



WAFER SYSTEMS

# Wafer Systems Limited

(Incorporated in the Cayman Islands with limited liability)

# Next Generation Network

Annual Report  
2003

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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 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 Exchange. GEM-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 at [www.hkgem.com](http://www.hkgem.com) 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 the Company (“Director(s)”) 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 (“GEM Listing Rules”) for the purpose of giving information with regard to the Company. The Directors, having made all responsible enquiries, confirm that, to the best of their knowledge and belief: (i) the information contained in this report is accurate and complete in all material respects and not misleading; (ii) there are no other matters the omission of which would make any statement in this report misleading; and (iii) all opinions expressed in this report have been arrived at after due and careful consideration and are founded on bases and assumptions that are fair and reasonable.*

# Contents

<b>2</b>	Corporate Information
<b>4</b>	Chairman's Statement
<b>8</b>	Comparison of Business Objectives with Actual Business Progress
<b>11</b>	Biographical Details of Directors and Senior Management
<b>13</b>	Management Discussion and Analysis
<b>16</b>	Directors' Report
<b>27</b>	Auditors' Report
<b>28</b>	Consolidated Income Statement
<b>29</b>	Consolidated Balance Sheet
<b>30</b>	Balance Sheet
<b>31</b>	Consolidated Statement of Changes in Equity
<b>32</b>	Consolidated Cash Flow Statement
<b>34</b>	Notes to Financial Statements
<b>58</b>	Financial Summary
<b>59</b>	Notice of Annual General Meeting

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## CORPORATE INFORMATION

### BOARD OF DIRECTORS

#### Executive Director

Mr. Chan Sek Keung, Ringo  
(Chairman & Chief Executive Officer)

#### Non-Executive Directors

Mr. Alasdair Gordon Nagle  
Ms. Clara Ho  
Mr. Kwan Kit Tong

#### Independent Non-Executive Directors

Mr. Pang Hing Chung, Alfred  
Mr. Tsoi Tai Wai, David

### COMPANY SECRETARY

Mr. Pang Kin Man, Edmond

### QUALIFIED ACCOUNTANT

Mr. Yau Kin Wa

### COMPLIANCE OFFICER

Mr. Chan Sek Keung, Ringo

### AUDIT COMMITTEE

Mr. Tsoi Tai Wai, David (Chairman)  
Mr. Pang Hing Chung, Alfred  
Mr. Chan Sek Keung, Ringo

### ADVISORS

Mr. Chen Sau Chung, John  
Mr. Samuel Lin Jr.

### AUTHORIZED REPRESENTATIVES

Mr. Chan Sek Keung, Ringo  
Mr. Pang Kin Man, Edmond

### REGISTERED OFFICE

4th Floor, Scotia Centre  
P.O. Box 2804  
George Town  
Grand Cayman  
Cayman Islands

### HEAD OFFICE AND PRINCIPAL PLACE OF BUSINESS

Units 901-7, 9th Floor  
MLC Millennia Plaza  
663 King's Road  
North Point  
Hong Kong

### PRINCIPAL SHARE REGISTRAR AND TRANSFER OFFICE

Bank of Butterfield International (Cayman) Limited  
Butterfield House  
68 Fort Street  
P.O. Box 705  
George Town  
Grand Cayman  
Cayman Islands

### HONG KONG BRANCH SHARE REGISTRAR AND TRANSFER OFFICE

Computershare Hong Kong Investor Services Limited  
Shops 1712-1716, 17th Floor  
Hopewell Centre  
183 Queen's Road East  
Hong Kong

### PRINCIPAL BANKERS

The Hongkong & Shanghai Banking  
Corporation Limited  
HSBC Main Building  
1 Queen's Road Central  
Hong Kong

Jian Sing Bank Limited  
41st Floor Tower 1  
Lippo Centre  
89 Queensway  
Hong Kong

Dah Sing Bank Limited  
36th Floor, Dah Sing Financial Centre  
108 Gloucester Road  
Wanchai  
Hong Kong

## **CORPORATE INFORMATION**

### **AUDITORS**

Deloitte Touche Tohmatsu  
Certified Public Accountants  
26th Floor, Wing On Centre  
111 Connaught Road Central  
Hong Kong

### **LEGAL ADVISORS**

Woo, Kwan, Lee & Lo  
27th Floor, Jardine House  
1 Connaught Place  
Hong Kong

### **SPONSOR**

CSC Asia Limited  
Units 3204-07, 32nd Floor  
COSCO Tower  
Grand Millennium Plaza  
183 Queen's Road Central  
Hong Kong

### **WEBSITE ADDRESS**

[www.wafersystems.com](http://www.wafersystems.com)

### **STOCK CODE**

8198

## CHAIRMAN'S STATEMENT

### TO OUR SHAREHOLDERS

For and on behalf of the board of Directors (the "Board"), I am pleased to present the annual report of Wafer Systems Limited (the "Company") and its subsidiaries (collectively, "Wafer Systems" or the "Group") for the year ended 31 December 2003 (the "Review Period").

During 2003, challenges and opportunities co-existed in the markets where Wafer Systems operates. The economy was hit hard by the SARS epidemic from April to June of 2003 in the Greater China region, hampering the pace of recovery in the network infrastructure industry. With the effective measures taken by governments, the situation improved in the second half of the year. The capricious market sentiment however did not deter Wafer Systems from pursuing our business growth. On the contrary, we used the opportunity to implement a series of cost-effective operation controls, at the same time investing in our research and development capabilities of our Next Generation Network ("NGN") business. Additionally, we are also reaching out to potential multinational corporations ("MNCs") and telecommunication clients. Our management team also successfully demonstrated our efficacy, consolidating our established foundations and bringing in consistent improvements in our operational and financial results.

Wafer Systems marked several highlights in 2003. First of all, the Group saw a turn around to profit. Secondly, the Group gained recognition as a pioneer in Next Generation Network ("NGN") while at the same time establishing a comprehensive portfolio of NGN offerings. Thirdly, the MNC business experienced healthy organic growth. Fourthly, the Group secured a strategic partnership with the China division of Cisco Systems Inc. ("Cisco") in the service provider sector ("SP") and developed good working relations with their Asia Pacific research and development team.

China's economy is growing rapidly and recent economic data indicate that Hong Kong is also on the road to recovery. This, and increasing economic vitality will provide the springboard for major leaps in our future business. Wafer Systems will continue to pursue growth in the future.

### FINANCIAL PERFORMANCE

#### Highlights

	2003	2002	Change
Turnover (HK\$'000)	<b>165,879</b>	180,333	-8%
Profit (Loss) from operations (HK\$'000)	<b>4,349</b>	(4,214)	-
Net Profit (Loss) (HK\$'000)	<b>857</b>	(5,849)	-
Basic Earnings (Loss) per share (HK cents)	<b>0.30</b>	(2.40)	-
Net Cash from/(used in) operations (HK\$'000)	<b>34,844</b>	(32,624)	-
Cash/Debt Ratio	<b>0.64</b>	0.13	+392%
Current Ratio	<b>1.67</b>	1.53	+9%
Quick Ratio	<b>1.52</b>	1.30	+17%
Debt Ratio (Debts/Assets)	<b>0.56</b>	0.68	-18%



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## CHAIRMAN'S STATEMENT

For the year ended 31 December 2003, the Group recorded a healthy shift in the financial results. During the year, we adjusted our business strategy and allocated more resources to the Group's business in Professional Services and Network Software. Although the move led to an overall decline of approximately 8.0% in turnover to approximately HK\$165.9 million, the overall segmental results improved significantly over those of 2002. The Group recorded a net profit attributable to shareholders of approximately HK\$857,000 during 2003 compared with a loss of approximately HK\$5.8 million recorded in the year ended 31 December 2002.

Mainland China continued to be the Group's major revenue source, accounting for approximately 88.5% of the Group's total turnover while the remaining portion of approximately 11.5% came from Hong Kong. During 2003, the Network Infrastructure business continued as the Group's main revenue contributor, with a turnover of approximately HK\$135.8 million. However, its contribution to the Group is gradually decreasing, and accounted for approximately 81.9% of the Group's turnover in 2003. (2002: 85.2%). The Professional Services and Network Software businesses developed rapidly during the year. The turnover generated from the Professional Services business increased by approximately 7.3% to reach approximately HK\$28.2 million (2002: HK\$26.3 million), while the turnover from the Network Software business surged approximately 4.2 times to approximately HK\$1.9 million (2002: approximately HK\$357,000). With the increasing demand for NGN and the Group's successful penetration into the MNC market and leading Mainland China corporations, Professional Services and Network Software businesses are expected to contribute an even larger share to both the Group's turnover and profit in the future.

