



**MILKYWAY IMAGE**

**Milkyway Image Holdings Limited**

**銀河映像控股有限公司**

(incorporated in the Cayman Islands with limited liability)

Third Quarterly Report 2002

## **CHARACTERISTICS OF THE GROWTH ENTERPRISE MARKET (“GEM”) OF THE STOCK EXCHANGE OF HONG KONG LIMITED (THE “STOCK EXCHANGE”)**

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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.*

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## HIGHLIGHTS

1. The turnover of the Group during the nine months ended 31 December, 2002 was approximately HK\$33.1 million representing a decrease of approximately 49% as compared with the corresponding period in 2001.
2. The net profit of the Group for the nine months ended 31 December, 2002 was approximately HK\$2.1 million representing a decrease of approximately 68% as compared with the corresponding period in 2001.
3. Earnings per share of the Group was approximately HK cent 0.39 for the nine months ended 31 December, 2002 (2001: HK cents 1.42).
4. The Board does not recommend the payment of any dividend for the nine months ended 31 December, 2002 (2001: HK\$2.208 million).

## **BUSINESS REVIEW AND PROSPECT**

### **Business Review**

For the nine months ended 31 December, 2002, Milkyway Image Holdings Limited (the "Company") and its subsidiaries (together the "Group") recorded an unaudited turnover of approximately HK\$33.1 million representing a drop of approximately 49% over the corresponding period in 2001. The decrease was mainly attributable to the economic downturn in the industry. For the three months period under review, the Group has completed two film projects.

The net profit attributable to shareholders for the nine months ended 31 December, 2002 amounted to approximately HK\$2.1 million, representing a decrease of approximately 68% compared to the corresponding period in 2001. The significant decrease was partly due to the drop in turnover and partly due to an increase in administrative and other operating expenses. Compared with the same period in 2001, administrative and other operating expenses increased by HK\$5.5 million from HK\$2.8 million to HK\$8.3 million. The increase in administrative and other operating expenses was mainly attributable to sharp increase in salaries expenses as a result of reallocation of a film director's fee from production costs. Other components included increased rent, rates and management fee and depreciation of property, plant and equipment.

### **Prospects**

Although the performance of the Hong Kong theatrical market was unexpected low as a result of piracy activities and economic slow down the directors of the Company (the "Directors") remain confident in film industry in that the market still demand for quality film. The Group will continue to focus on its film production business and maintain a leading position in the film production industry in Hong Kong.

Regarding the film production projects signed with One Hundred Years of Films Company Limited, Golden Harvest Film Productions Limited and Teamwork Motion Pictures Limited, the Group has completed one film for the three months ended 31 December, 2002 which has been screened in January 2003 with satisfactory box office receipt of approximately HK\$25 million. Besides, the Group has proceeded with the aforesaid film companies for two more film projects which are expected to be completed in the second quarter of 2003.

In addition, the Group has signed another film production agreement with Warner Bros., a leading American film investor, to produce a film which is expected to be completed between March and April 2003. The Directors believe that the collaboration with this film investor will reinvigorate the Chinese film market and open up new possibilities for the Group to penetrate into the global market.

Apart from the film production business, the Group has also engaged in the provision of TV movie and has signed a master production agreement with a TV movie company for the development and production of TV movies in PRC market. The Directors believe that the Group will benefit from the enormous business opportunities in PRC in the long run.

## UNAUDITED THIRD QUARTERLY RESULTS

The Board of Directors (the "Board") announces the unaudited condensed consolidated results of the Group for the periods of three months and nine months ended 31 December, 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 31 December,		(Unaudited) For the nine months ended 31 December,	
		2002 HK\$'000	2001 HK\$'000	2002 HK\$'000	2001 HK\$'000
<b>Turnover</b>	3	<b>14,500</b>	12,790	<b>33,075</b>	64,898
Film production costs		<b>(10,439)</b>	(11,833)	<b>(23,183)</b>	(56,209)
Gross profit		<b>4,061</b>	957	<b>9,892</b>	8,689
Other income		<b>135</b>	10	<b>557</b>	1,320
Administrative expenses		<b>(2,231)</b>	(901)	<b>(6,536)</b>	(1,876)
Other operating expenses		<b>(915)</b>	(252)	<b>(1,788)</b>	(949)
<b>Profit/(Loss) from operations</b>		<b>1,050</b>	(186)	<b>2,125</b>	7,184
Finance costs		–	–	–	(18)
<b>Profit/(Loss) before taxation</b>		<b>1,050</b>	(186)	<b>2,125</b>	7,166
Taxation	4	–	–	–	(410)
<b>Net profit/(loss) attributable to shareholders</b>		<b>1,050</b>	(186)	<b>2,125</b>	6,756
Dividend	5	–	2,208	–	2,208
Earnings/(Loss) per share	6				
(HK cents)					
Basic		<b>0.17</b>	(0.04)	<b>0.39</b>	1.42
Diluted		<b>0.16</b>	–	<b>0.38</b>	–

