

iMerchants Limited
Half Year Report 2002-2003

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This report, for which the directors of iMerchants Limited collectively and individually accept responsibility, includes particulars given in compliance with the Rules Governing the Listing of Securities on the Growth Enterprise Market of the Stock Exchange for the purpose of giving information with regard to iMerchants 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.

CHAIRMAN'S STATEMENT

I am pleased to announce the results for the first six months of iMerchants' 2002/2003 financial year. The Company has undertaken a number of important initiatives over the past half-year from which we are beginning to see some encouraging results. Although market conditions continue to be challenging, I am confident in the Company's prospects for the future.

Highlights

- In view of shifting market conditions, iMerchants undertook an intense business assessment followed by a restructuring of its business lines in effort to build a more tightly focused business with improved profit potential.
- In April 2002, iMerchants officially launched its PRC operations with the opening of its Beijing office.
- As a result of improvements in operational efficiency, direct costs as percentage of turnover for the first six months of the 2002/3 financial year decreased 12% from the first six months of the previous year.

Business direction

In the most recent quarter, iMerchants undertook a business review with the express purpose of creating an even more tightly focused business with improved profit potential. As a direct result, iMerchants has now narrowed its solution and service offering to two key business lines, namely Wealth Management and Professional Services.

The case for selecting Wealth Management as an area of focus is particularly compelling. Although still a relatively new concept in Asia, wealth management service provision is steadily gaining in popularity among financial services organizations across the region. Uniquely, this service has demonstrated its relevance across the industry with banks, insurers, brokers and financial advisors all scrambling to access the revenue potential of the mass affluent consumer market. For iMerchants as a solution provider, this presents an excellent opportunity to stretch our development and marketing investment across a relatively large yet targeted market and to leverage our existing expertise and relationships in the industry.

iMerchants' Wealth Management Suite provides financial services staff with instant access to customer portfolios, interactive portfolio assessment and other sales support tools as well as on demand updates for investment products. Specifically, it equips frontline staff to manage customer accounts efficiently and effectively; and to deliver the personal service that their high-value customers want in a cost effective and scalable manner. In the first half of this year, the Company continued to invest heavily in research and development in this area and, in addition, initiated sales and marketing activities for the Suite.

iMerchants Professional Services enables the Company to meet the special requirements of financial services clients through the provision of system integration and custom development services such as the e-submission and market surveillance systems recently delivered to a high-profile client. In complement to the Wealth Management business line, it enables iMerchants to be a broad service vendor offering excellent opportunity for cross- and up-sell of solutions and services. Additionally, the Professional Services business line provides the means for iMerchants and its clients to continue exploiting the wealth of experience that iMerchants has built up over the years through both product development and bespoke work in areas such as Public Key Infrastructure enablement and online bill publishing.

Geographical expansion

Another important step in the past half-year has been the launch of iMerchants' PRC operations in April 2002, under the name iMerchants' Technologies (Beijing) Co. Ltd. This new entity, staffed by employees from both the PRC and Hong Kong, enables the Company to take advantage of a young and vast IT market as well as the relatively low cost base offered by the PRC. Like in Hong Kong, iMerchants in the PRC is focusing on serving the needs of the financial services industry.

Quality and efficiency

Also in April 2002, iMerchants' core business processes, from prospecting and engagement through to development, implementation and client support, were certified as compliant with the ISO 9001:2000 quality standard. Following receipt of the certification, iMerchants initiated new continuous improvement procedures that enable the Company to further enhance its sale and service delivery methodology on an ongoing basis. The management team believes that through its formal quality management system and system development methodology, iMerchants will be able to give its clients additional confidence in its ability to deliver quality solutions, and that this in turn will improve the Company's ability to compete.

MANAGEMENT DISCUSSION AND ANALYSIS

Prospects for new business

Although the IT market continues to be difficult, iMerchants remains cautiously optimistic. iMerchants' target market, the financial service sector, continues to be under great pressure and, as a result, clients are still very careful with their IT investments placing substantial emphasis on those areas where a return can be most easily realized such as efficiency improvements and maintenance. The financial services market in the PRC offers additional opportunities as local

institutions work to enhance their performance in the light of new international competition, iMerchants is taking a careful yet deliberate approach in recognition of the challenges that come with entry into this new market.

iMerchants' approach to wealth management offers excellent value to clients as a vertical solution covering the back office order processing and reconciliation through to frontline customer service support. We believe that this emphasis on operational support will be an especially attractive feature for institutions looking to initiate or scale their wealth management service offering. The Company will continue to invest in research and development with plans to significantly ramp up sales and marketing efforts in the latter half of the fiscal year.

In the Professional Services area, iMerchants continues to provide support to a number of long-term clients and to build its reputation as a provider of highly specialized quality custom solutions. In addition, as a Public Key infrastructure enabler for both financial services and government organizations, the Company is well positioned to take advantage of the increasing demand for high-end security in the area of security solutions.

We believe with the new structure and initiatives in place, the Company has turned a corner and is well positioned to meet the current and future technology needs of the financial service industry both in Hong Kong and the PRC. With a number of strong leads in the sales pipeline, we are optimistic about our sales prospects for the second half of our 2002/2003 fiscal year.

