

iMerchants Limited

Third Quarterly Report 2003-2004

iMerchants
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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 the 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.

Given the emerging nature of companies listed on GEM, there is a risk that securities traded on GEM may be more susceptible to high market volatility than securities traded on the Main Board and no assurance is given that there will be a liquid market in the securities traded on GEM.

The principal means of information dissemination on GEM is publication on the internet website operated by the Stock Exchange. Listed companies are not generally required to issue paid announcements in gazetted newspapers. Accordingly, prospective investors should note that they need to have access to the GEM website in order to obtain up-to-date information on GEM-listed issuers.

The Stock Exchange takes no responsibility for the contents of this report, makes no representation as to its accuracy or completeness and expressly disclaims any liability whatsoever for any loss howsoever arising from or in reliance upon the whole or any part of the contents of this report.

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

For the third quarter of the 2003/2004 financial year, the Group recorded a net profit of HK\$2,864,000. This is partly attributed to a healthy return of securities investments amid the recent positive performance of the global stock markets. Our wealth management system business line continues to grow and we are optimistic regarding its development in the coming year. Various cost-cutting and productivity enhancement measures have enabled the Group to significantly reduce administrative expenses from approximately HK\$38,810,000 to approximately HK\$19,621,000. For the nine months ended 31 December 2003, net loss of the Group decreased to approximately HK\$4,230,000 from approximately HK\$31,105,000 for the previous corresponding period.

The Group continues to see significant demand for wealth management products and we have been actively investing in enhancements to, and expansion of, our WealthSuite™ line of products through our wholly-owned subsidiary, Asia Financial Network Limited. Anticipating a growing demand for the product line, the Group has expanded its sales team both in Hong Kong and the mainland. A number of additional financial institution customers, including one in Beijing, had been signed up in the past quarter for our WealthSuite™ products.

The Group will also continue to enhance aggressively our product development capabilities, focusing on building top-class domain knowledge. The Group aims to provide value to our wealth management customers not just in information technology services but also active assistance in business process building and execution.

Regarding treasury management, the Group will continue to adopt prudent investment strategies with the assistance of professional international investment advisers. The Group continues to be in a strong and healthy financial position with adequate funds for future operations and expansion.

The start of the new year marked a positive change in the overall market sentiment and at iMerchants we believe we are well-positioned in knowledge, product direction, market positioning and financial strength to take advantage of the opportunities in 2004 and beyond.




FINANCIAL REVIEW

iMerchants' financial results for the nine months ended 31 December 2003 have combined the steady growth in operation performance with a significant investment performance of the Group.

For the first nine months of the 2003/04 financial year, the Group's unaudited consolidated turnover decreased to approximately HK\$3,355,000 from approximately HK\$6,096,000 for the corresponding period in 2002/03. The decrease was mainly due to the decision of the Group in late 2002 to shift away from development of customized projects and step into the development of WealthSuite™ standard products, which are tools helping banks, insurance companies, or other finance-related entities to promote their sales and better serve their customers in the wealth management arena. The Group believes in, and has already proven the existence of, significant market demand for wealth management solutions in the Greater China region, especially when bank deposit interest rates are relatively low. Due to the size and nature of the wealth management products, our sales team needs to spend a longer time to secure business orders. During the quarter ended 31 December 2003, a number of sales contracts - some with companies in Mainland China and Macau - were signed. As these products are undergoing certain customisations to suit the specific needs of the customers, only a small part of revenue for these sales have been recognised in the Group's financial results for the three months ended 31 December 2003. It is currently expected that the remaining revenue will be recognised in subsequent financial periods as the customisation for these products are gradually completed.

Though the Group's unaudited gross consolidated profit of the Group for the nine months ended 31 December 2003 decreased to approximately HK\$823,000 from approximately HK\$1,219,000 for the same period in the previous year, the gross profit margin improved slightly to approximately 24% from approximately 20%. The increase in gross profit margin is partially attributed to increased revenue from the Group's Client Support Services, which consist of mainly after-sales maintenance services provided to support customers' operation of the Group's customised products and which usually generate a healthy revenue margins for the Group.

During the period under review, the management has continued to take a prudent approach towards generating income from the Group's surplus funds by either placing deposits in interest-bearing bank accounts, investing directly in highly-rated bonds and blue-chip or large-cap equity stocks, or investing through experienced funds managers with proven track records. The income from investments and interest for the quarter ended 31 December 2003 was approximately



HK\$10,591,000 compared to approximately HK\$1,889,000 for the quarter ended 30 September 2003. The management will continue its prudent approach and will review its investment strategy frequently to take appropriate actions whenever necessary.

The administrative expenses had dropped by approximately 50% to approximately HK\$19,621,000 for the nine months ended 31 December 2003 from HK\$38,810,000 for the corresponding period in 2002. The management has set a lot of cost control measures which have proven to be quite effective. Moreover, as the costs of human resources represented the largest portion amongst the administrative expenses, the management had carefully studied how these resources could be utilized more effectively and efficiently. In late 2002, inevitable restructuring exercises were carried out for cost reduction and to ensure the best possible fit of the staff's skills with the Group's chosen focus for business in the future. As a result, the Group's administrative expenses have dropped significantly during this financial year compared with last year.

