Far East Film	Official Selection
<i>The Mission (鎗火)</i>	2002 Croatia Motovun Film Festival 2002 Barcelona Asian Film Festival	Official Selection Official Selection

Establishment of studios

During the interim period, the Group has started to establish its own sound and editing studios with manner as disclosed in the Prospectus. The Directors expect that the studios can be put into operation within the third quarter period for the financial year ended 31 March, 2003.

Material acquisition, disposal and significant investments

The Group made investment in editing and sound mixing equipment as disclosed in the section headed "Use of proceeds" under the section headed "Statement of business objectives". Besides, the Group has entered into a co-investment agreement for film production.

Other than those mentioned, the Group had not made any acquisition or disposal of subsidiaries or affiliated companies, investments or divestments during the six months ended 30 September, 2002. During the same period in 2001, the Group had not made any material acquisition, disposal, investment or divestment. At present, the Group has no future plan for material investments and acquisition of capital assets other than those disclosed under the section on statement of business objectives in the Prospectus.

Employee information

As at 30 September, 2002, the Group had 14 employees (31 March, 2002: 14 employees) and all of them are working in Hong Kong. For the six months ended 30 September, 2002, staff costs including Directors' remuneration was approximately HK\$3.1 million (six months ended 30 September, 2001: HK\$0.6 million). The increase in staff cost was mainly due to increase in salaries of staff and the reallocation of a film director's fee in respect of a Director from production costs to salaries expenses of administration expenses.

The salary and benefit levels of the Group's employees are kept at a competitive level and employees are rewarded on a performance related basis. The Group also adopts an employee share option scheme whereby the employees of the Group may be granted share options to subscribe for shares in the Group. As at 30 September 2002, no such option has yet been granted.

Charges on Group assets

As at 30 September, 2002, the Group did not pledged any of its assets to banks and financial institutions to secure any general credit facilities (31 March, 2002: Nil).

Gearing ratio

As at 30 September, 2002, the Group's gearing ratio was zero (31 March, 2002: zero). The Group did not have any committed borrowing facilities or any borrowings other than the finance lease payables. For the purpose of calculating the gearing ratio, (i.e. total debts/total equity), only interest-bearing loans were treated as debts while shareholders' equity was treated as equity.

Contingent liabilities

The Group did not have any significant contingent liabilities as at 30 September, 2002 (31 March, 2002: Nil).

Use of proceeds from the Initial Public Offering

The Group received net proceeds of approximately HK\$17 million from the initial public offering. During the six months ended 30 September, 2002, HK\$10 million of the net proceeds had been applied and details of which were as follows:

1. as to about HK\$4.8 million for the purchase of editing and sound mixing equipment;
2. as to about HK\$2 million for the engagement of joint investment for a film project;
3. as to about HK\$2.7 million for the upfront payment to engage production personnel to enhance future expansion of film production; and
4. as to about HK\$0.5 million as general working capital of the Group.

For the six months ended 30 September, 2002, capital expenditure incurred for film production and film investment were HK\$2 million and HK\$3 million respectively less than the intended use of net proceeds as disclosed in the Prospectus. On 2 October, 2002, the Group made a film investment of HK\$2 million. The Directors intend to apply those unused net proceeds in subsequent periods as manner disclosed in the Prospectus when at such time those applications become necessary.

To the extent that the net proceeds are not immediately applied as scheduled in the Prospectus, the Group will maintain such net proceeds as short term deposits with banks in Hong Kong.

Comparison Of The Business Objective Set Out In The Prospectus With Actual Business Progress

Business objectives as stipulated in the Prospectus	Actual progress and development during the period from 1 April, 2002 to 30 September, 2002	Remarks
<i>Purchase of filming equipment and establish editing and mixing studio</i>		
<ul style="list-style-type: none"> – acquisition of hardware and software for establishing own editing and sound mixing studios to enhance the quality and efficiency of film production 	<ul style="list-style-type: none"> – implemented as planned 	
<ul style="list-style-type: none"> – employ one employee for operating the studio 	<ul style="list-style-type: none"> – no new staff employed 	<p>the industry did not perform as expected by the Group and so the position would be suspended until it becomes necessary</p>
<ul style="list-style-type: none"> – acquisition of camera and lighting equipment 	<ul style="list-style-type: none"> – not yet implemented 	