Financial performance review

iMerchants' financial results for the six months ended 30 September 2002 continue to show the effects of a difficult market as well as the

early impact of the Company's recent restructuring and quality improvement initiatives. This period represents a time of change for iMerchants.

Largely due to a substantial reduction in related hardware sales, the Company recorded a decrease in turnover to HK\$4,476,000 from HK\$13,278,000 in 2001. The Company's target sector continues to be under great pressure and clients remain particularly careful with their IT investments. Although the decrease appears to be dramatic, the decline in low-margin hardware sales has had limited impact on the bottom line. Turnover also includes an accompanying decrease in project income. This, however, appears to be short-lived with Second Quarter revenue for 2002 nearly doubling that reported for the First Quarter. Most encouragingly, gross profit demonstrates strong growth driven by the improvement in efficiency as reflected from the 12% decrease in direct costs as percentage of turnover for the first six months of the 2002 from 2001.

The Company generated a net loss of HK\$22,571,000 compared to HK\$16,650,000 for the corresponding period in 2001. This increase largely results from a management decision to change the treatment of salaries expenses whereby the recognition of those salaries directly related to product development which were previously capitalized as intangible assets, are now recognized as part of the administrative expenses. Due to the timing of the Company's restructuring effort, this period also carries the necessary costs associated with the restructuring. The related financial benefit however, will not be reflected until the forthcoming quarters.

Commentary on segmental information

The Group's turnover and contribution to results are substantially derived from the provision of IT solutions and related services. Accordingly, no analysis by business segment is presented in the financial statements.

For the six months ended 30 September 2002, as for the corresponding period in 2001, all of the Company's turnover was derived from the Hong Kong market reflecting the Company's current focus on its home market. Approximately 24% of the loss before taxation in Hong Kong can be directly attributed to presales investment, the adoption of a more conservative approach for recognition of product development related salaries, and compensation costs related to the restructuring.

The Company has, for the time being, decided to limit its geographical expansion to the PRC and regards those losses recognised for this location as a start-up investment.

Investments

The Group has an investment of approximately HK\$8 million in Net Alliance Company Limited ("Net Alliance"), a company which provides online banking service bureau operations to a group of four banks in Hong Kong. iMerchants believes that, as the cost is shared among the member banks of Net Alliance, Net Alliance has been quite successful at implementing new means of delivering IT solutions at a comparatively low cost to financial institutions in Hong Kong. The Group expects Net Alliance's revenues and costs to remain quite stable during the coming years and believes that, as additional services are offered, Net Alliance has the potential to attract more banks to join as members, leading it to become a successful service provider.

As at 30 September 2002, the Group has approximately HK\$95 million (31 March 2002: approximately HK\$55 million) worth of investments in marketable securities, which are all investment-grade fixed income investments with high ratings. The management currently intends to hold these investments on a long-term basis up to their respective maturity dates.

Liquidity, financial resources and capital structure

There has been no change in the capital structure of the Group during the reported period. The Group continues to be in a healthy financial position with current assets plus investments in marketable securities and time deposits totalling approximately HK\$231 million (31 March 2002: HK\$249 million) and no bank borrowings as at 30 September 2002. As 56% of this total consists of bank balances, time deposits and cash held in-hand, and investments in marketable securities account for a further 41% of the total, the Group considers its financial resources to be highly liquid. The Group aims to minimize its financing costs by managing the maturity of its financial investments in such manner so as to provide sufficient funds to cover ongoing expenses.

In accordance with the Business Objectives stated in the Company's prospectus dated 27 March 2000, the Group continues to explore the possibility of acquiring or taking equity stakes in companies whose activities have synergy with those of the Group. However, the Group does not currently have any target company in which it plans to invest. The Group currently expects its primary capital expenditures to be investments in the computer hardware and software required for it to perform its solution development activities and to provide services to its clients. It is also currently expected that these capital expenditures and the ongoing operating expenses will be financed from the Group's existing financial resources, and the Directors do not foresee the need for any material financing activities in order to execute the Group's plans. The Group did not undertake any material acquisitions and disposals of subsidiaries and affiliated companies in the course of the six months ended 30 September 2002.

In respect of trade receivables, as the Group's customers are predominantly other listed companies, banks, or divisions of large multinational companies, the management believes the risk of default payment by the Group's customers is very low. Nonetheless, the level of accounts receivable to each individual customer is monitored on a monthly basis, with late payments being promptly pursued by the Group's Accounting Department.

As at 30 September 2002, 17% of the Group's cash and bank balances and marketable investments were denominated in Hong Kong dollars, 82% in US dollars and a nominal amount is held in Renminbi. Given the liquid nature of these marketable investments and the currency peg between the Hong Kong dollar and the US dollar, the Group does not hedge its exchange rate exposures.