The Group continued to improve its financial resources and liquidity over the past twelve months. As at 31 December 2003, the Group had bank balances and cash totaling approximately HK\$45.2 million (2002: HK\$14.4 million). Total banking facilities was approximately HK\$67.0 million (2002: HK\$102.2 million), of which approximately HK\$43.0 million (2002: HK\$59.4 million) had been utilized.

### FINAL DIVIDEND

The Board of Directors do not recommenced the payment of any dividend for the year ended 31 December 2003 (2002: Nil).

### BUSINESS REVIEW

During 2003, the Group's Network Infrastructure business successfully entered a new stage of development. The emergence of NGN has generated tremendous business opportunities for the Group. As a pioneer in the NGN business, the Group experienced strong growth in this area during the year. In partnership with Cisco Systems Inc. ("Cisco"), the Group finalized the 2nd phase of the NGN-related infrastructure project for a well-known telecommunications services provider in Sichuan Province in the PRC. With the successful commercialization of the project, we strengthened our position as a pioneer and leader in the market, enabling us to better grasp the buoyant business opportunities arising in the PRC market ahead.

Building on our extensive experience in the implementation of network infrastructure for the telecommunications industry, the Group is committed to help telecommunications services provider integrate 2.5G and CDMA telephone networks with the Internet. Currently such projects cover seven provinces and cities including Gansu, Guangxi, Guangdong, Hunan, Jilin, Xinjiang and Shenzhen in the PRC. Additionally, the Group secured a project of over HK\$40 million to help Motorola Inc. integrate its mobile telephone network installed for their customers in China with the Internet, further demonstrating the Group's niche in the telecommunications sector.

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## CHAIRMAN'S STATEMENT

Over the past year, the Group continued to provide unique services to existing clients and at the same time successfully broadened its client base.. In China, they include China Netcom Corporation Ltd., Sony (China) Ltd., Samsung Networkes (Beijing) Co. Ltd., Industrial and Commercial Bank and China Wuling General Motors Co. Ltd.; and in Hong Kong New World PCS Ltd. and Galaxy Satellite Broadcasting Ltd..

Wafer Systems also possesses strong competitive advantages in network optimization & solutions. During the Review Period, the Group's sales of security solution projects reached HK\$7 million. Large-scale organizations such as the Hospital Authority, the Information Technology Services Department, the Vocational Training Council and Hutchison Global Centre Limited in Hong Kong; and China International Capital Corporation Ltd., IBM and China AT&T in the PRC demonstrated their confidence in the Group by adopting the Group's sophisticated solutions. These contracts further strengthen the Group's leading position in providing network optimization and security related solutions.

The Group's Professional Services business continues to gain momentum. The steady growth of this business has been mainly fueled by MNCs and domestic enterprises, which were gradually recovering as the spectre of SARS was removed. The Group won contracts from leading enterprises such as Dow Chemicals, Sun Microcomputer Systems, Industrial and Commercial Bank of China and China Unicom, to provide our expert services during 2003.

During the year, EMC Corporation, the world leader in information storage systems, software, networks, and services, appointed Wafer Systems as one of its Distribution Global Partner. This partnership has successfully enhanced our ability to deliver top quality and comprehensive solutions and services to our extensive client base, in particular, the banking and telecommunications sectors.

Benefiting from the state-of-the-art and self-developed NextG IP Billing software, the Group's Software business enjoyed substantial growth during the year. The NextG IP Billing software continues to receive favorable responses in the Greater China region, Canada, as well as Japan. As Wafer Systems possesses strong expertise in developing sophisticated software, which can also be applicable to clients with NGN projects, the synergies generated from the Group's core businesses enable the Group to further strengthen our market foothold.

Wafer Systems has also been invited to become Cisco's partner in its Service Provider Solutions Ecosystem ("SPSE") program. This program is offered to companies whose products and solutions exhibit market leadership with the use of Cisco's industry-leading technology while sharing in Cisco's commitment to customer service and satisfaction. Wafer Systems is the first Cisco partner in Hong Kong and China to receive this recognition under the solution category "Voice/Packet Telephony Application". This demonstrates just how widely the Group's capabilities in the research and development for NGN software and solutions are recognized by Cisco.

### PROSPECTS

Entering 2004, improvements in general economic conditions are continuing in the PRC and Hong Kong market. At the same time, the Chinese government is aggressively promoting the adoption of information technology in prosperous cities. These factors indicate that the industry is recovering. Reinforcing our capabilities in the three synergistic businesses plus the advantage as a pioneer in the NGN business, Wafer Systems is ideally poised to capture these opportunities ahead.



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## CHAIRMAN'S STATEMENT

With years of experience behind us at Wafer Systems, we have successfully shaped ourselves into a leading provider of Network Infrastructure, Professional Services and Network Software to telecommunications service providers and MNCs in Mainland China and Hong Kong. The Group is further recognized as a forerunner in the NGN industry and has established a reputation as a role model in the provision of sophisticated technologies and services for our clients.

Anticipating that NGN will become a major market driver, Wafer System, as a market pioneer, has developed a suite of NGN management software and formed a close alliance with Cisco's research and development team. Wafer Systems now enjoys advantages as a pioneer in introducing advanced NGN products and technologies to prestigious telecommunications clients.

To further enhance our competitiveness and capture higher profit margins, the Group will fully utilize our research and development capabilities in Xi'an and leverage our skills in network communication to focus on the design and development of software such as business support system ("BSS"), operation support system ("OSS") and soft switch system ("BTS"), and network security solutions for launch in the coming years.

The Group will also place additional effort into the further penetration of both the MNC and telecommunication markets, using our competitive cost structure as well as our fully integrated NGN capability as competitive advantages. Additionally, we will take steps to differentiate and penetrate new market segments and gain leading positions in specific industries, such as distinguished multinational enterprises and in the automobile industry in China.

We will concentrate our efforts and resources on factors and innovations that differentiate our products and services. Maintaining this focus, we will continue to thrive and generate increasing benefits for our customers and shareholders.

## CONCLUSION

In conclusion, I would like to thank our customers, suppliers, bankers, investors, business partners and advisers for their continued trust and support. I would also like to extend my thanks to all our staff for their hard work and major contribution to the Group's performance last year. We will continue to pursue growth into the future, bringing in better returns for our shareholders.

**CHAN Sek Keung, Ringo**

*Chairman and Chief Executive Officer*

Hong Kong, 25 March 2004

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## COMPARISON OF BUSINESS OBJECTIVES WITH ACTUAL BUSINESS PROGRESS

The following is a comparison of actual business progress in 2003 with the business objectives for the same period as set out in the prospectus of the Company dated 10 May 2002 (the "Prospectus"). The Group reviews its business objectives and strategies on an ongoing basis and makes adjustments as necessary.

### **Business Objectives for the Review Period as set out in the Prospectus**

### **Actual Business Progress in the Review Period**

#### **Business Development**

Establish two additional sales and marketing presences in mainland China, including one in Nanjing.

The one in Nanjing was established in March 2003.

The Group decided to defer the addition of the other marketing presence and consolidated marketing efforts on existing ones which produced good results.

Commence the operations of a subsidiary or an office of the Group in Taiwan.

The plan was deferred due to the uncertain political and economic environment in the region.

#### **Product Development and Service Launches**

##### **Network Infrastructure**

Complete, launch and promote phase 3 and the latest version of IP Multimedia Collaboration Solutions.

The Group has completed phase 3 of Navipresenter, the IP Multimedia Collaboration Solutions, and launched the product in July 2003.

With such successes, the Group has combined such promotion in co-operation with the NGN offerings at the later part of 2003.

Further increase its market share by promoting Infrastructure Solutions and Network Security Solutions, as well as Multimedia Solutions by adopting self-developed software and integrating with video conferencing equipment supplied by third parties.

The Group successfully increased its revenue generated from the Network Infrastructure business, especially for its network optimization and security solutions businesses as compared with 2002.