Business objectives as stipulated in the Prospectus	Actual progress and development during the period from 1 April, 2002 to 30 September, 2002	Remarks
<i>Film Production</i>		
– schedule to deliver two films	– one film was delivered	one film was under production and expected to deliver in January 2003
– schedule to enter into contracts with script writers, film directors and producers during the interim period	– engaged 2 script writers, one director and one artist	
– employ two persons responsible for assisting daily film production and administrative work	– no full-time staff has been employed	the Group changed its plan to employ part-time staff to adapt to the undermined business environment
<i>Film Investment</i>		
– make investment in one film project with other local film producers or companies	– implemented as planned	

UNAUDITED INTERIM RESULTS

The Board of Directors (the "Board") announces the unaudited condensed consolidated results of the Group for the periods of three months and six months ended 30 September, 2002 (the "Periods") together with the comparative unaudited consolidated results of the Group for the corresponding periods in 2001 as follows:

CONDENSED CONSOLIDATED INCOME STATEMENTS

	Notes	(Unaudited) For the three months ended 30 September,		(Unaudited) For the six months ended 30 September,	
		2002 HK\$'000	2001 HK\$'000	2002 HK\$'000	2001 HK\$'000
TURNOVER	2	18,200	48,908	18,575	52,107
Film production costs		(12,711)	(41,467)	(12,744)	(44,375)
Gross profit		5,489	7,441	5,831	7,732
Other income		305	1,134	422	1,309
Administrative expenses		(2,259)	(486)	(4,287)	(974)
Other operating expenses		(820)	(439)	(874)	(697)
PROFIT FROM OPERATIONS		2,715	7,650	1,075	7,370
Finance costs		(6)	(6)	–	(18)
Profit before taxation	4	2,709	7,644	1,075	7,352
Taxation	5	–	–	–	(410)
NET PROFIT ATTRIBUTABLE TO SHAREHOLDERS		2,709	7,644	1,075	6,942
Dividend	6	–	–	–	–
Earnings per share (HK cents)	7				
Basic		0.52	1.61	0.22	1.46
Diluted		0.49	–	0.21	–

CONDENSED CONSOLIDATED BALANCE SHEETS

	Notes	Unaudited Consolidated at 30 September, 2002 HK\$'000	Audited Consolidated at 31 March, 2002 HK\$'000
NON-CURRENT ASSETS			
Property, plant and equipment		7,536	813
CURRENT ASSETS			
Production in progress		8,096	5,089
Trade receivables	8	4,000	1,661
Prepayments, deposits and other receivables		11,450	10,209
Cash and bank balances		13,658	6,917
		37,204	23,876
CURRENT LIABILITIES			
Advanced receipts		17,663	19,163
Trade payables	9	1,734	1,758
Other payables		5,085	2,293
Finance lease payables		104	90
Provision for taxation		530	530
		25,116	23,834
NET CURRENT ASSETS		12,088	42
TOTAL ASSETS LESS CURRENT LIABILITIES		19,624	855
NON-CURRENT LIABILITIES			
Finance lease payables		(166)	(131)
NET ASSETS		19,458	724
CAPITAL AND RESERVES			
Issued capital	10	6,272	–
Reserves	11	13,186	724
		19,458	724

CONDENSED CONSOLIDATED CASH FLOW STATEMENTS

	Unaudited Consolidated six months ended 30 September, 2002 HK\$'000	Unaudited Consolidated six month ended 30 September, 2001 HK\$'000
Net cash outflow from operating activities	(3,975)	(15,009)
Net cash outflow from investing activities	(6,692)	(202)
Net cash inflow from financing activities	17,408	(128)
Increase/(decrease) in cash and cash Equivalents	6,741	(15,339)
Cash and cash equivalents brought forward	6,917	18,310
Cash and cash equivalents carried forward	13,658	2,971
Analysis of the balances of cash and cash equivalents		
Bank balances and cash	13,658	2,971

CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

	(Unaudited)			
	Share capital	Share premium	Retained earnings	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 1 April, 2001	–	–	(4,734)	(4,734)
Profit for the period	–	–	6,942	6,942
At 30 September, 2001	–	–	2,208	2,208
At 1 April, 2002	–	–	724	724
Capitalization issue of Shares	4,760	(4,760)	–	–
Shares issued upon				
Initial Public Offering	840	24,360	–	25,200
Shares issued expenses	–	(8,213)	–	(8,213)
Exercise of Pre-IPO Shares Options	672	–	–	672
Profit for the period	–	–	1,075	1,075
At 30 September, 2002	6,272	11,387	1,799	19,458