The Group's gearing ratio as at 30 September 2002 was 0% (31 March 2002: 0%), as calculated by taking the ratio of the Group's total interest-bearing borrowings, divided by its shareholders' funds. The Group has no borrowings as at 30 September 2002 (31 March 2002: Nil). The Group also has no contingent liabilities and no charges on group assets as at 30 September 2002 (31 March 2002: Nil).

Employees

As at 30 September 2002, the Group employed 64 staff (31 March 2002: 87). In concert with the Company's business assessment and re-focusing effort, iMerchants reviewed its complement of staff to ensure the best possible fit with the Company's chosen focus for the future. As a result, the Quarter ended with the current reduced headcount of 64 with express plans for recruitment to build our strength in selected areas.

Remuneration for the Group's employees is typically reviewed once a year, or as the management deems appropriate. Changes in remuneration are based on a range of factors including the Group's performance, the competitiveness of remuneration with the external market, and individual employees' performance during the year. For the six months ended 30 September 2002, the Group's total remuneration expenses, including contributions to the Mandatory Provident Fund were HK\$18.6 million (six months ended 30 September 2001: HK\$21.2 million). A portion of these expenses was charged to direct costs of development for projects, some paid for compensation and severance as a result of the restructuring exercise and the balance

was recorded as administrative expenses. This total was approximately 12% less than the corresponding period last year, because of the decrease in the average headcount, the departure of a management staff who received a high salary package and also because of the Company not having looked to replace staff who left through normal resignation.

The Group has introduced share option schemes to recognise the contributions of its employees to the development of the Group. As at 30 September 2002, a total of 76,960,000 share options remained outstanding. None had been exercised during the reported period. The schemes have been or will be amended from time to time to take into account changes in market conditions and the GEM Listing Rules.

USE OF PROCEEDS

The net proceeds raised from the public listing on 31 March 2000 were approximately HK\$325 million. These proceeds had been applied to achieve the business objectives as set out in the prospectus dated 27 March 2000 (“Prospectus”) and detailed below:

	As stated in the Prospectus (from 1 April 2000 to 31 March 2002) <i>HK\$ million</i>	Actual (from 1 April 2000 to 30 September 2002) <i>HK\$ million</i>
For enhancing knowledge creation and management processes and strengthening corporate infrastructure	90	30
For enhancing service offering and expanding capacity to deliver	35	40
For geographical expansion in Asia	42	3
For business development and marketing activities	48	22
For acquisition of or investment in ventures	64	24
For general working capital	46	64
	<hr/>	<hr/>
Total	<u>325</u>	<u>183</u>

The remaining net proceeds have been partly placed in interest-bearing accounts with licensed banks in Hong Kong and partly invested in fixed income marketable securities.

There has been no change in business nature since the time that the Group's Prospectus was prepared. Due to the recent unfavourable economic situation in Hong Kong and a very competitive market, the IT industry has developed and transformed into something quite different from the Group's forecast and the expected market situation at that time. In response, the Group has taken a more conservative tact in rolling out its business objectives than originally planned as it was considered to be in the best interest of the Group and its shareholders.

Due to the greatly slowed regional IT market, the Group has limited its geographical expansion to date to mainland China. Correspondingly, corporate infrastructure requirements as well as expenditure for business development and marketing have been limited to that required to support operations in Hong Kong and the PRC markets. The Group has, to date, also used less than originally planned for investment in or acquisition of ventures due to the Group's tight criteria for investment and the changed market environment.

RESULTS

The board of Directors (the “Board”) of the Company presents the unaudited consolidated results of the Company and its subsidiaries (the “Group”) for the three months and six months ended 30 September 2002 together with the comparative unaudited figures for the corresponding periods in 2001 as follows:

Unaudited Consolidated Income Statement

For the three months and six months ended 30 September 2002

	Notes	Three months ended 30 September		Six months ended 30 September	
		2002 HK\$'000	2001 HK\$'000	2002 HK\$'000	2001 HK\$'000
Turnover	2	2,910	4,673	4,476	13,278
Cost of sales and direct costs		(2,158)	(4,858)	(3,865)	(13,048)
Gross profit/(loss)		752	(185)	611	230
Other revenue	2	1,719	2,778	4,021	6,326
Administrative expenses		(14,622)	(10,703)	(27,203)	(21,274)
Loss from operations	4	(12,151)	(8,110)	(22,571)	(14,718)
Finance costs		-	(7)	-	(7)
Share of results of associates		-	(147)	-	(1,925)
Loss before taxation		(12,151)	(8,264)	(22,571)	(16,650)
Taxation	5	-	-	-	-
Loss attributable to shareholders		(12,151)	(8,264)	(22,571)	(16,650)
Loss per share – basic	6	(1.046) cent	(0.710) cent	(1.943) cent	(1.430) cent

