



**Xteam Software International Limited**  
**衝浪平台軟件國際有限公司**

*(Incorporated in the Cayman Islands with limited liability)*

**THIRD QUARTERLY RESULTS REPORT**  
**FOR THE NINE MONTHS ENDED**  
**31ST DECEMBER, 2003**

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

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

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*This report, for which the directors (“Directors”) of Xteam Software International Limited (the “Company”) collectively and individually accept responsibility, includes particulars given in compliance with the Rules Governing the Listing of Securities on the GEM of the Stock Exchange (the “GEM Listing Rules”) for the purpose of giving information with regard to the Company. 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.*

## **SUMMARY**

- The Group is one of the early movers in the development of the Chinese Linux operating system with kernel rewritten to specifically cater for Chinese users in the People's Republic of China ("PRC") and software based on the Linux operating platform for various hardware appliances. While its products support personal computer applications, the Group is also widely recognized for its efficient operating system that leads the server, Internet and Intranet markets. The Group also provides technical support and after-sales services to its customers.
- Turnover for the three months ended 31st December, 2003 amounted to approximately HK\$15,913,000, representing an increase of approximately 152% from approximately HK\$6,305,000 for the three months ended 30th September, 2003, and an increase of approximately 8.9% over the corresponding period in 2002 (2002: approximately HK\$14,606,000). Turnover for the nine months ended 31st December, 2003 amounted to approximately HK\$25,132,000 (2002: approximately HK\$30,110,000).
- Loss attributable to shareholders for the three month ended 31st December, 2003 narrowed to approximately HK\$2,860,000 compared to the loss attributable to shareholders for the three month ended 30th September, 2003 of approximately HK\$3,687,000. Loss attributable to shareholders for the nine months ended 31st December, 2003 amounted to approximately HK\$10,776,000 (2002: profit of approximately HK\$1,987,000).
- The Board does not recommend the payment of an interim dividend for the period (2002: Nil).

### THIRD QUARTERLY RESULTS FOR THE NINE MONTHS ENDED 31ST DECEMBER, 2003

The board of Directors (the “Board”) of the Company announces the unaudited results of the Company and its subsidiaries (collectively, the “Group”) for the three months and nine months ended 31st December, 2003, together with the unaudited comparative figures for the corresponding period in 2002, as follows:

	Note	Three months ended		Nine months ended	
		31st December, 2003 HK\$'000 (Unaudited)	2002 HK\$'000 (Unaudited)	31st December, 2003 HK\$'000 (Unaudited)	2002 HK\$'000 (Unaudited)
Revenue	2	15,913	14,606	25,132	30,110
Cost of sales		(12,949)	(10,049)	(20,853)	(12,964)
Gross profit		2,964	4,557	4,279	17,146
Other income/(expenses)		236	(47)	784	(47)
Operating expenses		(4,802)	(4,928)	(14,143)	(14,343)
(Loss)/profit from operations		(1,602)	(418)	(9,080)	2,756
Finance income/(cost), net		6	(16)	46	(141)
(Loss)/profit before tax		(1,596)	(434)	(9,034)	2,615
Income tax expense	3	(207)	-	(309)	-
(Loss)/profit after tax		(1,803)	(434)	(9,343)	2,615
Minority interests		(1,057)	(628)	(1,433)	(628)
(Loss)/profit attributable to shareholders		(2,860)	(1,062)	(10,776)	1,987
(Loss)/earnings per share	4				
- Basic (in cents)		(0.42)	(0.18)	(1.70)	0.35
- Diluted (in cents)		(0.41)	(0.18)	(1.69)	0.33
Dividend per share		Nil	Nil	Nil	Nil

Notes:

## 1. Basis of presentation

The unaudited interim financial statements have been prepared in accordance with Hong Kong Statement of Standard Accounting Practice (“SSAP”) No. 25 “Interim Financial Reporting”, issued by the Hong Kong Society of Accountants and Chapter 18 of Rules Governing the Listing of Securities on the Growth Enterprise Market of The Stock Exchange of Hong Kong Limited (the “GEM Listing Rules”).