NOTES TO THE INTERIM FINANCIAL STATEMENTS

1. Group reorganization and basis of preparation and principal accounting policies

- (a) The Company was incorporated in the Cayman Islands as an exempted company with limited liability on 9 November, 2001 under the Companies Law of the Cayman Islands.
- (b) In order to facilitate the preparation for the listing of the Shares in GEM, the Group effected the reorganization, pursuant to which the Company became the ultimate holding company of the Group. The reorganization was completed on 2 August, 2002 and involved the following:
 - (i) As at the date of incorporation of the Company, its authorized share capital was HK\$390,000.00 divided into 3,900,000 shares of HK\$0.10 each of which one share was allotted and issued for cash at par to Codan Trust Company (Cayman) Limited as initial subscriber and was transferred to Mr. To Kei Fung, the Chairman of the Group, on 20 November, 2001 for cash at par.
 - (ii) On 26 October, 2001, Galaxy Image (BVI) Limited ("Galaxy") was incorporated with an authorized share capital of US\$50,000.00 divided into 50,000 shares of US\$1.00 each, of which 1 share was allotted and issued to Mr. To for cash at par on 21 November, 2001.
 - (iii) On 22 November, 2001, Galaxy acquired 9,500 shares and 500 shares of HK\$1.00 each in Milkyway (HK) from Mr. To and Ms. Chan Dao Ho, an executive director of the Company, respectively in consideration of the issue and allotment of 9,499 shares and 500 shares of US\$1.00 each in Galaxy, credited as fully paid, to Mr. To and Ms. Chan Dao Ho respectively.

- (iv) On 28 November, 2001, Teamwork Corporation (“Teamwork”) acquired 2,500 shares in Galaxy from Mr. To and Bestrade Technologies Limited (“Bestrade”) acquired 400 shares in Galaxy from Mr. To.
- (v) On 22 April, 2002, each issued and unissued share of HK\$0.10 in the then share capital of the Company was subdivided into 10 shares.
- (vi) On 22 April, 2002, the Company acquired 10,000 shares of US\$1.00 each, being the entire issued capital of Galaxy, in consideration for the issue, credited as fully paid, by the Company of an aggregate of 9,990 shares, as to 590 Shares to Mr. To, 6,000 Shares to Pearl Rider at the direction of Mr. To, 500 Shares to Ms. Chan Dao Ho, 2,500 Shares to Teamwork and 400 Shares to Bestrade.
- (vii) On 14 May, 2002, Teamwork transferred 1,250 Shares to each of Mr. Andy Lau Tak Wah (“Mr. Lau”) and Growth Promise Enterprises Limited (“GPEL”).
- (viii) On 11 July, 2002, GPEL transferred 1,250 Shares to Grand Sum Assets Limited.
- (ix) On 2 August, 2002, the authorized share capital of the Company was increased from HK\$390,000.00 to HK\$100,000,000.00 by the creation of an additional 9,961,000,000 Shares.
- (x) On 2 August, 2002, upon the Capitalization, 285,594,000 Shares was issued and allotted, credited as fully paid, to Pearl Rider, 28,559,400 Shares was issued and allotted, credited as fully paid, to Mr. To, 23,799,500 Shares was issued and allotted, credited as fully paid, to Ms Chan Dao Ho, 59,498,750 Shares each was issued and allotted, credited as fully paid, to Mr. Lau and GSAL, and 19,039,600 Shares was issued and allotted, credited as fully paid, to Bestrade.

- (xi) On 26 August, 2002, the Shares of the Company were listed on GEM by offering 14,588,000 new shares and placing 69,412,000 new shares to the public.
- (c) The preparation of the unaudited condensed consolidated interim financial statements was prepared in accordance with accounting policies generally accepted in Hong Kong. The interim financial statements have been reviewed by the audit committee.

The interim financial statements include the consolidated results of the Group for the six months ended 30 September, 2002 and the corresponding period in the previous year.

For information and comparative purposes, the unaudited pro forma consolidated results of the Company's subsidiaries are prepared on a consolidated basis as if the current Group structure had been in existence.