Further, the Company has developed NGN management solutions to enable the Company to stay at a leading position in the supply of converged multi-media solutions to customers.

Further enhance the joint research and development with New Eracom of IP Multimedia Collaboration Solutions.

The Group stopped the co-operation with New Eracom. Instead, the Group has been working with several other partners on IP Multimedia Collaboration Solutions in order to satisfy the broader needs of such solutions on the NGN platform.

## COMPARISON OF BUSINESS OBJECTIVES WITH ACTUAL BUSINESS PROGRESS

### Business Objectives for the Review Period as set out in the Prospectus

#### *Professional Services*

Further increase its market share by promoting Customer Services, Expert Services and Outsourcing Services.

#### *Network Software*

Complete the research and development and launch phase 2 and phase 3 of the Network Management Software.

Further increase its market share by promoting the latest version of the NextG IP Billing Software.

Continue and further enhance the research and development of the NextG IP Billing Software, the Network Management Software, and the OSS/BSS Software.

Complete and launch the 2nd version of OSS/BSS Software.

Commence the research and development of the 3rd version of OSS/BSS Software.

Complete the research and development of and launch the 3rd version of the OSS/BSS Software.

### Actual Business Progress in the Review Period

Revenue from this business segment continued to increase though at a slower pace after the big increase experienced during the first 6 months in 2003.

The Group completed the research, development and launch of both phase 2 and phase 3 of the Network Management Software.

Further, foreseeing the advent of the NGN, the Group has consolidated the various OSS/BSS Network Management and IP Billing software to a suite of NGN management software, which supports network management and billing of converged voice, video and data networks.

The Group has recorded a steady growth in Network Software revenues and successfully signed contracts with several telecommunications providers in Canada and Japan.

The Group has consolidated the various OSS/BSS Network Management and IP Billing software to a suite of NGN management software, which supports network management and billing of converged voice, video and data networks.

The Group completed and launched the 2nd version of OSS/BSS Software.

The Group also commenced the research and development of the 3rd version of OSS/BSS Software up to the middle of 2003.

Foreseeing the advent of the NGN, the Group has consolidated the various OSS/BSS Network Management and IP Billing software to a suite of NGN management software, which supports network management and billing of converged voice, video and data networks.

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## COMPARISON OF BUSINESS OBJECTIVES WITH ACTUAL BUSINESS PROGRESS

### **Business Objectives for the Review Period as set out in the Prospectus**

### **Actual Business Progress in the Review Period**

#### ***Sales and Marketing***

Promote self-developed software in Taiwan and further enhance the sales network in Greater China and Southeast Asia.

This was deferred due to the uncertain political and economic environment in the region.

Further enhance the sales network in the PRC and the Southeast Asia region.

With business focus in Mainland China and Hong Kong, the Group has maintained its presence in other Southeast Asian counties in co-marketing exercises with various vendors.

Increase efforts in brand building of the Group for its three business segments through comprehensive marketing campaigns in Mainland China.

The Group's increased efforts on brand building helped produce better overall results.

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## BIOGRAPHICAL DETAILS OF DIRECTORS AND SENIOR MANAGEMENT

### EXECUTIVE DIRECTOR

**Mr. Chan Sek Keung**, Ringo, aged 44, is the founder, the chief executive officer and the executive Director of the Company. Mr. Chan founded the Group in November 1998 and is responsible for the overall management, strategic planning and development of the Group. Mr. Chan has over 20 years of working experience in the data and network communication industry. Mr. Chan holds a Bachelor's degree in Electrical Engineering from the University of Hong Kong.

### NON-EXECUTIVE DIRECTORS

**Mr. Alasdair Gordon Nagle**, aged 41, is a non-executive Director. Mr. Nagle joined the group in March 1999. He is a director of HSBC Private Equity Technology (Asia) Limited, which is a wholly-owned subsidiary of HSBC Private Equity (Asia) Limited, and is a nominee of The Applied Research Council ("ARC") on the Board. Mr. Nagle is a member of the Institute of Chartered Accountants in England & Wales and holds a Master of Arts degree in French and Business Studies from Edinburgh University.

**Ms. Clara Ho**, aged 32, is a non-executive Director. Ms. Ho joined the Group in May 2001. Ms. Ho is an associate director of HSBC Private Equity (Asia) Limited and is a nominee of ARC on the Board. Ms. Ho holds a Bachelor's degree in Economics and Accounting from the University of Bristol and is a member of the Institute of Chartered Accountants in England & Wales.

**Mr. Kwan Kit Tong**, aged 45, is a non-executive Director. Mr. Kwan joined the Group in May 2001. He is the financial controller of QPL International Holdings Limited ("QPL") and the nominee of QPL on the Board. Mr. Kwan holds a Bachelor's degree in Commerce from the University of Southern Queensland and also holds fellow membership of the Chartered Association of Certified Accountants and the Hong Kong Society of Accountants.

### INDEPENDENT NON-EXECUTIVE DIRECTORS

**Mr. Pang Hing Chung, Alfred**, aged 42, is an independent non-executive Director. Mr. Pang was appointed as an independent non-executive Director of the Company in March 1999. Mr. Pang is a Managing Director and Vice Chairman of the Investment Banking Division of BOC International. Mr. Pang holds an MBA degree from the Stanford Graduate School of Business and also a Bachelor of Arts degree in Economics from Cornell University.

**Mr. Tsoi Tai Wai, David**, aged 56, is an independent non-executive Director. Mr. Tsoi was appointed as an independent non-executive Director of the Company in October 2001. Mr. Tsoi is a Certified Public Accountant by profession, and he is currently the managing director of Alliot Tsoi Ha CPA Limited. Mr. Tsoi holds a Master's degree in Business Administration from the University of East Asia, Macau and also holds fellow membership of the Chartered Association of Certified Accountants, the Hong Kong Society of Accountants and associate membership of the Association of Certified General Accountants.

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## BIOGRAPHICAL DETAILS OF DIRECTORS AND SENIOR MANAGEMENT

### SENIOR MANAGEMENT

**Ms. Wang Fang**, aged 35, is the vice president of the Group. Ms. Wang joined the Group in June 2001 and is responsible for the Group's overall operations, financial performance as well as sales and marketing activities in mainland China. Ms. Wang graduated from the Faculty of Telecommunications Engineering of the Nanjing Post and Telecom University in China and also holds an International MBA degree from Peking University.

**Mr. Pang Kin Man, Edmond**, aged 56, is the company secretary of the Company. Mr. Pang has more than 30 years of working experience. Mr. Pang holds an associate membership of the Institute of Chartered Secretaries and Administrators and the Hong Kong Institute of Company Secretaries. Mr. Pang joined the Group in August 2001.

**Mr. Yau Kin Wa**, aged 35, is the qualified accountant and finance manager of the Group, Mr. Yau is a Fellow member of the Association of Chartered Certified Accountants and an Associate member of the Hong Kong Society of Accountants. Mr. Yau joined the Group in June 1999.

**Mr. Sha Sue Wen, Jack**, aged 34, is the head of research and development of the Group. Mr. Sha holds a Bachelor's degree in Applied Mathematics from Northwest Polytechnic University in Xi'an, China. Mr. Sha joined the Group in June 1999.

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## MANAGEMENT DISCUSSION AND ANALYSIS

### LIQUIDITY, FINANCIAL RESOURCES AND CAPITAL STRUCTURE

During the Review Period, the Group maintained conservative policies in cash and financial management. Surplus funds were placed on interest-bearing deposits with banks. The Group generally financed its operations and serviced its debts with its internal resources, short-term bank loans and convertible bonds.

The financial and liquidity position of the Group remained healthy during the Review Period. As at 31 December 2003, the Group had net current assets of approximately HK\$45.7 million (2002: HK\$53.1 million), including bank balances and cash of approximately HK\$45.2 million (2002: HK\$14.4 million), total short term bank loans of approximately HK\$33.1 million (2002: HK\$41.1 million) and convertible bonds maturing within one year of approximately HK\$9.3 million (2002: HK\$7.4 million). The Group's current ratio improved from approximately 1.53 as at 31 December 2002 to approximately 1.67 as at 31 December 2003. In addition, the Group's non-current liabilities reduced by approximately 75% from approximately HK\$11.3 million as at 31 December 2002 to approximately HK\$2.8 million as at 31 December 2003.