Overall, the Group's unaudited net consolidated loss for the nine months ended 31 December 2003 decreased substantially to approximately HK\$4,230,000 from approximately HK\$31,105,000 for the corresponding period in 2002. The Group continues to be in a healthy financial position, with current assets plus investments and time deposits totaling approximately HK\$220 million and without bank borrowings as at 31 December 2003.

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 nine months ended 31 December 2003 together with the comparative unaudited figures for the corresponding periods in 2002 as follows:

	<i>Notes</i>	Three months ended		Nine months ended	
		31 December		31 December	
		2003	2002	2003	2002
		<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Turnover	2	839	1,620	3,355	6,096
Cost of sales and direct costs		(474)	(1,012)	(2,532)	(4,877)
Gross profit		365	608	823	1,219
Other operating income		10,611	2,467	14,568	6,488
Administrative expenses		(8,112)	(11,609)	(19,621)	(38,812)
Profit/(loss) from operations	3	2,864	(8,534)	(4,230)	(31,105)
Taxation	4	–	–	–	–
Profit/(loss) for the period attributable to shareholders		2,864	(8,534)	(4,230)	(31,105)
Earnings/(loss) per share					
– basic and diluted	5	0.247 cent	(0.735) cent	(0.364) cent	(2.678) cent

Notes:

1. Basis of preparation of the financial statements

The financial statements have been prepared under the historical cost convention and in accordance with accounting principles generally accepted in Hong Kong.

2. Turnover

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.

3. Profit/(loss) from operations

Profit/(loss) from operations is arrived at after charging (crediting):

	Nine months ended	
	31 December	
	2003	2002
	HK\$'000	HK\$'000
Cost of inventories sold	–	903
Depreciation and amortisation	2,092	4,640
Bank interest income	(1,813)	(2,851)
Interest income from debt securities (net of amortization of premium of approximately HK\$416,000 (2002: approximately HK\$714,000))	(3,639)	(2,709)
Profit on disposal of trading securities	(713)	–
Increase in fair value of trading securities held at period end	(8,343)	–

4. Taxation

No provision for Hong Kong Profits Tax has been made in the financial statements as the Group incurred tax losses for both periods. No provision for taxation in other jurisdictions was made as the Group's subsidiaries operated outside Hong Kong had no assessable profits.

5. Earnings/(loss) per share

The calculation of the basic and diluted earnings/(loss) per share for the three months and the nine months ended 31 December 2003 is based on the profit of the Group of approximately HK\$2,864,000 (2002: loss of approximately HK\$8,534,000) and loss of approximately HK\$4,230,000 (2002: loss of approximately HK\$31,105,000), respectively, and on the weighted average number of ordinary shares of 1,161,382,000 (2002: 1,161,382,000).

The computation of diluted earnings/(loss) per share has not assumed the exercise of the Company's outstanding share options as their exercise prices were higher than the average market price of the Company's shares for both periods.

6. Interim dividend

The Directors do not recommend the payment of an interim dividend for the nine months ended 31 December 2003 (2002: Nil).

7. Movements of reserves

	Share premium <i>HK\$'000</i>	Negative goodwill <i>HK\$'000</i>	Capital redemption reserve <i>HK\$'000</i>	Merger reserve <i>HK\$'000</i>	Acc- umulated losses <i>HK\$'000</i>	Total <i>HK\$'000</i>
At 1 April 2002	207,130	1,884	409	45,918	(107,032)	148,309
Loss for the period	—	—	—	—	(31,105)	(31,105)
At 31 December 2002	<u>207,130</u>	<u>1,884</u>	<u>409</u>	<u>45,918</u>	<u>(138,137)</u>	<u>117,204</u>

	Share premium <i>HK\$'000</i>	Negative goodwill <i>HK\$'000</i>	Capital redemption reserve <i>HK\$'000</i>	Merger reserve <i>HK\$'000</i>	Acc- umulated losses <i>HK\$'000</i>	Total <i>HK\$'000</i>
At 1 April 2003	207,130	1,884	409	45,918	(143,522)	111,819
Loss for the period	—	—	—	—	(4,230)	(4,230)
At 31 December 2003	<u>207,130</u>	<u>1,884</u>	<u>409</u>	<u>45,918</u>	<u>(147,752)</u>	<u>107,589</u>

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

At no time during the nine months ended 31 December 2003 did the Company or its subsidiaries purchase, sell or redeem 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' AND CHIEF EXECUTIVES' INTEREST AND SHORT POSITIONS IN THE SHARES, UNDERLYING SHARES AND DEBENTURES

At 31 December 2003, the interests and short positions of the directors and chief executives in the shares, underlying shares and debentures of the Company and its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance (the "SFO")) as recorded in the register requires to be kept under Section 352 of the SFO or as otherwise notified to the Company and The Stock Exchange of Hong Kong Limited (the "Stock Exchange") pursuant to Rule 5.40 of the GEM Listing Rules were as follows:

Long positions in shares

Name of director	Number of ordinary shares in the Company held as			Total	Percentage of issued share capital
	personal interests	family interests	corporate interests		
Mr Leroy Kung Lin Yuen ("Mr Kung")	-	-	749,949,000 (Note i)	749,949,000	64.57%

Note:

- (i) The registered shareholder of 749,949,000 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 749,949,000 shares owned by iMerchants Group 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.