Consolidated Balance Sheet

As at 30 September 2002

		30 September 2002 (Unaudited) HK\$'000	31 March 2002 (Audited) HK\$'000
	<i>Notes</i>		
NON-CURRENT ASSETS			
Property, plant and equipment		6,005	8,512
Interests in associates		7,884	9,309
Investment in securities		78,891	53,403
Long-term bank deposits		23,400	23,400
		<hr/> 116,180 <hr/>	<hr/> 94,624 <hr/>
CURRENT ASSETS			
Inventories		599	1,024
Amount due from customers for contract work		798	892
Trade and other receivables	8	5,334	10,639
Investment in securities		15,654	1,497
Amount due from an associate		–	24
Short-term bank deposits		92,369	142,463
Bank balances and cash		13,731	15,958
		<hr/> 128,485 <hr/>	<hr/> 172,497 <hr/>
CURRENT LIABILITIES			
Trade and other payables	9	2,788	2,673
Tax liabilities		–	–
		<hr/> 2,788 <hr/>	<hr/> 2,673 <hr/>
NET CURRENT ASSETS			
		<hr/> 125,697 <hr/>	<hr/> 169,824 <hr/>
		<hr/> 241,877 <hr/>	<hr/> 264,448 <hr/>
CAPITAL AND RESERVES			
Share capital	10	116,139	116,139
Reserves	11	125,738	148,309
		<hr/> 241,877 <hr/>	<hr/> 264,448 <hr/>

Unaudited Condensed Consolidated Cash Flow Statement

For the six months ended 30 September 2002

	Six months ended	
	30 September	
	2002	2001
	(Unaudited)	(Unaudited)
	HK'000	HK'000
Net cash used in operating activities	(18,071)	(32,346)
Net cash (used in)/from investing activities	(60,197)	118,852
Net cash from/(used in) financing activities	2,547	(671)
	<hr/>	<hr/>
Net decrease/increase in cash and cash equivalents	(75,721)	85,835
Cash and cash equivalents at beginning of period	158,421	132,444
	<hr/>	<hr/>
Cash and cash equivalents at end of period	82,700	218,279
	<hr/> <hr/>	<hr/> <hr/>
Analysis of balances of cash and cash equivalents		
Short-term bank deposits	92,369	206,923
Bank balances and cash	13,731	11,356
Less: Short-term bank deposits with more than three months' maturity	(23,400)	–
	<hr/>	<hr/>
	82,700	218,279
	<hr/> <hr/>	<hr/> <hr/>

Consolidated Statement of Changes in Equity

For the six months ended 30 September 2002

	Six months ended	
	30 September	
	2002	2001
	(Unaudited)	(Unaudited)
	HK'000	HK'000
At beginning of the period – total equity	264,448	340,017
Loss for the period	(22,571)	(16,650)
Share repurchased	–	(671)
	<hr/>	<hr/>
At end of the period – total equity	<u>241,877</u>	<u>322,696</u>

Notes to the condensed interim financial statements

1. Basis of preparation and accounting policies

The unaudited condensed interim financial statements have been prepared under the historical cost convention and in accordance with Hong Kong Statement of Standard Accounting Practice (“SSAP”) 2.125 “Interim Financial Reporting” issued by the Hong Kong Society of Accountants and the disclosure requirements set out in Chapter 18 of the GEM Listing Rules. The unaudited condensed interim financial statements should be read in conjunction with the annual financial statements for the year ended 31 March 2002.

The accounting policies and methods of computation used in the preparation of the unaudited condensed interim financial statements are consistent with those used in the annual financial statements for the year ended 31 March 2002, except that the Group has adopted the new and revised SSAPs which became effective on 1 April 2002. The adoption of these new and revised SSAPs has no material effect on the Group's results.

Certain comparative figures have been reclassified to conform with the current period's presentation.

2. Turnover and other revenue

Turnover represents revenue generated from contracts for consultancy and software development, including the sale of the related equipment and the amounts received and receivable for other related services rendered, and sales of goods by the Group to customers during the period.

An analysis of turnover is as follows:

	Six months ended	
	30 September	
	2002	2001
	HK'000	HK'000
Revenue from contracts for consultancy, software development and related hardware	4,080	13,278
Sales of goods	396	—
	<hr/>	<hr/>
	4,476	13,278
	<hr/> <hr/>	<hr/> <hr/>

Other revenue for the period comprised, among others, interest income of approximately HK\$4,021,000 (2001: HK\$5,967,000).

3. Segment information

Business segments

The Group's turnover and results are substantially derived from the provision of IT solutions and related services. Accordingly, no analysis by business segment is presented.

Geographical segments

The following table provides an analysis of the Group's sales by the geographical area in which the Group's companies are operated:

	Hong Kong		Republic of Singapore		People's Republic of China		Consolidated	
	6 months ended		6 months ended		6 months ended		6 months ended	
	30 September		30 September		30 September		30 September	
	2002	2001	2002	2001	2002	2001	2002	2001
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Turnover	4,476	13,278	-	-	-	-	4,476	13,278
Cost of sales and direct costs	(3,865)	(12,949)	-	(99)	-	-	(3,865)	(13,048)
Depreciation and amortisation	(3,529)	(3,975)	-	-	(50)	-	(3,579)	(3,975)
Administrative expenses	(22,438)	(17,288)	(35)	(11)	(1,151)	-	(23,624)	(17,299)
Segment results	(25,356)	(20,934)	(35)	(110)	(1,201)	-	(26,592)	(21,044)
Other revenue	4,018	6,320	-	6	3	-	4,021	6,326
Interest on bank overdrafts	-	(7)	-	-	-	-	-	(7)
Share of results of associates	-	(1,925)	-	-	-	-	-	(1,925)
Loss before taxation	(21,338)	(16,546)	(35)	(104)	(1,198)	-	(22,571)	(16,650)
Taxation	-	-	-	-	-	-	-	-
Loss for the period	(21,338)	(16,546)	(35)	(104)	(1,198)	-	(22,571)	(16,650)