The unaudited condensed consolidated interim financial statements have been prepared in accordance with Statement of Standard Accounting Practice ("SSAP") 25 "Interim Financial Reporting" issued by the Hong Kong Society of Accountants and with the disclosure requirements set out in the Chapter 18 of the Rules Governing the Listing of Securities on GEM of the Stock Exchange (the "GEM Listing Rules").

- (d) The accounting policies and basis of preparations used in the preparation of the unaudited condensed consolidated interim financial statements are consistent with those used for the Prospectus which were set out in the Accountants' Report in the Prospectus.
- (e) The Group reorganization as more fully described in the Prospectus is accounted for under merger accounting in accordance with the SSAP No. 27 "Accounting for Group Reconstruction" issued by the Hong Kong Society of Accountants.

2. Turnover

Turnover represents revenue generated from film production and TV movie production income.

3. Segment Information

(a) Business Segment

The principal activity of the Group is the provision of film and TV movie production services for the six months ended 30 September, 2002. The unaudited business segment information for the six months ended 30 September, 2002 and the corresponding period in 2001 is as follows:

	Film Production		TV Movie Production		Total	
	Six months ended 30 September,		Six months ended 30 September,		Six months ended 30 September,	
	2002 HK\$'000	2001 HK\$'000	2002 HK\$'000	2001 HK\$'000	2002 HK\$'000	2001 HK\$'000
Turnover	13,075	52,107	5,500	–	18,575	52,107
Production costs	(10,744)	(44,375)	(2,000)	–	(12,744)	(44,375)
Gross profits	2,331	7,732	3,500	–	5,831	7,732
Other income					422	1,309
Unallocated expenses					(5,178)	(1,689)
Profit from operations					1,075	7,352
Finance costs					–	–
Profit before taxation					1,075	7,352
Taxation					–	(410)
Net profit attributable to shareholders					1,075	6,942

(b) Geographical Segment

Since all the revenue and income generated by the Group is derived from Hong Kong, no geographical segment information is presented.

4. Profit before taxation

	From 1 July, 2002 to 30 September, 2002 HK\$'000	From 1 July, 2001 to 30 September, 2001 HK\$'000	From 1 April, 2002 to 30 September, 2002 HK\$'000	From 1 April, 2001 to 30 September, 2001 HK\$'000
This is stated after charging:				
Directors' remuneration	1,041	–	2,082	–
Depreciation on property, plant and equipment	144	47	204	93
Loss on disposal of property, plant and equipment	–	14	66	14
Operating lease payments in respect of premises	349	62	408	81
Staff costs	514	271	1,022	582

5. Taxation

No provision for Hong Kong Profits Tax has been made as the Group had no estimated assessable profits for the three months and six months ended 30 September, 2002 (Three months and six months ended 30 September, 2001: Nil and HK\$410,000, respectively). The provisions for Hong Kong Profits Tax of HK\$530,000 as at 30 September, 2002 and HK\$410,000 as at 30 September, 2001 have been made at the rate of 16% on the Group's estimated net assessable profit.

Deferred taxation assets is not recognized as it is uncertain whether the tax benefit will be realized in the foreseeable future. The deferred taxation liability is not provided for in the interim financial statements as the amount involved is insignificant.

6. Dividend

The Board does not recommend the payment of an interim dividend for the three months and six months ended 30 September, 2002 (2001: Nil).

7. Earnings per share

The calculation of basic earnings per share for the three months and six months ended 30 September, 2002 is based on the respective unaudited net profit from ordinary activities attributable to shareholders of approximately HK\$2,709,000 and HK\$1,075,000 (Three months and six months ended 30 September, 2001: profit of HK\$7,644,000 and HK\$6,942,000, respectively) and on weighted average number of Shares of 523,478,261 and 499,868,852 for the three months and six months ended 30 September, 2002, respectively, taking into account that 476,000,000, 560,000,000 and 627,200,000 (Three months and six months ended 30 September, 2001: 476,000,000) ordinary shares were in issue during the periods.