During the Review Period, the Company issued 7,676,745 new ordinary shares at the par value of HK\$0.01 each for cash to QPL International Holdings Limited ("QPL") on its exercise of the warrants granted. This allotment increased the total number of issued shares of the Company to 289,944,745 shares and total issued share capital to approximately HK\$2.9 million.

As at 31 December 2003, all assets and liabilities of the Group were denominated in U.S. dollars, Hong Kong dollars and Renminbi.

### ORDER BOOK AND PROSPECTS OF NEW BUSINESS

As at 31 December 2003, the Group had contracts on hand for sales amounting to approximately HK\$28.1 million (2002: HK\$35.5 million) which would be booked as revenue upon delivery and implementation.

While closely tracking the development of the NGN and its business opportunities, the Group will continue to concentrate on its present core business segments.

### SIGNIFICANT INVESTMENT HELD

The Group had not made any significant investment since floatation or during the Review Period.

### SEGMENTAL INFORMATION

The segmental information of the Group is covered in paragraph 2 of Financial Performance under the Chairman's Statement and in note 4 to the financial statements.



## **MANAGEMENT DISCUSSION AND ANALYSIS**

### **CHARGES ON GROUP ASSETS**

As at 31 December 2003, the Group did not have any significant charges on assets.

As at 31 December 2002, the Group had general banking facilities of approximately HK\$102.2 million which were secured by pledged bank deposits of approximately HK\$18.4 million.

### **GEARING RATIO**

As at 31 December 2003, the gearing ratio, i.e. non-current liabilities over total assets, reduced to approximately 2.2% from approximately 6.8% as at 31 December 2002. The improvement was mainly due to significant reduction of non-current liabilities during the Review Period.

### **FOREIGN EXCHANGE EXPOSURE**

During the Review Period, the Group earned revenue and incurred costs and expenses mainly in U.S. dollars, Hong Kong dollars and Renminbi. As the exchange rates of such currencies have been stable, no hedging or other alternatives have been implemented.

### **CONTINGENT LIABILITIES**

Except for those commitments and contingent liabilities set out in the note 26 and note 27 to the financial statements, the Group had no significant contingent liabilities as at 31 December 2003.

### **ACQUISITIONS, DISPOSALS AND SIGNIFICANT INVESTMENT**

The Group had not made any significant acquisition, disposal or investment during the Review Period.

### **FUTURE PLANS FOR INVESTMENTS OR CAPITAL ASSETS AND SOURCES OF FUNDING**

With the exception of those plans set out in the Prospectus, there are no plans for any significant investments in capital assets and sources of funding.

## MANAGEMENT DISCUSSION AND ANALYSIS

### EMPLOYEE INFORMATION

As at 31 December 2003, the Group had 131 employees comprising 24 employees based in Hong Kong and 107 employees based in mainland China with a total staff cost, excluding for directors, of approximately HK\$15.5 million (2002: HK\$18.7 million) during the Review Period. The Group continues to provide remuneration package to employees according to market practices and past performance. In addition to basic remuneration, the Group also provides employees with other benefits such as a mandatory provident fund, medical scheme, share option schemes and staff training program. There has been no major change on staff remuneration policies during the year.

The share option scheme continues to play an important role in the motivation and retention of quality employees.

### USE OF PROCEEDS

The net proceeds raised from the new issue of shares by way of placing were approximately HK\$19.2 million, and were utilized in the following areas:

	Use of proceeds as stated		
	in the Prospectus		Actual amount
	Total	Up to 31	utilized up to 31
	December 2003	December 2003	
	HK\$'million	HK\$'million	HK\$'million
Research and development*	6.0	3.8	5.6
Expansion of geographical establishments**	4.0	2.6	0.5
Establishment of network monitoring centre	3.0	2.0	1.6
Sales and marketing	2.0	1.3	0.9
Working capitals	4.0	4.0	4.0
<b>Total</b>	<b>19.0</b>	<b>13.7</b>	<b>12.6</b>

The remaining proceeds of approximately HK\$6.6 million were placed with licensed banks in Hong Kong and PRC.

\* The higher than projected spending on R&D has been due to the speeding up of research on NGN.

\*\* The lower than projected spending has been due to the postponement of expansion plans.

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## **DIRECTORS' REPORT**

The Directors present their annual report and the audited financial statements for the year ended 31 December 2003.

### **PRINCIPAL ACTIVITIES**

The Company acts as an investment holding company while its subsidiaries are principally engaged in the provision of network infrastructure solutions, including the sales of network equipment and software and the provision of related network infrastructure services, provision of network professional services, and sales of its proprietary network software.

The principal activities of the Company's principal subsidiaries are set out in note 29 to the financial statements.

### **RESULTS**

The results of the Group for the year ended 31 December 2003 are set out in the consolidated income statement on page 28 of this annual report.

### **DIVIDEND**

The Directors do not recommend the payment of dividend.

### **SHARE CAPITAL**

Details of the movements in share capital of the Company during the year are set out in note 20 to the financial statements.

### **RESERVES**

Movements in the reserves of the Group and the Company during the year are set out on page 31 of the annual report and note 23 to the financial statements respectively.

The Company's reserves available for distribution represent the share premium less deficit which in aggregate amounted to approximately HK\$39.7 million as at 31 December 2003. Under the Companies Law (Revised) Chapter 22 of the Cayman Islands, the share premium of the Company is available for paying distributions or dividends to shareholders subject to the provisions of its Memorandum and Articles of Association and provided that immediately following the distribution or dividend the Company is able to pay its debts as they fall due in the ordinary course of business. In accordance with the Company's Articles of Association, dividends shall be distributed out of the retained profits or other reserves, including the share premium account, of the Company.

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## DIRECTORS' REPORT

### PROPERTY, PLANT AND EQUIPMENT

During the year, the Group incurred approximately HK\$2.8 million in the acquisition of property, plant and equipment which mainly comprised computer equipment and tools. Details of these and other movements in property, plant and equipment of the Group during the year are set out in note 11 to the financial statements.

### DIRECTORS AND SERVICE CONTRACTS

The Directors of the Company during the year and up to the date of this report were as follows:

#### **Executive Director:**

Chan Sek Keung, Ringo (*Chairman and Chief Executive Officer*)

#### **Non-executive Directors:**

Alasdair Gordon Nagle

Clara Ho

Kwan Kit Tong

#### **Independent Non-executive Directors:**

Pang Hing Chung, Alfred

Tsoi Tai Wai, David

The executive Director has entered into a service contract with the Company for an initial term of three years commencing on 1 January 2002 which will continue thereafter until terminated by either party giving to the other not less than six months' prior written notice.

Each of the non-executive Directors and independent non-executive Directors has been appointed for a term of two years commencing on 1 April 2002, subject to rotation as required by the Articles of Association of the Company.

In accordance with Article 87 of the Company's Articles of Association, Mr. Alasdair Gordon Nagle retires by rotation and, being eligible, offers himself for re-election.

## DIRECTORS' REPORT

### DIRECTORS' AND CHIEF EXECUTIVE'S INTERESTS OR SHORT POSITION IN SHARES AND UNDERLYING SHARES

As at 31 December 2003, the interests and short positions of the directors, chief executive and their respective associates in the shares, underlying shares and debenture or short position and share options of the Company and its associated corporations, as recorded in the register maintained by the Company pursuant to Section 352 of the Securities and Futures Ordinance (the "SFO"), or as otherwise notified to the Company and The Stock Exchange of Hong Kong Limited (the "Stock Exchange") pursuant to rules 5.40 to 5.59 of Rules Governing the Listing of Securities on the Growth Enterprise Market of the Stock Exchange (the "GEM Listing Rules"), were as follows:

#### Long positions:

##### (a) Long position in ordinary shares of HK\$0.01 each of the Company

Name of director	Capacity	Number of issued ordinary shares held	Approximate percentage of the issued share capital of the Company
Chan Sek Keung, Ringo	Beneficial owner	3,136,000	1.08%
	Held by controlled corporation*	56,400,000	19.45%
		59,536,000	20.53%

\* These shares are held by Woodstock Management Limited ("Woodstock"), a company wholly-owned by Mr. Chan Sek Keung, Ringo who is deemed, by virtue of the SFO, to be interested in these shares.