The following is an analysis of the carrying amount of segment assets, additions to property, plant and equipment, intangible assets and the carrying amount of segment liabilities analysed by reference to the geographical area in which the Group's companies are operated:

	Hong Kong		Republic of Singapore		People's Republic of China		Consolidated	
	30 Sept 2002	31 March 2002	30 Sept 2002	31 March 2002	30 Sept 2002	31 March 2002	30 Sept 2002	31 March 2002
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Segment assets	<u>12,049</u>	<u>21,901</u>	<u>9</u>	<u>41</u>	<u>678</u>	<u>372</u>	12,736	21,504
Unallocated assets							<u>231,929</u>	<u>245,617</u>
Consolidated total assets							<u>244,665</u>	<u>267,121</u>
Segment liabilities	<u>2,715</u>	<u>2,610</u>	<u>39</u>	<u>48</u>	<u>34</u>	<u>15</u>	2,788	2,673
Unallocated liabilities							<u>-</u>	<u>-</u>
Consolidated total liabilities							<u>2,788</u>	<u>2,673</u>
Additions of property, plant and equipment	<u>85</u>	<u>2,212</u>	<u>-</u>	<u>-</u>	<u>553</u>	<u>-</u>	<u>638</u>	<u>2,212</u>
Additions of platform development costs	<u>-</u>	<u>9,592</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>9,592</u>

4. Loss from operations

Loss from operations is arrived at after charging:

	Six months ended 30 September	
	2002	2001
	<i>HK'000</i>	<i>HK'000</i>
Depreciation	3,145	3,008
Amortisation of platform development costs	–	963
Amortisation of premium on acquisition of held-to-maturity securities	<u>434</u>	<u>4</u>

5. Taxation

No provision for Hong Kong Profits Tax has been made as the Group incurred tax losses for the period (2001: Nil).

6. Loss per share

The calculation of the loss per share for the three months and the six months ended 30 September 2002 is based on the loss of the Group of approximately HK\$12,151,000 (2001: loss of approximately HK\$8,264,000) and approximately HK\$22,571,000 (2001: loss of approximately HK\$16,650,000), respectively, and on the weighted average number of ordinary shares of 1,161,382,000 (2001: 1,164,026,721).

No diluted loss per share has been presented because the exercise price of the Company's outstanding share options was higher than the average market price of the Company's shares for both periods.

7. Interim dividend

The Directors do not recommend the payment of an interim dividend for the six months ended 30 September 2002 (2001: Nil).

8. Trade and other receivables

The Group allows an average credit period of 30-45 days to its trade customers.

The following is an aged analysis of trade receivable at the period end date:

	30 September 2002 HK\$'000	31 March 2002 HK\$'000
0-60 days	1,554	4,019
61-90 days	–	204
Over 90 days	<u>269</u>	<u>1,281</u>
Trade receivables	1,823	5,504
Accounts receivable repayable by monthly instalments	–	2,320
Other receivables	<u>3,511</u>	<u>2,815</u>
	<u>5,334</u>	<u>10,639</u>

9. Trade and other payables

	30 September 2002 HK\$'000	31 March 2002 HK\$'000
Trade payables	–	–
Other payables	<u>2,788</u>	<u>2,673</u>
	<u>2,788</u>	<u>2,673</u>

There were no trade payables as at 30 September 2002 and so no ageing analysis is presented.

10. Share capital

	Number of ordinary shares	Amount HK\$
Ordinary shares of HK\$0.10 each		
<i>Authorised:</i>		
At 31 March and 30 September 2002	<u>8,000,000,000</u>	<u>800,000</u>
<i>Issued and fully paid:</i>		
At 31 March and 30 September 2002	<u>1,161,382,000</u>	<u>116,139</u>

None of the Company's subsidiaries purchased, sold or redeemed any of the Company's listed securities during the six months ended 30 September 2002.

There was no movement in the Company's authorised share capital for the year ended 31 March 2002 and for the six months ended 30 September 2002.