## NOTES TO THE FINANCIAL STATEMENTS

### 1. Group reorganization

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 and its shares have been listed on the GEM of the Stock Exchange on 26 August, 2002.

In order to facilitate the preparation for the listing of the Shares on GEM, the Group effected the reorganization, pursuant to which the Company became the ultimate holding company of the Group. Details of the reorganization are set out in the Prospectus dated 13 August, 2002 (the "Prospectus").

### 2. Basis of preparation and principal accounting policies

The unaudited condensed consolidated results have been prepared in accordance with accounting policies generally accepted in Hong Kong and the applicable disclosure requirements of the GEM Listing Rules.

The results of the Group for the nine months ended 31 December, 2002 and the corresponding period in the previous year have been prepared on a consolidated basis as if the current Group structure had been in existence.

The accounting policies and basis of preparations used in the preparation of the unaudited condensed consolidated results are consistent with those followed in the Accountants' Report as set out in the Prospectus.

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.



### 3. Turnover

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

### 4. Taxation

No provision for Hong Kong profits tax has been made as the Group had no estimated assessable profits for the three months and nine months ended 31 December, 2002 (Three months and nine months ended 31 December, 2001: Nil and HK\$410,000 respectively). Last year provision for Hong Kong profits tax have been made at the rate of 16% on the Group's estimated net assessable profit.

### 5. Dividend

The Board does not recommend the payment of an interim dividend for the nine months ended 31 December, 2002.

An interim dividend of HK\$220.80 per share was declared prior to the reorganisation and paid out on 29 November, 2001.

### 6. Earnings/(Loss) per share

The calculation of basic earnings per share for the three months and nine months ended 31 December, 2002 is based on the respective unaudited net profit from ordinary activities attributable to shareholders of approximately HK\$1,050,000 and HK\$2,125,000 (Three months and nine months ended 31 December, 2001: approximately (HK\$186,000) and HK\$6,756,000 respectively) and on weighted average number of Shares of 627,200,000 and 542,466,909 for the three months and nine months ended 31 December, 2002, respectively, taking into account that 476,000,000, 560,000,000 and 627,200,000 (Three months and nine months ended 31 December, 2001: 476,000,000) ordinary shares were in issue during the periods.

The calculation of diluted earnings per share for the three months and nine months ended 31 December, 2002 is based on the respective unaudited net profit from ordinary activities attributable to shareholders of approximately HK\$1,050,000 and HK\$2,125,000 (Three months and nine months ended 31 December, 2001: approximately (HK\$186,000) and HK\$6,756,000 respectively), and on weighted average number of Shares of 644,000,000 and 556,640,000 for the three months and nine months ended 31 December, 2002 respectively, taking into account that 476,000,000 and 644,000,000 (no diluted earnings per share for the three months and nine months ended 31 December, 2001) were in issue pursuant to the exercise of the options granted under the Pre-IPO Share Options Scheme.

#### 7. Movements of reserves

	<b>(Unaudited)</b>		<b>Retained earnings</b>	<b>Total</b>
	<b>Share capital</b>	<b>Share premium</b>		
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 1 April, 2001	–	–	(4,734)	(4,734)
Profit for the period	–	–	6,756	6,756
Dividends	–	–	(2,208)	(2,208)
At 31 December, 2001	–	–	(186)	(186)
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	–	–	2,125	2,125
At 31 December, 2002	6,272	11,387	2,849	20,508

## OTHER INFORMATION

### 1. DIRECTORS' INTERESTS IN EQUITY

As at 31 December, 2002, the interests of directors and their associates in the equity of the Company and any associated corporations as recorded in the register maintained by the Company under Section 29 of the Securities (Disclosure of Interests) Ordinance ("SDI Ordinance") are as follows:

#### Shares in the Company

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

Note: The shares are 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 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.