##### (b) Long positions in the underlying shares in the Company

Name of director	Capacity	Number of share options held	Approximate percentage of the issued share capital of the Company
Chan Sek Keung, Ringo	Beneficial owner	4,200,000	1.44%
Alasdair Gordon Nagle	Beneficial owner	375,000	0.13%
Clara Ho	Beneficial owner	375,000	0.13%
Kwan Kit Tong	Beneficial owner	375,000	0.13%
Pang Hing Chung, Alfred	Beneficial owner	1,500,000	0.52%
Tsoi Tai Wai, David	Beneficial owner	750,000	0.26%
		7,575,000	2.61%

Other than as disclosed above, none of the directors, chief executive and their respective associates, had any interests or short positions in any shares, underlying shares or debentures of the Company or any of its associated corporations as at 31 December 2003.

## DIRECTORS' REPORT

### SUBSTANTIAL SHAREHOLDERS AND OTHER SHAREHOLDERS WHOSE INTEREST ARE RECORDED UNDER SECTION 336 OF THE SFO

As at 31 December 2003, the following persons or corporations, in addition to the Director stated under the paragraph headed "Directors' and chief executive's interests or short positions in shares and underlying shares", has relevant interests in the issued share capital of the Company which were recorded in the register of interests required to be kept by the Company pursuant to Section 336 of the SFO.

#### (a) Long positions in ordinary shares of HK\$0.01 each of the Company

Name of shareholder	Capacity	Type of interests	Number of shares	Approximate percentage of the Company's issued share capital
The Applied Research Council ("ARC") (Note i)	Beneficial owner	Corporate	48,460,000	16.71%
HSBC Private Equity Technology (Asia) Limited (Note ii)	Investment manager	Corporate	48,460,000	16.71%
HSBC Private Equity (Asia) Limited (Note ii)	Interest of a controlled corporation	Corporate	48,460,000	16.71%
North 22 Nominees Limited (Note iii)	Beneficial owner	Corporate	36,900,000	12.73%
Mr. Ng Lai Yick (Note iii)	Interest of a controlled corporation	Corporate	36,900,000	12.73%
QPL International Holdings Limited ("QPL") (Note iv)	Beneficial owner	Corporate	35,456,745	12.23%
Mr. Li Tung Lok (Note iv)	Interest of a controlled corporation	Corporate	35,456,745	12.23%
Madam Su Ching Wah (Note iv)	Interest of spouse	Family	35,456,745	12.23%
North 22 Capital Partners Inc.	Beneficial owner	Corporate	19,652,000	6.78%

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## DIRECTORS' REPORT

### SUBSTANTIAL SHAREHOLDERS AND OTHER SHAREHOLDERS WHOSE INTEREST ARE RECORDED UNDER SECTION 336 OF THE SFO *(Continued)*

#### (a) Long positions in ordinary shares of HK\$0.01 each of the Company *(Continued)*

*Notes:*

(i) In addition to these shares, ARC also holds the convertible bonds issued by the Company with a face value of HK\$12,460,000 in aggregate. If these convertible bonds were fully converted on their respective maturity dates, ARC would hold an additional 23,656,730 shares in the Company.

(ii) HSBC Private Equity Technology (Asia) Limited is deemed, by virtue of the SFO, to be interested in these shares as it is the investment manager of ARC.

HSBC Private Equity (Asia) Limited is deemed, by virtue of the SFO, to be interested in these shares as HSBC Private Equity Technology (Asia) Limited is its wholly-owned subsidiary.

(iii) Mr. Ng Lai Yick is deemed, by virtue of the SFO, to be interested in these shares as North 22 Nominees Limited is beneficially wholly-owned by him.

(iv) Mr. Li Tung Lok is the controlling shareholder of QPL and is deemed, by virtue of the SFO, to be interested in the 35,456,745 shares held by QPL.

Madam Su Ching Wah is the spouse of Mr. Li Tung Lok and is deemed, by virtue of the SFO, to be interested in the 35,456,745 shares held by QPL.



## DIRECTORS' REPORT

### (b) Long positions in underlying shares in the Company

Name of Shareholder	Capacity	Amount of convertible bonds of the Company issued	Number of underlying Shares
ARC ( <i>Note i</i> )	Beneficial owner	HK\$12,460,000	23,656,730
HSBC Private Equity Technology (Asia) Limited ( <i>Note ii</i> )	Investment manager	HK\$12,460,000	23,656,730
HSBC Private Equity (Asia) Limited ( <i>Note ii</i> )	Interest of a controlled corporation	HK\$12,460,000	23,656,730

*Notes:*

(i) Pursuant to an agreement dated 26 April 2002 entered into among ARC, the Group and Woodstock, ARC would subscribe for five convertible bonds to be issued by the Company with respective face values of HK\$4,188,100, HK\$3,400,000, HK\$4,800,000, HK\$4,660,000 and HK\$3,000,000. As at 30 September 2003, the Company had redeemed two convertible bonds of face value of HK\$4,188,100 and HK\$3,400,000 respectively on their maturity date leading to ARC's underlying interests in Company's shares being decreased from 38,063,603 shares to 23,656,730 shares.

(ii) HSBC Private Equity Technology (Asia) Limited is deemed (by virtue of the SFO) to be interested in 23,656,730 underlying shares held by ARC as the Company is the investment manager of ARC.

HSBC Private Equity (Asia) Limited is deemed (by virtue of the SFO) to be interested in 23,656,730 underlying shares held by ARC as HSBC Private Equity Technology (Asia) Limited is its wholly-owned subsidiary.

Other than as disclosed above, the Company has not been notified of any other relevant interests or short positions in the shares or underlying shares in the Company as at 31 December 2003.

## DIRECTORS' REPORT

### SHARE OPTION SCHEMES

The Company in a general meeting held on 20 April 2002 adopted both a pre-Initial Public Offering ("IPO") share option scheme (the "Pre-IPO Share Option Scheme") and a post-IPO share option scheme (the "Post-IPO Share Option Scheme").

Save as disclosed below, no options granted pursuant to either the Pre-IPO Share Option Scheme or the Post-IPO Share Option Schemes had been exercised during the year.

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

A summary of the Pre-IPO Share Option Scheme granted on 30 April 2002 which were exercisable from 17 November 2002 to 29 April 2012 is as follows:

	Exercise price per share	Number of share options		
		Outstanding as at 1.1.2003	Cancelled during the year	Outstanding as at 31.12.2003
<i>HK\$</i>				
Type of Participants:				
Directors:				
Chan Sek Keung, Ringo	0.55	3,000,000	–	3,000,000
Pang Hing Chung, Alfred	0.55	750,000	–	750,000
		3,750,000	–	3,750,000
Adviser	0.55	750,000	–	750,000
Employees	0.55	5,913,000	440,000	5,473,000
		10,413,000	440,000	9,973,000

The \$0.55 exercise price per share of the above share options granted under the Pre-IPO Share Option Scheme is the same as the initial public offering price of the Company's shares. No options granted under this scheme lapsed or were exercised since the date of grant and up to 31 December 2003.

Options granted are exercisable as to (i) a maximum of 25% of the total number of options granted six months after 17 May 2002, (the "Date of Listing"); (ii) a maximum additional 6.25% of the total number of options granted after the expiry of each 3-month period twelve months after Date of Listing; and (iii) the remaining options granted on or after the third anniversary of the Date of Listing until the end of the option period or lapse of an option.

The total number of shares in respect of which options are issuable under this scheme was 9,973,000, representing approximately 3.44% of the issued share capital of the Company as at 31 December 2003.