11. Reserves

	Share premium HK\$'000	Goodwill HK\$'000	Negative goodwill HK\$'000	Capital redemption reserve HK\$'000	Merger reserve HK\$'000	Accumulated losses HK\$'000	Total HK\$'000
At 1 April 2001	207,130	(4,900)	1,884	-	46,715	(27,360)	223,469
Premium arising on share repurchases	-	-	-	-	(340)	-	(340)
Transfer	-	-	-	331	(331)	-	-
Loss for the period	-	-	-	-	-	(16,650)	(16,650)
At 30 September 2001	<u>207,130</u>	<u>(4,900)</u>	<u>1,884</u>	<u>331</u>	<u>46,044</u>	<u>(44,010)</u>	<u>206,479</u>

	Share premium HK\$'000	Negative goodwill HK\$'000	Capital redemption reserve HK\$'000	Merger reserve HK\$'000	Accumulated losses HK\$'000	Total HK\$'000
At 1 April 2002	207,130	1,884	409	45,918	(107,032)	148,309
Loss for the period	—	—	—	—	(22,571)	(22,571)
At 30 September 2002	<u>207,130</u>	<u>1,884</u>	<u>409</u>	<u>45,918</u>	<u>(129,603)</u>	<u>125,738</u>

12. Operating lease commitments

At the balance sheet date, the Group had commitments for future minimum lease payments under non-cancellable operating leases which fall due as follows:

	Land and buildings		Software licensing	
	30 Sept 2002	31 March 2002	30 Sept 2002	31 March 2002
Within one year	2,747	2,455	—	316
In the second to fifth year inclusive	2,894	190	—	3,702
	<u>5,641</u>	<u>2,645</u>	<u>—</u>	<u>4,018</u>

Operating lease payments in respect of land and buildings represent rentals payable by the Group for its office premises. Leases are negotiated for an average term of four years and rentals are fixed for an average of two years.

Operating lease contract in respect of software licensing has been terminated on 24 July 2002 by a mutual agreement with the vendor.

13. Capital commitments

	30 September	31 March
	2002	2002
	<i>HK\$'000</i>	<i>HK\$'000</i>
Capital expenditure in respect of the acquisition of property, plant and equipment contracted for but not provided in the financial statements	—	164

14. Other commitments

At the balance sheet date, the Group had commitments for future minimum payments for software maintenance and support services which fall due as follows:

	30 September	31 March
	2002	2002
	<i>HK\$'000</i>	<i>HK\$'000</i>
Within one year	—	286
In the second to fifth year inclusive	—	3,332
	—	3,618

The contract for software maintenance and support services has been terminated on 24 July 2002 by a mutual agreement with the vendor.

15. Related party disclosures

During the period, the Group had the following transactions with related parties:

	Six months ended 30 September	
	2002	2002
	HK\$'000	HK\$'000
Revenue generated from contracts for consultancy and software development performed for:		
– associates	1,018	723
Rental income from the immediate holding company	–	240
Service fee income from the immediate holding company	–	73
	<u>–</u>	<u>73</u>

The above related party transactions were carried out in accordance with the relevant agreements governing these transactions.

PURCHASE, SALE OR REDEMPTION OF SHARES

During the six months ended 30 September 2002, neither the Company nor any of its subsidiaries purchased, sold or redeemed any of the Company's listed securities.

COMPETING INTERESTS

During the period under review, none of the directors or the management shareholders (as defined in the GEM Listing Rules) of the Company had an interest in a business that competed with the Group or might compete with the business of the Group.

DIRECTORS' INTERESTS IN SECURITIES

At 30 September 2002, the interests of the directors of the Company and their associates in the securities of the Company as recorded in the register maintained by the Company pursuant to Section 29 of the Securities (Disclosure of Interests) Ordinance (the "SDI Ordinance") were as follows:

Name of director	Number of ordinary shares held as		Number of shares entitled under the share option schemes held as
	personal interests	corporate interests	personal interests
Mr Leroy Kung Lin Yuen ("Mr Kung")	–	747,023,000 <i>(Note i)</i>	–
Mr Edward Un Ding Bong ("Mr Un")	–	–	10,000,000 <i>(Note ii)</i>

Notes:

- (i) The registered shareholder of 747,023,000 shares is iMerchants Group Limited ("iMerchants Group"). iMerchants Group is wholly-owned by Asian Gold Associates Limited ("Asian Gold"), in which 76% of the issued share capital of Asian Gold is owned by Galaface Limited ("Galaface"). Mr Kung is deemed to have interests in the 747,023,000 shares owned by iMerchants Group under the SDI Ordinance as he owns the entire interest in Galaface and is entitled to exercise more than one-third of the voting power at general meetings of both Asian Gold and Galaface.

- (ii) Among the balance, 2,000,000 share options were granted on 23 August 2000 under a share option scheme, which was approved by the written resolution of the shareholders of the Company dated 15 March 2000. These share options entitle Mr Un to subscribe for 2,000,000 shares of HK\$0.10 each in the Company at HK\$0.53 each in various stages from 31 March 2001 to 23 August 2010.

The remaining 8,000,000 share options were granted on 27 September 2002 under the 2002 Share Option Scheme, which was approved by the shareholders of the Company in the special general meeting dated 2 August 2002. These share options entitle Mr Un to subscribe for 8,000,000 shares of HK\$0.10 each in the Company at HK\$0.172 each in various stages from 1 September 2003 to 28 August 2012.

Save as disclosed above, at 30 September 2002, none of the directors or any of their associates had any interests in any securities of the Company or any of its associated corporations as defined in the SDI Ordinance.