The calculation of diluted earnings per share for the three months and six months ended 30 September, 2002 is based on the respective unaudited net profit from ordinary activities attributable to shareholders of approximately HK\$2,709,000 and HK\$1,075,000 (Three months and six months ended 30 September, 2001: profit of HK\$7,644,000 and HK\$6,942,000, respectively), and on weighted average number of Shares of 549,043,478 and 512,721,311 for the three months and six months ended 30 September, 2002 respectively, taking into account that 476,000,000 and 644,000,000 (no diluted earnings per share for the three months and six months ended 30 September, 2001) were in issue pursuant to the fully exercise of the options granted under the Pre-IPO Share Options Scheme.

8. Trade receivables

Credit terms granted by the Group to its customers normally ranges from 7 days to 30 days. The aging analysis of the Group's trade receivables as at 30 September, 2002 and 31 March, 2002 are as follows:

	Unaudited 30 September, 2002 HK\$'000	Audited 31 March, 2002 HK\$'000
Within one month	–	–
After one month but within three months	4,000	–
After three months but within six months	–	1,661
	4,000	1,661

Trade receivables were usually settled within a period of six months.

9. Trade payables

The following is an aging analysis of trade payables as at 30 September and 31 March, 2002:

	Unaudited 30 September, 2002 HK\$'000	Audited 31 March, 2002 HK\$'000
Within six months	1,392	1,012
From seven to twelve months	342	40
Over one year	–	706
	1,734	1,758

10. Share Capital

HK\$'000

Authorised share capital:

10,000,000,000 shares of HK\$0.01 each 100,000

Ordinary shares of HK\$0.01 each

Issued and fully paid:

	Number of shares	HK\$
As at 1 April, 2002	1	0.10
Subdivided issued share into 10 shares	9	–
As at 22 April, 2002 (Note 1)	10	0.10
Issue of Shares in exchange for shares in Galaxy	9,990	99.90
Capitalization issue of shares	475,990,000	4,759,900.00
Issue of Shares pursuant to public offer and placing	84,000,000	840,000.00
Issue of Shares pursuant to the exercise of Pre-IPO Shares Options	67,200,000	672,000.00
As at 30 September, 2002	627,200,000	6,272,000.00

Note 1: Pursuant to a written resolution of the sole shareholder of the Company passed on 22 April, 2002, each issued and unissued share of HK\$0.1 in the then share capital of the Company was subdivided into 10 shares.

11. Reserves

	(Unaudited)		
	Share	Accumulated	
	premium	(loss) profits	Total
	HK\$'000	HK\$'000	HK\$'000
As at 1 April, 2001			
Accumulated losses	–	(4,734)	(4,734)
Net profit for the year	–	6,942	6,942
As at 30 September, 2001	–	2,208	2,208
As at 1 April, 2002	–	724	724
Capitalization issue of Shares	(4,760)	–	(4,760)
Shares issued upon Initial Public Offering	24,360	–	24,360
Shares issued expenses	(8,213)	–	(8,213)
Profit for the period	–	1,075	1,075
As at 30 September, 2002	11,387	1,799	13,186

12. Commitments

At 30 September and 31 March, 2002, the lease commitments of the Group for future minimum lease payments under non-cancellable operating lease in respect of land and buildings falling due as follows:

	Unaudited At 30 September, 2002 HK\$'000	Audited At 31 March, 2002 HK\$'000
Within one year	1,864	40
After one year but within five years	3,300	7
	5,164	47

OTHER INFORMATION

1. DIRECTORS' AND CHIEF EXECUTIVE'S INTERESTS IN EQUITY

As at 30 September, 2002, the interests of directors and their associates in the equity of the Company and any associated corporations as recorded in the register which will have to be notified to the Company and the Stock Exchange pursuant to section 29 of the SDI Ordinance are as follows:

Ordinary shares of HK\$0.010 each of the Company

Name of Director	Personal Interest	Other Interest	Total
Mr. To Kei Fung	–	285,600,000	285,600,000
		(Note)	

Note: The shares is held by Pearl Rider Overseas Limited which is wholly owned by Sliver Seal Finance Limited as trustee for and on behalf of The To Kei Fung Family Unit Trust, all units of which are beneficially owned as to 99.99% by The To Kei Fung Family Trust and 0.01% by Ms. Wong Po Ling, Pauline, the spouse of Mr. To. Mr. To is the sole discretionary object of The To Kei Fung Family Trust for the 12 months period from the listing of the Shares on GEM.