## DIRECTORS' REPORT

### SHARE OPTION SCHEMES (Continued)

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

A summary of the Post-IPO Share Option Scheme is as follows:

	Date of grant	Exercisable period	Closing price*	Exercise price per share <sup>#</sup>	Number of share options				
					Outstanding as at 1.1.2003	Granted during the year	Cancelled during the year	Outstanding as at 31.12.2003	
			HK\$	HK\$					
Types of Participants:									
Directors									
Chan Sek Keung, Ringo	20.2.2003	20.2.2004 to 19.2.2013	0.138	0.138	-	1,200,000	-	1,200,000	
Alasdair Gordon Nagle	20.2.2003	20.2.2004 to 19.2.2013	0.138	0.138	-	375,000	-	375,000	
Clara Ho	20.2.2003	20.2.2004 to 19.2.2013	0.138	0.138	-	375,000	-	375,000	
Kwan Kit Tong	20.2.2003	20.2.2004 to 19.2.2013	0.138	0.138	-	375,000	-	375,000	
Pang Hing Chung, Alfred	20.2.2003	20.2.2004 to 19.2.2013	0.138	0.138	-	750,000	-	750,000	
Tsoi Tai Wai, David	20.2.2003	20.2.2004 to 19.2.2013	0.138	0.138	-	750,000	-	750,000	
						-	3,825,000	-	3,825,000
Adviser									
	20.2.2003	20.2.2004 to 19.2.2013	0.138	0.138	-	300,000	-	300,000	
Employees									
	12.7.2002	12.7.2003 to 11.7.2012	0.385	0.384	5,007,000	-	1,588,000	3,419,000	
	20.2.2003	20.2.2004 to 19.2.2013	0.138	0.138	-	3,734,000	383,000	3,351,000	
	10.10.2003	10.10.2004 to 9.10.2013	0.142	0.142	-	385,000	-	385,000	
						5,007,000	4,119,000	1,971,000	7,155,000
						5,007,000	8,244,000	1,971,000	11,280,000

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## DIRECTORS' REPORT

### SHARE OPTION SCHEMES *(Continued)*

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

\* *The closing price of the Company's shares immediately before the date of grant.*

# *The exercise price represented the average of the closing prices of the Company's shares quoted on the Stock Exchange on the five trading days immediately preceding the date of grant of the options.*

No options granted under this scheme lapsed or were exercised since the date of grant and up to 31 December 2003.

These grants under the Post-IPO Share Option Scheme are exercisable, starting from the first anniversary of the grant date at stepped annual increments of 25% of the total options granted, for a period not later than 10 years from the date of grant.

The total number of shares in respect of which options are issuable under this scheme shall not in aggregate exceed 10% of the number of issued shares.

No participant shall be granted an option which, if exercised in full, would result in such participant becoming entitled to subscribe for such number of shares, as when aggregated with the total number of shares already issued under all the options previously granted to him or her which have been exercised, and, issuable under all the outstanding options previously granted to him or her which are for the time being subsisting and unexercised, would exceed 1% of the total number of shares in issue in any 12 month period up to the date of grant of the option.

The directors of the Company consider that it is inappropriate to state the value of the options granted during the year under the above share option schemes of the Company adopted on 20 April 2002 (the "Schemes") due to the following reasons:

- (i) the calculation of the value of the options will be based on a number of undetermined but crucial variable such as the subscription price payable for the shares in the Company, the number of options to be granted under the Schemes during their duration, the exercise period, interest rate, expected volatility and other relevant variables. In particular, the duration of the Schemes of 10 years will make these volatile variables very difficult to ascertain with accuracy;
- (ii) the generally accepted pricing models of options normally value options which are transferable but the options granted to a grantee under the Schemes are personal to the grantee which are non-transferable and non-assignable and hence calculation of the value of the options granted under the Schemes using such pricing models may not be appropriate; and
- (iii) the directors of the Company are of the view that the calculation on speculative assumptions would not be meaningful and would be misleading to shareholders of the Company.

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## **DIRECTORS' REPORT**

### **DIRECTORS' INTERESTS IN CONTRACTS**

No contracts of significance to which the Company or any of its subsidiaries was a party and in which a director of the Company had a material interest, whether directly or indirectly, subsisted at the end of the year or at any time during the year.

### **MAJOR CUSTOMERS AND SUPPLIERS**

During the year, the aggregate sales attributable to the Group's five largest customers comprised approximately 50% of the Group's total sales while the sales attributable to the Group's largest customer constituted approximately 31% of the Group's total sales.

The aggregate purchases during the year attributable to the Group's five largest suppliers comprised approximately 75% of the Group's total purchases while the purchases attributable to the Group's largest supplier was approximately 48% of the Group's total purchases.

None of the directors, their associates or any shareholder, which to the knowledge of the directors owned more than 5% of the Company's issued share capital, had any interest in the share capital of any of the five largest customers or suppliers of the Group.

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

During the year, neither the Company nor any of its subsidiaries purchased, sold or redeemed any of the Company's listed securities.

### **PRE-EMPTIVE RIGHTS**

There is no provision for pre-emptive rights under the Company's Articles of Association or the laws of Cayman Islands, which would oblige the Company to offer new shares on a pro-rata basis to existing shareholders.

### **CORPORATE GOVERNANCE**

The Company has complied throughout the year ended 31 December 2003 with the board practices and procedures as set out in Rules 5.28 to 5.39 of the GEM Listing Rules.

The audit committee comprises of three members, the two independent non-executive directors, Messrs. Tsoi Tai Wai, David and Pang Hing Chung, Alfred and the executive director, Mr. Chan Sek Keung, Ringo. Mr. Tsoi Tai Wai, David was the Chairman of the audit committee.

During the year, the audit committee held four meetings and the primary duties of the meetings were to review and supervise the financial reporting process and internal control system of the Group.

## **DIRECTORS' REPORT**

### **COMPETING INTEREST**

None of the directors or the management shareholders (as defined in the GEM Listing Rules) of the Company or their respective associates had any interest in a business which competes with or may compete with the business of the Group.

### **SPONSOR'S INTERESTS**

None of the Company's sponsor, CSC Asia Limited, its directors, employees or associates (as referred to in Note 3 to the Rule 6.35 of the GEM Listing Rules) had any interests in any class of securities of the Company or any other company in the Group (including options or rights to subscribe for such securities) as at 31 December 2003.

Pursuant to an agreement dated 10 May 2002, CSC Asia Limited has been retained to act as the Company's sponsor for the period up to 31 December 2004 in return for a monthly advisory fee.

### **AUDITORS**

Messrs. Arthur Andersen & Co were the auditors of the Group up to 31 July 2002, on which date they resigned. On 13 September 2002, Messers. Deloitte Touche Tohmatsu were appointed as auditors of the Group to fill the casual vacancy.

The financial statements accompanying this Annual Report were audited by Messers. Deloitte Touche Tohmatsu. A resolution will be submitted to the annual general meeting of the Company to be held on 28 April 2004 for their re-appointment.

On behalf of the Board of Directors

**CHAN Sek Keung, Ringo**

*Chairman and Chief Executive Officer*

Hong Kong, 25 March 2004

## AUDITORS' REPORT

### 德勤·關黃陳方會計師行

Certified Public Accountants  
26/F, Wing On Centre  
111 Connaught Road Central  
Hong Kong

香港中環干諾道中111號  
永安中心26樓

**Deloitte  
Touche  
Tohmatsu**

#### TO THE SHAREHOLDERS OF WAFER SYSTEMS LIMITED

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

We have audited the financial statements on pages 28 to 57 which have been prepared in accordance with accounting principles generally accepted in Hong Kong.

#### RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITORS

The Company's directors are responsible for the preparation of financial statements which give a true and fair view. In preparing financial statements which give a true and fair view it is fundamental that appropriate accounting policies are selected and applied consistently.

It is our responsibility to form an independent opinion, based on our audit, on those financial statements and to report our opinion solely to you, as a body, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

#### BASIS OF OPINION

We conducted our audit in accordance with Statements of Auditing Standards issued by the Hong Kong Society of Accountants. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgments made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the circumstances of the Company and the Group, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance as to whether the financial statements are free from material misstatement. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements. We believe that our audit provides a reasonable basis for our opinion.

#### OPINION

In our opinion the financial statements give a true and fair view of the state of affairs of the Company and the Group as at 31 December 2003 and of the profit and cash flows of the Group for the year then ended and have been properly prepared in accordance with the disclosure requirements of the Hong Kong Companies Ordinance.