The principal accounting policies and methods of computation used in the preparation of the unaudited third quarterly financial statements are consistent with those adopted in the latest annual financial statements of the Group.

## 2. Turnover and revenue

Turnover represents the invoiced value of goods sold and services rendered, net of value added tax and business tax in the PRC, and after allowances for goods returned and trade discounts.

## 3. Taxation

- (i) No provision for profits tax has been made as no income was earned or derived from Hong Kong during the period.
- (ii) No provision for profits tax has been provided in respect of the Cayman Islands or the British Virgin Islands as there were no assessable tax for the period in those jurisdictions. The tax expenses during the period represents tax charges on the assessable profits of certain subsidiaries operating in the PRC calculated at the applicable rates.
- (iii) No provision for deferred tax has been made as the Group had overall deferred tax benefits which will be recognized when realization of such benefits is assured beyond reasonable doubt.

## 4. (Loss)/earnings per share

The calculation of basic loss per share for the nine months and three months ended 31st December, 2003 is calculated based on the Group’s unaudited loss attributable to shareholders of approximately HK\$10,776,000 and HK\$2,860,000, respectively (2002: profits of approximately HK\$1,987,000 and loss of approximately HK\$1,062,000, respectively), and on the weighted average number of 633,269,902 shares and 688,399,242 shares, respectively, in issue during the period (2002: 568,402,108 shares and 577,377,910 shares, respectively).

The diluted loss per share for the nine months and three months ended 31st December, 2003 is based on the weighted average number of 638,547,389 shares and 698,073,970 shares, respectively, taking into account the options granted to certain directors, employees, advisers and consultants of the Company to subscribe for shares of the Company under the Pre-IPO Share Option Scheme and Share Option Scheme (2002: 610,002,108 shares and 586,876,277 shares, respectively).

## 5. Movements in reserves

	<b>Share premium account <i>HK\$'000</i></b>	<b>Accumulated losses <i>HK\$'000</i></b>	<b>Total <i>HK\$'000</i></b>
Consolidated (unaudited)			
At 1st April, 2002	36,248	(6,191)	30,057
Issue of new shares	21,714	-	21,714
Share issue expenses	(1,317)	-	(1,317)
Profit for the period	-	3,049	3,049
	<u>56,645</u>	<u>(3,142)</u>	<u>53,503</u>
At 31st December, 2002			
At 1st April, 2003	59,401	(16,780)	42,621
Issue of new shares	13,531	-	13,531
Share issue expenses	(1,111)	-	(1,111)
Profit for the period	-	(10,776)	(10,776)
	<u>71,821</u>	<u>(27,556)</u>	<u>44,265</u>
At 31st December, 2003			

## INTERIM DIVIDEND

The Board does not recommend the payment of an interim dividend for the period (2002: Nil).

## MANAGEMENT DISCUSSION AND ANALYSIS

### General

The Group is one of the early movers in the development of the Chinese Linux operating system with kernel rewritten to specifically cater for Chinese users in the PRC and software based on the Linux operating platform for various hardware appliances. While its products support personal computer applications, the Group is most widely recognized for its efficient operating system and its diversified software applications that leads the server, Internet, Intranet and mobile markets. The Group also provides technical support and after-sales services to its customers.

### Business review

During the first half of the year, the SARS outbreak was detrimental to the Group's activities. During the period under review, the SARS impact started to diminish and the sales of the Group recorded modest growth compared with the corresponding period of 2002 as business and marketing activities picked up gradually. The gross margin of products was squeezed to capture the market share. During the period under review, the Group adopted prudent cost control measures in its operations while maintaining its sales and marketing efforts.