OUTSTANDING SHARE OPTIONS

Pursuant to the Pre-IPO Share Option Plan, Share Option Scheme and 2002 Share Option Scheme, there were 32,830,000, 36,130,000 and 8,000,000 share options, respectively, granted to and held by the grantees (which include the options granted to a director of the Company, as disclosed above) as at 30 September 2002. Details of which are as follows:

(a) Pre-IPO Share Option Plan

As at 30 September 2002, options comprising an aggregate of 32,830,000 underlying shares to subscribe for shares in the Company at an exercise price of HK\$1.48 per share (granted on 15 March 2000) were outstanding. No options have been granted during the six months ended 30 September 2002 under the Pre-IPO Share Option Plan as the right to do so was terminated upon the listing of the Company on the GEM.

Details of the outstanding Pre-IPO share options during the six months ended 30 September 2002 are set out below:

Type of grantees	As at 1 April 2002	Lapsed during the six months	Reclassification	As at 30 September 2002
Director	11,670,000	–	(11,670,000)	–
Employees	25,330,000	(4,170,000)	11,670,000	32,830,000
	<u>37,000,000</u>	<u>(4,170,000)</u>	<u>–</u>	<u>32,830,000</u>
		(note 1)	(note 2)	

Notes:

1. These options granted to one employee were lapsed when he ceased to be employed by the Company.
2. On 15 March 2000, 11,670,000 share options were granted to Mr Matthew P Johnston (“Mr Johnston”) when he was an executive director of the Company. Mr Johnston resigned as the director of the Company with effect from 20 July 2002 and so the options are reclassified.
3. The exercise period of the Pre-IPO options is from 31 March 2001 to 14 March 2010.
4. Options pursuant to the Pre-IPO Share Option Plan may be exercised in accordance with the terms of the scheme as to:
 - a. one quarter of the options (rounded down to the nearest board lot) will be exercisable from 1 April 2001 (“First Exercise Date”);
 - b. an additional one eighth of the options (rounded down to the nearest board lot) will be exercisable after the expiry of each successive six-month period from the First Exercise Date; and

- c. the balance of the options exercisable after the expiry of a period of 48 months from 1 April 2001.
5. As of 30 September 2002, no options under the Pre-IPO Share Option Plan have been exercised or cancelled.

(b) Share Option Scheme

As at 30 September 2002, options comprising an aggregate of 36,130,000 underlying shares to subscribe for shares in the Company at an exercise price of HK\$0.53 per share (granted on 23 August 2000) were outstanding. No options have been granted during the six months ended 30 September 2002 under the Share Option Scheme. Details of the grant of share options under the Share Option Scheme to the Directors are set out in the previous section headed "Directors' Interests in Securities" in this report.

Details of the outstanding options under the Share Option Scheme during the six months ended 30 September 2002 are set out below:

Type of grantees	As at 1 April 2002	Lapsed during the six months	Reclassification	As at 30 September 2002
Director	11,670,000	–	(9,670,000)	2,000,000
Employees	28,630,000	(4,170,000)	9,670,000	34,130,000
	<u>40,300,000</u>	<u>(4,170,000)</u>	<u>–</u>	<u>36,130,000</u>
		(note 1)	(notes 2 and 3)	

Notes:

1. These options granted to one employee were lapsed when he ceased to be employed by the Company.

2. On 23 August 2000, 11,670,000 share options were granted to Mr Matthew P Johnston ("Mr Johnston") when he was an executive director of the Company. Mr Johnston resigned as the director of the Company with effect from 20 July 2002 and so the options are reclassified.
3. On 23 August 2000, 2,000,000 share options were granted to Mr Un when he was a full-time employee of the Company. Mr Un was appointed as an executive director of the Company with effect from 25 June 2002 and so the options are reclassified.
4. The exercise period of the share options under the Share Option Scheme is from 31 March 2001 to 23 August 2010.
5. Options pursuant to the Share Option Scheme may be exercised in accordance with the terms of the relevant scheme which are the same as those of the Pre-IPO Share Option Plan set out in Note 4 of the subsection headed "Pre-IPO Share Option Plan" above.
6. As of 30 September 2002, no options under the Share Option Scheme have been exercised or cancelled.

(c) **2002 Share Option Scheme**

On 2 August 2002, the Company adopted the 2002 Share Option Scheme under which the board of directors of the Company may at its discretion offer to any Eligible Participant (as defined in the circular of the Company dated 11 July 2002) options to subscribe for shares in the Company in accordance with the terms of the 2002 Share Option Scheme and Chapter 23 of the GEM Listing Rules. The principal purposes of the 2002 Share Option Scheme are to recognise the significant contributions of the Eligible Participants to the growth of the Group. The Pre-IPO Share Option Plan and the Share Option Scheme approved on 15 March 2000 were simultaneously terminated but the options which have been granted during the life of the said option schemes shall continue to be exercisable in accordance

with their respective terms of issue and in all other respects the provisions of the said option schemes shall remain in full force and effect.