**DELOITTE TOUCHE TOHMATSU**

Hong Kong, 25 March 2004



## CONSOLIDATED INCOME STATEMENT

FOR THE YEAR ENDED 31 DECEMBER 2003

	<i>Notes</i>	<b>2003</b> <i>HK\$'000</i>	2002 <i>HK\$'000</i>
Turnover	4	<b>165,879</b>	180,333
Other operating income		<b>510</b>	424
Changes in materials and equipment		<b>(125,577)</b>	(138,836)
Staff costs		<b>(14,461)</b>	(17,441)
Depreciation and amortisation		<b>(5,134)</b>	(4,771)
Other operating expenses		<b>(16,868)</b>	(23,923)
Profit (loss) from operations	5	<b>4,349</b>	(4,214)
Finance costs	8	<b>(3,207)</b>	(2,186)
Profit (loss) before taxation		<b>1,142</b>	(6,400)
Taxation	9	<b>(285)</b>	551
Net profit (loss) attributable to shareholders		<b>857</b>	(5,849)
Earnings (loss) per share			
– Basic	10	<b>0.30 cents</b>	(2.40) cents
– Diluted	10	<b>0.29 cents</b>	N/A

## CONSOLIDATED BALANCE SHEET AT 31 DECEMBER 2003

	Notes	2003 HK\$'000	2002 HK\$'000
<b>Non-current assets</b>			
Property, plant and equipment	11	4,606	5,550
Software product development costs	12	6,795	5,552
Investments in securities	14	–	400
		<b>11,401</b>	11,502
<b>Current assets</b>			
Inventories		10,623	22,740
Trade and other receivables	15	56,490	97,161
Pledged bank deposits		1,042	19,948
Bank balances and cash		45,167	14,412
		<b>113,322</b>	154,261
<b>Current liabilities</b>			
Trade and other payables	16	24,842	52,531
Taxation		481	196
Convertible bonds maturing within one year	17	9,280	7,363
Short-term bank loans		14,953	–
Trust receipts and import loans	18	18,103	40,697
Bank overdrafts	19	–	356
		<b>67,659</b>	101,143
<b>Net current assets</b>		<b>45,663</b>	53,118
<b>Total assets less current liabilities</b>		<b>57,064</b>	64,620
<b>Non-current liabilities</b>			
Convertible bonds maturing after one year	17	2,804	11,294
<b>Net assets</b>		<b>54,260</b>	53,326
<b>Capital and reserves</b>			
Share capital	20	2,900	2,823
Reserves		51,360	50,503
<b>Shareholders' funds</b>		<b>54,260</b>	53,326

The financial statements on pages 28 to 57 were approved and authorised for issue by the Board of Directors on 25 March 2004 and are signed on its behalf by:

**CHAN Sek Keung, Ringo**  
*Chairman and  
 Chief Executive Officer*

**TSOI Tai Wai, David**  
*Director*

**BALANCE SHEET** AT 31 DECEMBER 2003

	Notes	2003 HK\$'000	2002 HK\$'000
Non-current asset			
Investment in a subsidiary	13	10	10
Current asset			
Amount due from a subsidiary		55,788	53,745
Current liabilities			
Accounts payables		46	50
Amounts due to subsidiaries		1,103	1,058
Convertible bonds maturing within one year	17	9,280	7,363
		<b>10,429</b>	8,471
Net current assets		<b>45,359</b>	45,274
Total assets less current liabilities		<b>45,369</b>	45,284
Non-current liabilities			
Convertible bonds maturing after one year	17	2,804	11,294
Net assets		<b>42,565</b>	33,990
Capital and reserves			
Share capital	20	2,900	2,823
Reserves	23	39,665	31,167
Shareholders' funds		<b>42,565</b>	33,990

**CHAN Sek Keung, Ringo**
*Chairman and  
Chief Executive Officer*
**TSOI Tai Wai, David**
*Director*

## CONSOLIDATED STATEMENT OF CHANGES IN EQUITY FOR THE YEAR ENDED 31 DECEMBER 2003

	Share capital <i>HK\$'000</i>	Share premium <i>HK\$'000</i>	Statutory surplus reserve fund <i>HK\$'000</i>	Enterprise expansion fund <i>HK\$'000</i>	Staff welfare fund <i>HK\$'000</i>	Deficit <i>HK\$'000</i>	Total <i>HK\$'000</i>
At 1 January 2002	1,778	20,059	543	272	272	(559)	22,365
Exercise of conversion rights of a convertible note	354	17,084	–	–	–	–	17,438
Exercise of warrants	131	73	–	–	–	–	204
Issue of new shares on listing	560	30,251	–	–	–	–	30,811
Expenses incurred in connection with the issue of shares	–	(11,643)	–	–	–	–	(11,643)
Net loss attributable to shareholders	–	–	–	–	–	(5,849)	(5,849)
Transfers	–	–	460	230	230	(920)	–
At 31 December 2002	2,823	55,824	1,003	502	502	(7,328)	53,326
Exercise of warrants	77	–	–	–	–	–	77
Net profit attributable to shareholders	–	–	–	–	–	857	857
At 31 December 2003	2,900	55,824	1,003	502	502	(6,471)	54,260

As stipulated by the relevant laws and regulations for foreign investment enterprises in the Mainland China (the "PRC"), the PRC subsidiaries of the Company are required to maintain three statutory reserves, being a statutory surplus reserve fund, an enterprise expansion fund and a staff welfare fund which are non-distributable. Appropriations to such reserves are made out of net profit after taxation of the statutory financial statements of the PRC subsidiaries and the amount and allocation basis are decided by its board of directors annually. The statutory surplus reserve fund can be used to make up prior year losses of the PRC subsidiaries, if any, and can be applied in conversion into capital by means of capitalisation issue. The enterprise expansion fund is used for expanding the capital base of the PRC subsidiaries by means of capitalisation issue. The staff welfare fund, which is to be used for the welfare of the staff and workers of the Company, is of a capital nature.

## CONSOLIDATED CASH FLOW STATEMENT

FOR THE YEAR ENDED 31 DECEMBER 2003

	2003 HK\$'000	2002 HK\$'000
Operating activities		
Profit (loss) before taxation	1,142	(6,400)
Adjustments for:		
Interest income	(222)	(311)
Interest expenses	2,192	967
Amortisation of discount on convertible bonds	1,015	1,219
Depreciation and amortisation	5,134	4,771
Loss (gain) on disposal of property, plant and equipment	122	(18)
Loss on disposal of investment in securities	362	–
Allowance for bad and doubtful debts	45	2,293
Operating cash flows before movements in working capital	9,790	2,521
Decrease (increase) in inventories	12,117	(17,180)
Decrease (increase) in trade and other receivables	40,626	(43,818)
(Decrease) increase in trade and other payables	(27,689)	27,455
Cash from (used in) operations	34,844	(31,022)
Mainland China income tax paid	–	(1,602)
Net cash from (used in) operating activities	34,844	(32,624)
Investing activities		
Interest received	222	311
Purchase of property, plant and equipment	(2,820)	(2,415)
Proceeds from disposal of property, plant and equipment	270	94
Software product development costs paid	(3,005)	(3,674)
Proceeds from disposal of investments in securities	38	–
Decrease in pledged bank deposits	18,906	1,490
Net cash from (used in) investing activities	13,611	(4,194)
Financing activities		
Interest paid	(2,192)	(966)
Proceeds from issue of shares	77	31,015
Expenses incurred in connection with the issue of shares	–	(11,643)
Redemption of convertible bonds	(7,588)	–
Borrowings raised from (repayment of) short-term bank loans	14,953	(4,421)
(Repayment of) borrowings raised from trust receipts and import loans	(22,594)	29,574
Net cash (used in) from financing activities	(17,344)	43,559

**CONSOLIDATED CASH FLOW STATEMENT** FOR THE YEAR ENDED 31 DECEMBER 2003

	2003 <i>HK\$'000</i>	2002 <i>HK\$'000</i>
Net increase in cash and cash equivalents	<b>31,111</b>	6,741
Cash and cash equivalents at 1 January	<b>14,056</b>	7,315
Cash and cash equivalents at 31 December	<b>45,167</b>	14,056
Analysis of the balances of cash and cash equivalents		
Bank balances	<b>45,167</b>	14,412
Bank overdrafts	–	(356)
	<b>45,167</b>	14,056

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## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2003

### 1. GENERAL

The Company was incorporated in the Cayman Islands as an exempted company with limited liability. The shares of the Company are listed on the Growth Enterprise Market of The Stock Exchange of Hong Kong Limited (the "Stock Exchange").

The Company acts as an investment holding company while its subsidiaries are principally engaged in the provision of network infrastructure solutions, including the sales of network equipment and software and the provision of related network infrastructure services, provision of network professional services, and sales of its proprietary network software.