In December 2003, the number of customers subscribing to the Group's Postal Server 6.0 exceeded the record high level of 10 million. The favourable market response to Postal Server 6.0 was boosted by the "2003 Editor's Choice Award in Postal Server" (2003年郵件服務器的編輯選擇獎) from Open Source World (開放系統世界), one of the leading IT publications in the PRC run by CCID. The award was in recognition of the Group's outstanding products and software specifically developed for the PRC market.

## **Prospects**

Starting from 1st January, 2004, the credit system would be introduced to all PRC technical institutions to replace the existing school year system. 5,000 state and provincial institutions out of a total of 30,000 existing technical institutions in the PRC will need the credit system educational software installation in the next 5 years. The Group is one of the few software companies endorsed by the Ministry of Education in provision of credit system educational software and will continue its headway to meet with the increasing demand of the software. This is in par with the State Council's policy to urge all government ministries to purchase only PRC-made software at their next upgrade cycle. These initiatives would help spur the development of local software firms. Local products based on Linux and other open-source software were expected to gain momentum.

The sustainable growth in the PRC economy and the government policies gave strong impetus to the development of local software firms. As one of the forerunners in the Chinese Linux operating system, the Group will strive to cement its leading position to benefit from the continued rapid development of the PRC software market.

## **FINANCIAL REVIEW**

The Group reported an unaudited, consolidated turnover of approximately HK\$15,913,000 for the three months ended 31st December, 2003, representing an increase of approximately 8.9% over the corresponding period in 2002 (2002: approximately HK\$14,606,000). The loss attributable to shareholders for the three months ended 31st December, 2003 was approximately HK\$2,860,000 (2002: approximately HK\$1,062,000).

The Group recorded a decrease in gross margin compared to the same period in last year, which was mainly due to keen competition in software market and the relatively low profit margin for certain profits.

The Group's operating expenses stood steadily at approximately HK\$4,802,000 (2002: approximately HK\$4,928,000) to maintain its sales and marketing activities to capture a larger market share.

## **SUBSEQUENT EVENTS**

On 9th February, 2004, the Company has requested the suspension of trading of the Company's shares on GEM pending for an announcement in relation to certain proposed transactions entered into by the Group on 10th February, 2004. As at the date hereof, the Company is in the process of compiling certain information for the aforesaid announcement. For further details of the said transactions, please refer to that announcement which is expected to be issued by the Company shortly.

## **CAPITAL STRUCTURE, EXPOSURE TO EXCHANGE RATES FLUCTUATION**

As at 31st December, 2003, the number of issued share capital of the Company was 693,007,938 (as at 31st March, 2003: 588,327,938).

On 23rd September, 2003, the Company entered into a placing agreement with Christfund Securities Limited to place 53,000,000 new ordinary shares of HK\$0.01 each in the share capital of the Company. On 3rd October, 2003, approval from the GEM Listing Committee for the listing of, and permission to deal in, the Placing Shares was obtained and the placing of the Placing Shares was completed on 8th October, 2003. Approximately HK\$3 million of the net proceeds from the placing will be used for product(s) development, mainly for educational use, approximately HK\$1 million will be used for advertising and marketing activities to promote the aforementioned new product(s) and the remaining of approximately HK\$4 million will be used as general working capital for daily operations.

As at 31st December, 2003 the Group held cash and cash equivalents denominated in Hong Kong Dollars and Renminbi.

Substantially all of the revenue-generating operations of the Group are transacted in Renminbi, which is not freely convertible into foreign currencies. The Group had prudent policy to manage currency and interest rate exposures, and as most of the Group's monetary assets and liabilities are denominated in Renminbi and Hong Kong Dollars, the exchange rate risks of the Group is considered minimal.