2. SHARE OPTIONS SCHEMES

A. Pre-IPO Share Option Scheme

Pursuant to a written resolutions of the Company passed on 2 August, 2002, the Company conditionally adopted a Pre-IPO Share Option Scheme, the principal terms of which are set out in the section headed "Pre-IPO Share Option Schemes" in Appendix IV to the Prospectus.

As at the Listing Date, options to subscribe for an aggregate of 84,000,000 Shares of the Company were granted to a senior management and six

independent contractors. As at 30 September, 2002, movement of the options granted as from the Listing date is as follow:

Name of grantees	Number of option granted	Date of grant	Exercise period	Exercise price HK\$	Outstanding
					number of shares as at 30 September 2002
<i>Senior management</i>					
Ding Yui-Shan	16,800,000	02/08/2002	26/08/2002 to 25/08/2007	0.01	16,800,000
<i>Independent contractors</i>					
Yau Nai Hoi	22,400,000	02/08/2002	26/08/2002 to 25/08/2007	0.01	–
Law Wing Cheong	11,200,000	02/08/2002	26/08/2002 to 25/08/2007	0.01	–
Sie Oi Ling	11,200,000	02/08/2002	26/08/2002 to 25/08/2007	0.01	–
Cheng Siu Keung	8,400,000	02/08/2002	26/08/2002 to 25/08/2007	0.01	–
Wu Kwok Chiu	8,400,000	02/08/2002	26/08/2002 to 25/08/2007	0.01	–
Kwong Ting Fong	5,600,000	02/08/2002	26/08/2002 to 25/08/2007	0.01	–
	84,000,000				16,800,000

All the options granted under Pre-IPO Option Scheme may be exercised within 5 years from the listing date. During the period to 30 September, 2002, 67,200,000 options out of 84,000,000 options granted were exercised. The relevant number of options, dates of exercise and the weighted average closing prices for the period from the listing date to the dates immediately before the dates of exercise are as follows:

Name of option holders	Number of options exercised	Date of exercise	Weighted average closing price HK\$
Yau Nai Hoi	22,400,000	28/08/2002	0.2725
Law Wing Cheong	11,200,000	10/09/2002	0.2305
Sie Oi Ling	11,200,000	16/09/2002	0.2247
Cheng Siu Keung	8,400,000	16/09/2002	0.2247
Wu Kwok Chiu	8,400,000	16/09/2002	0.2247
Kwong Ting Fong	5,600,000	16/09/2002	0.2221
	67,200,000		

As at 30 September, 2002, the number of outstanding options was 16,800,000 that are owned by Mr. Ding Yuin-Shan. Mr. Ding Yuin-Shan has undertaken to the Company, the Sponsor (on behalf of the Underwriters) and the Stock Exchange that in the event that he exercises his right attached to the options granted to him under the Pre-IPO Option Scheme, he will not, save as provided in Rule 13.18 of the GEM Listing Rules, dispose of (or enter into any agreement to dispose of) or permit the registered holder to dispose of (or enter into any agreement to dispose

of) any of the direct or indirect interest in the relevant securities for a period from the date he becomes a beneficial owner of the relevant securities to the expiry of a period of 12 months from the date of listing of the Shares on GEM.

As at 30 September, 2002, no options had been granted or agreed to be granted to any Director.

The options granted under the Pre-IPO Share Option Schemes are not recognized in the financial statements until they are exercised. The Directors consider that it is not appropriate to state the value of the share options granted during the period on the ground that a number of variables such as the market price when the options are exercised and volatility of the market price which are crucial for the valuation of the option value cannot be reasonably determined.

Save as disclosed above, none of the Directors or their associates as well as the chief executive of the Company and its subsidiaries had any personal, family, corporate or other interest in the equity or debt securities of the Company or any of its associated corporations, as defined in the SDI Ordinance. During the interim period, there was no debt securities issued by the Company at any time.

B. Share Option Scheme

The Company conditionally adopted a Share Option Scheme on 2 August, 2002, the principal terms of which are set out in the section headed "Share Option Scheme" in Appendix IV to the Prospectus.

As at 30 September, 2002, no options had been granted or agreed to be granted under the Share Option Scheme. The Group's accounting policy is to recognize the options in the financial statements until they are exercised.