Save as disclosed above, none of the other Directors or their associates had, as at 31 December, 2002, any interests in the equity of the Company and any associated corporations as recorded in the register maintained under Section 29 of the SDI Ordinance which are required to be notified to the Company and the Stock Exchange.

### 2. SHARE OPTIONS SCHEMES

The Company has adopted two share option schemes on 2 August, 2002, namely, the Pre-IPO Share Option Scheme and the Share Option Scheme. The principal terms of which are set out in the sections headed "Pre-IPO Share Option Scheme" and "Share Option Scheme" in Appendix IV to the Prospectus.

A. *Pre-IPO Share Option Scheme*

As at 31 December, 2002, options to subscribe for an aggregate of 84,000,000 Shares of the Company had been granted to a senior management and six independent contractors. Details of which are as follow:

Name of grantees	Number of option granted	Date of grant	Exercise period	Exercise price HK\$	Number of options outstanding as at 31 December 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 31 December, 2002, 67,200,000 options out of 84,000,000 options granted were exercised.

As at 31 December, 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 31 December, 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.

*B. Share Option Scheme*

As at 31 December, 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:

<b>Name of shareholder</b>	<b>Number of Shares held</b>	<b>% of holding as at Listing Date</b>
Grand Sum Assets Limited (Note)	59,500,000	10.63

Note: Due to the exercise of options for 67,200,000 Shares of the Company under the Pre-IPO Share Option Scheme, the number of Shares of the Company issued as at 31 December, 2002 became 627,200,000. As such, Grand Sum Assets Limited only effectively held 9.49% shareholdings of the Company as at 31 December, 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 required to be disclosed by the Company pursuant to Section 16(1) of the SDI Ordinance as at 31 December, 2002.

#### 4. INITIAL MANAGEMENT SHAREHOLDERS

So far as the Directors are aware, as at 31 December, 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:

<b>Name of shareholder</b>	<b>Number of Shares held</b>	<b>% of holding as at Listing Date</b>
Pearl Rider Overseas Limited (Note)	285,600,000	51.00
Lau Tak Wah (Note)	59,500,000	10.63

Note: Due to the exercise of options for 67,200,000 Shares of the Company under the Pre-IPO Share Option Scheme, the number of Shares of the Company issued as at 31 December, 2002 became 627,200,000. As such, Pearl Rider Overseas Limited and Lau Tak Wah only effectively held 45.54% and 9.49% shareholdings of the Company respectively as at 31 December, 2002.

#### 5. SPONSOR'S INTEREST

Pursuant to a sponsor's agreement dated 12 August, 2002 between the Company and Hantec Capital Limited ("Hantec"), Hantec has agreed, for a fee, to act as the continuing sponsor of the Company as required under the GEM Listing Rules for the period from 26 August, 2002 to 31 March, 2005.

As notified to the Company by the Sponsor, as at 31 December, 2002, neither Hantec, its directors, employees nor their 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.

## 6. COMPETING INTERESTS

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 investor of the Group in order to further expand the Group’s film production and investment businesses. The Directors believe that competition may exist between the Group and Teamwork in the realm of the businesses of film production, investment and distribution. As at 31 December, 2002, Mr. Lau held effectively 9.49% of shareholdings in the Company after taking into account of the exercise of options for 67,200,000 shares of the Company under the Pre-IPO Share Option Scheme. 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 the following mechanisms and undertakings given by Mr. Lau would sufficiently safeguard the interests of the the Shareholders and the Company as a whole.

### *Film investment*

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.



*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.

*Film distribution*

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")*

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 also 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 films. 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 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. PURCHASE, SALE OR REDEMPTION OF LISTED SECURITIES**

During the nine months ended 31 December, 2002, neither the Company nor any of its subsidiaries had purchased, sold or redeemed any of the Company's listed shares.

**8. AUDIT COMMITTEE**

The Company has established an audit committee on 2 August, 2002 with written terms of reference in compliance with the GEM Listing Rules. 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 comprised two independent non-executive directors. The Group's unaudited results for the nine months ended 31 December, 2002 had been reviewed by the audit committee.

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

Hong Kong, 14 February, 2003