## DIRECTORS' AND CHIEF EXECUTIVES' INTERESTS OR SHORT POSITIONS IN THE SHARES AND UNDERLYING SHARES

As at 31st December, 2003, the interests or short positions of the Directors and chief executives of the Company in the shares and underlying shares of the Company or any of its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance (the "SFO")) which were required, pursuant to section 352 of the SFO, to be entered in the register referred to therein, or which were required, pursuant to Rules 5.40 to 5.58 of the GEM Listing Rules, to be notified to the Company and the Stock Exchange, were as follows:

### (1) Interests in shares

Name of directors	Number of shares of the Company			Total	% of issued share capital
	Personal interests	Family interests	Corporate interests		
Mr. Ma Gary					
Ming Fai ( <i>note 1</i> )	-	-	116,681,821	116,681,821	16.84%
Mr. Ren Yi ( <i>note 2</i> )	-	-	1,481,507	1,481,507	0.21%
Mr. Wu Meng Jie	6,219,962	-	-	-	0.90%

#### Notes:

- 1 These shares are held by Upwise Investments Ltd. and Princeton Venture Partners Limited. 74,821,349 shares are held by Upwise Investments Ltd. and the entire issued share capital of Upwise Investment Ltd. is beneficially owned by Mr. Ma Gary Ming Fai. 41,860,472 shares are held by Princeton Venture Partners Limited. Princeton Venture Partners Limited is wholly owned by PVP Limited. PVP Limited is in turn owned as to 43.56% by Innovative Group Ltd. Innovative Group Ltd. is in turn wholly owned by Mr. Ma Gary Ming Fai. Mr. Ma Gary Ming Fai is taken to be interested in 74,821,349 shares and 41,860,472 shares by virtue of his corporate interests in Upwise Investments Ltd. and Innovative Group Ltd. respectively.
- 2 The 1,481,507 shares are held by One Focus Group Limited, a company incorporated in the British Virgin Islands, the issued capital of which is beneficially owned by Mr. Ren Yi.

### (2) Interests in underlying shares

#### (a) Pre-IPO share options

Pursuant to the pre-IPO share option scheme (the "Pre-IPO Share Option Scheme") of the Company adopted on 30th May, 2001, the Directors and employees of the Group may be granted share options to subscribe for shares of the Company at an exercise price of HK\$0.266 each. All options have a duration of 10 years from the date of grant of the options and exercisable after three months from the date of listing of the Company on GEM on 11th December, 2001.

Details of the pre-IPO share options granted to certain Directors are as follows:

Name of Director	Date granted	Exercise period	No. of shares eligible for subscription under the pre-IPO share option	Exercise price per share
Mr. Ma Gary	14th November, 2001	11th June, 2002 to 13th November, 2011	50,000,000	HK\$0.266
Mr. Mak To Wai	14th November, 2001	11th June, 2002 to 13th November, 2011	30,000,000	HK\$0.266
			80,000,000	

Up to 31st December, 2003, no options under the Pre-IPO Share Option Scheme have been exercised.

*(b) Post-IPO share options*

On 21st November, 2001, the shareholders of the Company adopted a share option scheme (“Share Option Scheme”), the principal terms of which were set out on pages 199 to 208 of the Prospectus. Under the terms of the Share Option Scheme, the Board may, at their discretion, invite any full-time employees of the Group, including any executive and non-executive directors, and any advisers, consultants of or to any member of the Group to take up options to subscribe for shares in the Company.

On 19th December, 2003, 63,000,000 post-IPO share options were granted and accepted at an exercise price of HK\$0.14 per shares.

Details of the outstanding post-IPO share options granted to certain Directors are as follows:

Name of Director	Date granted	Exercise period	No. of shares eligible for subscription under the pre-IPO share option	Exercise price per share
Mr. Cheng Shu Wing	19th December, 2003	19th December, 2003 to 18th December, 2013	1,000,000	HK\$0.14
Mr. Wang Shi Yu	19th December, 2003	19th December, 2003 to 18th December, 2013	1,000,000	HK\$0.14
			2,000,000	

Up to 31st December, 2003, no options under the Share Option Scheme have been exercised.