Type of grantees	As at 1 April 2002	Granted during the six months	As at 30 September 2002
Director	<u>–</u>	<u>8,000,000</u> <i>(note 1)</i>	<u>8,000,000</u>

Notes:

1. 8,000,000 share options were granted to Mr Un on 27 September 2002 under the 2002 Share Option Scheme at an exercise price of HK\$0.172 per share.
2. The exercise period of the share options under the 2002 Share Option Scheme is from 1 September 2003 to 28 August 2012.
3. Options pursuant to the 2002 Share Option Scheme may be exercisable in accordance with the terms of the scheme as to:
 - a. Options to subscribe for 4,000,000 shares of the Company (rounded down to the nearest board lot) will be exercisable from 1 September 2003 to 28 August 2012; and
 - b. The balance of 4,000,000 options is exercisable from 1 September 2004 to 28 August 2012.
4. As of 30 September 2002, no options under the 2002 Share Option Scheme have been exercised or cancelled.

Save as disclosed above, during the six months ended 30 September 2002, none of the directors and employees of the Company or its subsidiaries was granted options to subscribe for shares in the Company.

Valuation of share options

In assessing the value of the share options granted during the six months ended 30 September 2002, the Black-Scholes Model has been used. The Black-Scholes Model is one of the most generally accepted methodologies to calculate the value of options and is one of the recommended options pricing models as set out in Rule 23.08 of the GEM Listing Rules. The variables of the Black-Scholes Model, include, risk-free interest rate, expected life of the options, and expected volatility and expected dividend of the shares of the Company, if applicable.

The interest rate applied in the Black-Scholes Model is 4.222%, representing the 10-year yield of the Hong Kong Exchange Fund Notes as at the date of grant of the share options (the "Measurement Date"). The volatility ratio of 24.86%, representing the standard deviation of the daily closing share prices of the Company for the last twelve months from the Measurement Date, is used in the Black-Scholes Model. It is assumed that, based on historical pattern, no dividend would be paid out during the vesting period.

The summary of variables used in the Black-Scholes Model for the valuation of 8,000,000 share options granted under the 2002 Share Option Scheme during the six months ended 30 September 2002 and the value thereon is as follows:

Exercise price	HK\$0.172
Time to expiry	10 years
Date of grant	27 September 2002
Stock price as at the Measurement Date	HK\$0.114
Interest rate as at the Measurement Date	4.222%
Volatility as at the Measurement Date	24.86%
Value of each share option granted as at the Measurement Date	HK\$0.0351
Aggregate value of 8,000,000 share options granted as at the Measurement Date (value of each share option X number of share options granted)	HK\$280,800

The summary of the treatment of forfeiture of option prior to the expiry date is set out in the Appendix “Summary of the Principal Rules of the 2002 Share Option Scheme” of the circular dated 11 July 2002 of the Company.

It should be noted that the value of options calculated using the Black-Scholes Model is only an estimate of the value of share options granted during the period. Amongst other variables, it uses the time to expiry to determine a value based on the past performance of the share price as measured by the volatility factor. If, however, the Company’s future financial and/or operating performance fluctuates, it is likely that the share price will be affected. In such case, the financial benefit accruing to the grantee of an option will be considerably different from the value determined under the Black-Scholes Model.

DIRECTORS’ RIGHTS TO ACQUIRE SHARES OR DEBENTURES

Other than the share option schemes as described in the section headed “OUTSTANDING SHARE OPTIONS” above, at no time during the period was the Company, any of its holding companies, fellow subsidiaries or subsidiaries a party to any arrangement to enable the directors of the Company to acquire benefits by means of the acquisition of shares in, or debentures of, the Company or any other body corporate and none of the directors, or their spouses or children under the age of 18, had any right to subscribe for the securities of the Company, or had exercised any such rights.

SUBSTANTIAL SHAREHOLDERS

At 30 September 2002, other than the interests disclosed in the section headed “DIRECTORS’ INTERESTS IN SECURITIES” above, the Company has not been notified of any other interests at 30 September 2002 representing 10% or more of the issued share capital of the Company.

OTHER DIRECTOR'S INTERESTS

Mr Ronny Chow Fan Chim, an independent non-executive director, is a partner of Deacons, legal advisers to the Company. Deacons will receive usual professional fees in connection with the legal services it provides to the Company from time to time.

AUDIT COMMITTEE

The Company's audit committee was formed on 15 March 2000, comprising all the independent non-executive directors, namely, Dr Alice Piera Lam Lee Kiu Yue and Messrs Alex Ko Po Ming and Ronny Chow Fan Chim. The terms of reference of the audit committee have been established with regard to "A Guide for the Formation of an Audit Committee" issued by the Hong Kong Society of Accountants in December 1997. The primary duties of the audit committee are to review and supervise the financial reporting process and internal control procedures of the Group. The audit committee has reviewed the draft of this report and has provided advice and comments thereon.

BOARD PRACTICES AND PROCEDURES

The Company has complied with Board Practices and Procedures as set out in Rules 5.28 to 5.39 of the GEM Listing Rules during the six months ended 30 September 2002.

By order of the Board
Leroy Kung Lin Yuen
Chairman

Hong Kong, 7 November 2002