3. SUBSTANTIAL SHAREHOLDERS

As at the Listing Date, the register of substantial shareholders maintained by the Company under Section 16(1) of the SDI Ordinance showed that the following party was entitled to exercise 10% or more of the voting power at general meetings of the Company, or otherwise interested in 10% or more of the Shares then in issue:

Name of shareholder	Number of Shares held	% of holding as at Listing Date
Grand Sum Assets Limited <i>(Note)</i>	59,500,000	10.625

Note: Due to the exercise of options for 67,200,000 Shares of the Company under the Pre-IPO Share Option Scheme during the Interim Period, the number of Shares of the Company issued as at 30 September, 2002 became 627,200,000. As such, Grand Sum Assets Limited only effectively held 9.497% shareholdings of the Company as at 30 September, 2002 and thus it was not a substantial shareholder as at the reporting date.

Save as disclosed above, the Company has not been notified of any other interests representing 10% or more of the issued share capital of the Company.

4. INITIAL MANAGEMENT SHAREHOLDERS

So far as the Directors are aware, as at 30 September, 2002, the following parties were the management shareholders of the Company and were entitled to exercise or control the exercise of 5% or more of the voting power at general meetings of the Company:

Name of shareholder	Number of Shares held	% of holding as at Listing Date
Pearl Rider Overseas Limited	285,600,000	51.00
Lau Tak Wah	59,500,000	10.625

5. SPONSOR'S INTEREST

As at 30 September, 2002, the Company's sponsor, Hantec Capital Limited ("Hantec"), has confirmed that neither it nor its directors, employees or associates (as referred to in Note 3 of Rule 6.35 of the GEM Listing Rules) had any interests in any class of securities (including options or rights to subscribe for such securities) of the Company or any other companies of the Group.

Pursuant to the agreement dated 12 August, 2002 entered into between the Company and Hantec, whereby for a fee as Hantec has agreed to act as the retained sponsor of the Company for the purpose of Chapter 6 of the GEM Listing Rules for the period from 26 August, 2002 to 31 March, 2005.

6. COMPETING INTERESTS

The Directors consider that the business of film production is highly dependent on individual talent and style of a pool of professionals, including film director, screenplay writer, cinematographer as well as actor and actress, to create and present the story of film to audience. The Directors also consider that the audience of a particular film can be varied in terms of demographics and thus each type of films has no specific target audience. As such, the Directors are of the view that no delineation of business in terms of customers, target market, presentation style and production budget could be identified. The Directors aim at strengthening the relationship between Teamwork Corporation Limited ("Teamwork") and the Group by having Mr. Lau Tak Wah Andy ("Mr. Lau"), being one of the shareholders of Teamwork, to become the strategic investors of the Group in order to further expand the Group's film production and investment businesses. On 14th May, 2002, Teamwork transferred 1,250 Shares to Mr. Lau at a consideration of HK\$7,500,000. The Directors believe that competition may exist between the Group and Teamwork in the realm of the businesses of film production, investment and distribution. Upon completion of the Capitalisation Issue and to Share Offer, Mr. Lau will own approximately 10.625% of shareholdings in the Company. Regardless of the foregoing, Mr. Lau is a passive investor and is not controlling shareholder and has not participated and will not actively participate in the daily operations of the Group. Therefore, the Directors believe that following mechanisms and undertakings given by Mr.

Lau would sufficiently safeguard the interests of the Shareholders and the Company as a whole.

Film investment

Following the listing of the Shares on GEM, the Group will continue its existing film production business and intends to explore film investment business. The Directors are of the view that the film investment business of Teamwork Group will not compete directly with the Group's film investment business but rather they are complementary to each other. Whilst any film projects invested by Teamwork Group can provide an opportunity for the Group to invest and vice versa. However, in respect of any business opportunity for film investment available to or received by Teamwork and any of its subsidiaries initiated by third parties, it would not be appropriate for Team work to invite the Group to engage in such opportunity.

Mr. Lau has undertaken to the Company that he will use his reasonable endeavours to grant a first right of refusal to the Company on the same terms and conditions applicable to him and/or his associates in respect of any film project to be invested by Mr. Lau and/or his associates. Such first right of refusal for each film project will lapse if it is not exercised by the Company within 7 business days from the offer made by Mr. Lau.

Such right of first refusal given by Mr. Lau to the Company will cease to have effect on the date on which (i) the Company ceases to be listed on GEM; or (ii) the Group ceases to engage in film production business; or (iii) Mr. Lau and his associates as a group cease to be a substantial shareholder of the Company.