Details of the 61,000,000 outstanding post-IPO share options granted to individuals other than Directors were set out in the sub-section headed “Post-IPO Share Option Scheme” under the section headed “Share Option Scheme”.

Save as disclosed above, as at 31st December, 2003, none of the Directors, chief executive of the Company and their associates had any personal, family, corporate or other interest or short positions in the shares and underlying shares of the Company or any of its associated corporations (within the meaning of Part XV of the SFO) which were required, pursuant to section 352 of the SFO, to be entered in the register referred to therein, or which were required, pursuant to Rules 5.40 to 5.58 of the GEM Listing Rules, to be notified to the Company and the Stock Exchange. During the reporting period, there were no debt securities issued by the Group.

#### **DIRECTORS’ AND CHIEF EXECUTIVES’ RIGHTS TO ACQUIRE SHARES OR DEBT SECURITIES**

Save as disclosed herein, and other than in connection with the Reorganization prior to the listing of the Company’s shares on GEM, as at the date hereof, neither the Company nor any of its subsidiaries was a party to any arrangements to enable the Directors and/or the chief executives of the Company to acquire benefits by means of the acquisition of shares in, or debt securities, including debentures, of the Company or any other body corporate, and none of the Directors, chief executives or their respective spouses or children under the age of 18 had any right to subscribe for the securities of the Company, or had exercised any such right.

## INTERESTS DISCLOSEABLE UNDER THE SFO AND SUBSTANTIAL SHAREHOLDERS

As at 31st December, 2003, the following persons (other than the Directors and chief executive of the Company) had interests or short position in the shares and underlying shares of the Company as recorded in the register required to be kept under Section 336 of the SFO and/or were directly or indirectly interested in 10% or more of the issued share capital carrying rights to vote in all circumstances at general meetings of any other members of the Group.:

Name	Number of shares	Percentage of issued share capital
Upwise Investments Ltd.	74,821,349 ( <i>note 1</i> )	10.80%
Princeton Venture Partners Limited	41,860,472 ( <i>note 2</i> )	6.04%
PVP Limited	41,860,472 ( <i>note 3</i> )	6.04%
Olympic Glory Limited	41,860,472 ( <i>note 4</i> )	6.04%
Omnicorp Limited	42,340,472 ( <i>note 5</i> )	6.11%
Innovative Group Ltd.	41,860,472 ( <i>note 6</i> )	6.04%
Positivism Securities Limited	33,173,133	4.79%

### Notes:

1. The entire issued share capital of Upwise Investments Ltd. is beneficially owned by Mr. Ma Gary Ming Fai, the Chairman of the Company.
2. Princeton Venture Partners Limited is wholly owned by PVP Limited. PVP Limited is in turn owned as to 43.56% by Innovative Group Ltd. and as to 37.22% by Olympic Glory Limited. Olympic Glory Limited is wholly owned by Omnicorp Limited (formerly Omnitech Group Limited), a company incorporated in Bermuda with limited liability and the securities of which are listed on the Main Board of the Exchange.
3. PVP Limited is deemed to be interested in 41,860,472 shares by virtue of its corporate interests in Princeton Venture Partners Limited.
4. Olympic Glory Limited is deemed to be interested in 41,860,472 shares by virtue of its corporate interests in PVP Limited.
5. Omnicorp Limited is deemed to be interested in 41,860,472 shares by virtue of its corporate interests in Olympic Glory Limited. 480,000 shares are held by Clever United Holdings Limited, which is wholly owned by Omnicorp Limited. Omnicorp Limited is deemed to be interested in 480,000 shares by virtue of its corporate interests in Clever United Holdings Limited.
6. Innovative Group Ltd. is deemed to be interested in 41,860,472 shares by virtue of its corporate interests in PVP Limited.