Long positions in underlying shares

Name of director	Date of grant	Options in the Company		Number of options
		Exercise price	Exercisable period	at 1 April 2003 and outstanding at 31 December 2003
Mr Edward Un ("Mr Un")	23 August 2000	HK\$0.53	In various stages from 31 March 2001 to 23 August 2010	2,000,000 (Note i)
	27 September 2002	HK\$0.172	In various stages from 1 September 2003 to 28 August 2012	8,000,000 (Note ii)

Notes:

- (i) 2,000,000 share options were granted on 23 August 2000 under the 2000 Share Option Scheme, which was approved by the written resolution of the shareholders of the Company dated 15 March 2000. Options pursuant to the 2000 Share Option Scheme may be exercised in accordance with the terms of the scheme as to:
- a. one quarter of the options would be exercisable from 1 April 2001 ("First Exercise Date");
 - b. an additional one eighth of the options would 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.
- (ii) 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. 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 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.



Long positions in debentures

No long positions of directors and chief executives in the debentures of the Company and its associated corporations were recorded in the register or as otherwise notified to the Company and the Stock Exchange pursuant to Rule 5.40 of the GEM Listing Rules.

Short positions in shares

No short positions of directors and chief executives in the shares of the Company and its associated corporations were recorded in the register or as otherwise notified to the Company and the Stock Exchange pursuant to Rule 5.40 of the GEM Listing Rules.

Short positions in underlying shares

No short positions of directors and chief executives in the underlying shares of the equity derivatives of the Company and its associated corporations were recorded in the register or as otherwise notified to the Company and the Stock Exchange pursuant to Rule 5.40 of the GEM Listing Rules.

Short positions in debentures

No short positions of directors and chief executives in the debentures of the Company and its associated corporations were recorded in the register or as otherwise notified to the Company and the Stock Exchange pursuant to Rule 5.40 of the GEM Listing Rules.

Save as disclosed above, as at 31 December 2003, none of the directors and chief executives had interest in any shares, underlying shares and debentures of the Company and its associated corporations (within the meaning of Part XV of the SFO) as recorded in the register requires to be kept under Section 352 of the SFO or as otherwise notified to the Company and the Stock Exchange pursuant to Rule 5.40 of the GEM Listing Rules.

INTEREST DISCLOSEABLE UNDER THE SFO AND SUBSTANTIAL SHAREHOLDERS

At 31 December 2003, the following persons (other than the directors and chief executive of the Company) had interests and short positions in the shares and underlying shares of the Company as recorded in the register required to be kept under Section 336 of the SFO.

Long positions in shares

Name	Capacity	Nature of interest	Number of ordinary shares	Percentage of issued share capital
Reuters Greenhouse Fund LP <i>(Note i)</i>	Beneficial owner	Corporate	58,125,000	5.00%
Reuters Group PLC <i>(Note i)</i>	Interest of a controlled corporation	Corporate	58,125,000	5.00%

Note:

- (i) Reuters Greenhouse Fund LP is a wholly owned subsidiary of Reuters Group PLC.

Long positions in underlying shares

No long positions of other persons and substantial shareholders in the underlying shares of equity derivatives of the Company were recorded in the register.

Short positions in shares

No short positions of other persons and substantial shareholders in the shares of the Company were recorded in the register.

Short positions in underlying shares

No short positions of other persons and substantial shareholders in the underlying shares of equity derivatives of the Company were recorded in the register.

Save as disclosed above, as at 31 December 2003, the directors were not aware of any other person who had an interest or short position in the shares or underlying shares of the Company as recorded in the register required to be kept under Section 336 of the SFO.



DIRECTORS' RIGHTS TO ACQUIRE SHARES OR DEBENTURES

Other than the share option schemes as described in the section headed "DIRECTORS' AND CHIEF EXECUTIVES' INTEREST AND SHORT POSITIONS IN THE SHARES, UNDERLYING SHARES AND DEBENTURES" 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 31 December 2003, other than the interests disclosed in the section headed "DIRECTORS' AND CHIEF EXECUTIVES' INTEREST AND SHORT POSITIONS IN THE SHARES, UNDERLYING SHARES AND DEBENTURES" above, the Company has not been notified of any other interests at 31 December 2003 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 nine months ended 31 December 2003.

By order of the Board
Leroy Kung Lin Yuen
Chairman

Hong Kong, 13 February 2004