The independent non-executive Directors will review the reasonableness of rejecting each business opportunity offered by each of Mr. Lau and his associates. In addition, the Company has undertaken to provide all necessary assistance (together with all information, documents and other materials) to the independent non-executive Directors in reviewing and opining on the reasonableness of the Group in rejecting each business opportunity offered by each of them and/or their respective associates.

Film production

In respect of any business opportunity for film production available to or received by Teamwork and any of its subsidiaries initiated by third parties, it would not be appropriate for Teamwork to invite the Group to engage in such business opportunity.

Mr. Lau has undertaken to the Company that in the event Mr. Lau considers appropriate to outsource the production of films for which he and/or his associates is the sole producer, priority will be given to the Group if the terms of engagement offered by the Group are comparable with those offered by other film production companies.

The above undertaking shall cease to have effect on the date on which (i) the Company ceases to be listed on GEM; or (ii) the Group ceases to engage in film production business; or (iii) Mr. Lau and his associates as a group cease to be a substantial shareholder of the Company.

Film distribution

The Group intends to establish its film library by making investment in selected film projects. The Directors envisage that the Group will not distribute any film titles that are not invested by it or co-invested with other film companies. As such, the Directors consider that the Group will not compete with Teamwork in the business of film distribution as Teamwork would be one of its partners to co-investing in particular film projects and sharing income generated from distribution of these film projects.

Significance of relationship with Teamwork and its subsidiaries ("Teamwork Group")

Given the proven success and wide recognition of Teamwork Group and Mr. Lau in the film industry in Hong Kong and Asian countries, the Directors believe that the relationship with Teamwork Group would enhance the Group's public awareness and access to additional business opportunities in film production as well as film investment. The Directors believe that such relationship gives the

Group access to opportunities, exposures and relationships that it might not otherwise have.

In addition, the Group and Teamwork Motion Pictures Limited (“Teamwork MP”) have entered into a Master Production Agreement pursuant to which the Group has been engaged by Teamwork MP to produce six films with an aggregate estimated production budget of approximately HK\$66.0 million. Such transaction constitutes ongoing connected transactions for the Company subsequent to the listing of the Shares on GEM and the Company has applied for and obtained a waiver from the Stock Exchange.

Save as disclosed above and as far as the Directors are aware, none of the Shareholders or Directors has any interest in any business that is in competition with that of the Group.

Non-competition undertaking

Mr. To Kei Fung (“Mr To”) has unconditionally and irrevocably undertaken to the Company that he will not at any time during which the Company is listed on the GEM and as long as he and/or his associates hold, whether individually or altogether, 10% or more direct or indirect interest of the Company, or he is a Director, directly or indirectly carry on, participate in or be engaged, concerned or interested in any business which competes or may compete with the business of the Group from time to time including in the provision of film director, producer and/or consultant services to companies whose business shall compete, or may compete, from time to time with any members of the Group.

Save as disclosed above, none of the Directors or of chief executives of the Group, the management shareholders or the substantial shareholders (as defined in the GEM Listing Rules) of the Company or their respective associates had any interests in any business which cause or may cause any significant competition with the business of the Group.

7. BOARD PRACTICES AND PROCEDURES

During the period from the date on which dealings of the shares of the Company first commenced on GEM to 30 September 2002, the Company had complied with the board practice and procedures as set out in Rules 5.28 to 5.39 of the GEM Listing Rules.

8. PURCHASE, SALE OR REDEMPTION OF LISTED SECURITIES

During the period from the date on which dealings of the shares of the Company first commenced on GEM to 30 September, 2002, neither the Company nor any of its subsidiaries had purchased, sold or redeemed any of the Company's listed shares.

9. AUDIT COMMITTEE

The Company has established an audit committee on 2 August, 2002 with written terms of reference in compliance with Rules 5.23 to 5.25 of the GEM Listing Rules. The primary duties of the audit committee are to review and supervise the financial reporting process and internal control system of the Group. The audit committee is consisted of two independent non-executive directors. The Group's unaudited results for the six months ended 30 September, 2002 had been reviewed by the audit committee.

By order of the board
Milkyway Image Holdings Limited
Mr. To Kei Fung
Chairman

Hong Kong, 12 November 2002