Save as disclosed above, as at 31st December, 2003, the Directors were not aware of any other person (other than the Directors and chief executive of the Company) who had an interest or short position in the shares and underlying shares of the Company as recorded in the register required to be kept under Section 336 of the SFO and/or were directly or indirectly interested in 10% or more of the issued share capital carrying rights to vote in all circumstances at general meetings of any other members of the Group.

## SHARE OPTIONS SCHEME

### (a) Pre-IPO Share Option Scheme

Details of the pre-IPO share options granted to Directors are set out in the sub-section headed “Interests in underlying shares” under the section headed “Directors’ and chief executives’ interests or short position in the shares and underlying shares”. There is no outstanding pre-IPO share options granted to other executives and full time employees as at 31st December, 2003.

### (b) Post-IPO Share Option Scheme

On 21st November, 2001, the shareholders of the Company adopted a share option scheme (“Share Option Scheme”), the principal terms of which were set out on pages 199 to 208 of the Prospectus. Under the terms of the Share Option Scheme, the Board may, at their discretion, invite any full-time employees of the Group, including any executive and non-executive directors, and any advisers, consultants of or to any member of the Group to take up options to subscribe for shares in the Company.

On 19th December, 2003, 63,000,000 post-IPO share options were granted and accepted at an exercise price of HK\$0.14 per shares.

Details of the outstanding post-IPO share options granted to are as follows:

Type of grantees	Date granted	Exercise period	No. of shares eligible for subscription under the post-IPO share option	Exercise price per share
Directors	19th December, 2003	19th December, 2003 to 18th December, 2013	2,000,000	HK\$0.14
Employees, advisers and consultants	19th December, 2003	19th December, 2003 to 18th December, 2013	61,000,000	HK\$0.14
			63,000,000	

Up to 31st December, 2003, no options under the Share Option Scheme have been exercised.

Details of the post-IPO share options granted to Directors are set out in the sub-section headed “Interests in underlying shares” under the section headed “Directors’ and chief executives’ interests or short position in the shares and underlying shares”.

## **PURCHASE, SALE OR REDEMPTION OF THE COMPANY’S LISTED SECURITIES**

During the nine months ended 31st December, 2003, 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 any interest in a business that competed or might compete with the business of the Group.

## **INTERESTS OF SPONSOR**

First Shanghai Securities Limited (“FSSL”) entered into a sponsor agreement (“Sponsor Agreement”) on 30th November 2001 with the Company whereby, for a fee, FSSL would act as the Company’s continuing sponsor for the purpose of Chapter 6 of the GEM Listing Rules for the period from 11th December, 2001 to 31st March, 2004.

FSSL has undergone a business rationalization with a view to having a better demarcation of various business units, including the segregation of corporate finance and securities trading business originally operated by it. As part of the rationalization, the corporate finance business and relevant staff of FSSL had been transferred to another fellow subsidiary, First Shanghai Capital Limited (“FSCL”), with effect from 16th January, 2002.

On 16th January, 2002, the Company agreed to novate with FSCL the rights and obligations under the Sponsor Agreement. As a result, FSCL will act as the continuing sponsor of the Company until 31st March, 2004.

None of FSCL, its directors, employees or associates had any interests in the securities of the Company or any member of the Group, or any right to subscribe for or to nominate persons to subscribe for the securities of the Company or any member of the Group as at 31st December, 2003.

## **AUDIT COMMITTEE**

As required by Rule 5.23 of the GEM Listing Rules, the Company has established an audit committee on 21st November, 2001 with written terms of reference which deal clearly with its authority and duties. The audit committee's principal duties are the review and supervision of the Company's financial reporting process and internal control systems. The audit committee comprises two independent non-executive Directors, namely Mr. Cheng Shu Wing and Mr. Wang Shi Yu. The Group's unaudited results have been reviewed by the two independent non-executive Directors of the Company.

## **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 since listed on GEM of the Stock Exchange.

By order of the Board  
**Xteam Software International Limited**  
**Mak To Wai**  
*Director*

Hong Kong, 12th February, 2004