### 2. ADOPTION OF REVISED STATEMENT OF STANDARD ACCOUNTING PRACTICE

In the current year, the Group has adopted for the first time, Hong Kong Financial Reporting Standard ("HKFRS") – Statement of Standard Accounting Practice ("SSAP") 12 (Revised) "Income taxes" issued by the Hong Kong Society of Accountants ("HKSA"). The term of HKFRS is inclusive of SSAPs and Interpretations approved by the HKSA. The adoption of this revised SSAP 12 has introduced a new basis of accounting for income taxes (including both current tax and deferred tax) and additional disclosure requirements. These changes have not had any significant impact on the results for the current or prior periods. Accordingly, no prior period adjustment was required.

### 3. SIGNIFICANT ACCOUNTING POLICIES

The financial statements have been prepared under the historical cost convention and in accordance with accounting principles generally accepted in Hong Kong. The principal accounting policies adopted are as follows:

#### **Basis of consolidation**

The consolidated financial statements incorporate the financial statements of the Company and its subsidiaries made up to 31 December each year.

All significant inter-company transactions and balances within the Group are eliminated on consolidation.

#### **Investments in subsidiaries**

Investments in subsidiaries are stated at cost less any identified impairment loss.

#### **Turnover**

Turnover represents the aggregate of the net amounts received and receivable from third parties in connection with the provision of network infrastructure solutions, network professional services and network software.



## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2003

### 3. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

#### Revenue recognition

Sales of network equipment and software are recognised when the network equipment and software are delivered and title has passed.

Revenue from the provision of network infrastructure services and network professional services are recognised when the services are provided.

Interest income is accrued on a time basis, by reference to the principal outstanding and at the interest rate applicable.

#### Property, plant and equipment

Property, plant and equipment are stated at cost less depreciation and any identified impairment loss at the balance sheet date.

The gain or loss arising from the disposal or retirement of an asset is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognised in the income statement.

Depreciation is provided to write off the cost of property, plant and equipment over their estimated useful lives, using the straight line method, at the rate of 33 $\frac{1}{3}$ % per annum.

#### Software product development costs

Expenditure on research activities is recognised as an expense in the period in which it is incurred.

An internally-generated asset arising from software product development expenditure is recognised only if it is anticipated that the development costs incurred on a clearly-defined project will be recovered through future commercial activity. The resultant asset is amortised on a straight line basis over its estimated useful life of three years.

Where no internally-generated software product can be recognised, development expenditure is recognised as an expense in the period in which it is incurred.

#### Inventories

Inventories, which represent goods held for sale, are stated at the lower of cost and net realisable value. Cost, which comprises all costs of purchase and, where applicable, other costs that have been incurred in bringing the inventories to their present location and condition, is calculated using the weighted average method. Net realisable value represents the estimated selling price in the ordinary course of business less all estimated costs necessary to make the sale.

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## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2003

### 3. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

#### **Impairment**

At each balance sheet date, the Group reviews the carrying amounts of its assets to determine whether there is any indication that those assets have suffered an impairment loss. If the recoverable amount of an asset is estimated to be less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount. Impairment losses are recognised as an expense immediately.

Where an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset in prior years. A reversal of an impairment loss is recognised as income immediately.

#### **Convertible bonds**

Convertible bonds are separately disclosed and regarded as liabilities unless conversion actually occurs. The finance cost recognised in the income statement in respect of the convertible bonds, including the amortisation of discount payable upon the final redemption of the convertible bonds, is calculated so as to produce a constant periodic rate of charge on the remaining balance of the convertible bonds for each accounting period.

#### **Taxation**

Income tax expense represents the sum of the tax currently payable and deferred tax.

The tax currently payable is based on taxable profit for the year. Taxable profit differs from net profit as reported in the income statement because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible.

Deferred tax is the tax expected to be payable or recoverable on differences between the carrying amount of assets and liabilities in the financial statements and the corresponding tax basis used in the computation of taxable profit, and is accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognised for all taxable temporary differences, and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised. Such assets and liabilities are not recognised if the temporary difference arises from the initial recognition of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

Deferred tax liabilities are recognised for taxable temporary differences arising on investments in a subsidiary, except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future.

**NOTES TO THE FINANCIAL STATEMENTS** FOR THE YEAR ENDED 31 DECEMBER 2003**3. SIGNIFICANT ACCOUNTING POLICIES** *(Continued)***Taxation** *(Continued)*

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the asset to be recovered.

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset is realised. Deferred tax is charged or credited to the income statement, except when it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity.

**Foreign currencies**

Transactions in foreign currencies are translated at the rates ruling on the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies are re-translated at the rates ruling on the balance sheet date. Gains and losses arising on translation are dealt with in the income statement.

On consolidation, the assets and liabilities of the Group's overseas operations are translated at exchange rate prevailing on the balance sheet date. Income and expense items are translated at the average exchange rates for the period. Translation differences arising, if any, are classified as equity and transferred to the Group's translation reserve. Such translation differences are recognised as income or as expenses in the period in which the operation is disposed of.

**Operating leases**

Rentals payable under operating leases are charged to the income statement on a straight line basis over the period of the respective leases.

**4. BUSINESS AND GEOGRAPHICAL SEGMENTS****Business segments**

For management purposes, the Group's operations are organised into three operating divisions namely network infrastructure, network professional services and network software. These divisions are the basis on which the Group reports its primary segment information.

Principal activities are as follows:

Network infrastructure	–	the sales of network equipment and software and the provision of related network infrastructure services
Network professional services	–	provision of network professional services
Network software	–	the sales of the Group's proprietary network software

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2003

### 4. BUSINESS AND GEOGRAPHICAL SEGMENTS *(Continued)*

#### Business segments *(Continued)*

Business segments for the year are as follows:

	Turnover		Results	
	2003 <i>HK\$'000</i>	2002 <i>HK\$'000</i>	2003 <i>HK\$'000</i>	2002 <i>HK\$'000</i>
Network infrastructure	<b>135,775</b>	153,650	<b>3,088</b>	(1,327)
Network professional services	<b>28,241</b>	26,326	<b>1,813</b>	(1,169)
Network software	<b>1,863</b>	357	<b>(725)</b>	(1,787)
	<b>165,879</b>	180,333	<b>4,176</b>	(4,283)
Other operating income			<b>510</b>	424
Central administrative expenses			<b>(337)</b>	(355)
Profit (loss) from operations			<b>4,349</b>	(4,214)
Finance costs			<b>(3,207)</b>	(2,186)
Profit (loss) before taxation			<b>1,142</b>	(6,400)
Taxation			<b>(285)</b>	551
Net profit (loss) attributable to shareholders			<b>857</b>	(5,849)

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2003

### 4. BUSINESS AND GEOGRAPHICAL SEGMENTS (Continued)

#### Business segments (Continued)

	2003 HK\$'000	2002 HK\$'000
<b>BALANCE SHEET</b>		
Assets		
Segment assets		
– network infrastructure	60,459	85,518
– network professional services	4,380	20,984
– network software	9,107	6,259
Unallocated corporate assets	50,777	53,002
	<b>124,723</b>	165,763
Liabilities		
Segment liabilities		
– network infrastructure	57,898	93,228
Unallocated corporate liabilities	12,565	19,209
	<b>70,463</b>	112,437
	2003 HK\$'000	2002 HK\$'000
<b>OTHER INFORMATION</b>		
Capital additions		
– network infrastructure	1,160	3,070
– network professional services	682	1,316
– network software	3,983	3,784
	<b>5,825</b>	8,170
Depreciation and amortisation		
– network infrastructure	2,125	2,047
– network professional services	1,248	877
– network software	1,761	1,847
	<b>5,134</b>	4,771

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2003

### 4. BUSINESS AND GEOGRAPHICAL SEGMENTS *(Continued)*

#### Geographical segments

The Group's operations are located in Mainland China (the "PRC") and Hong Kong. The following table provides an analysis of the Group's geographical segment information:

	Turnover	
	2003 <i>HK\$'000</i>	2002 <i>HK\$'000</i>
PRC	<b>146,830</b>	164,798
Hong Kong	<b>19,049</b>	15,535
	<b>165,879</b>	180,333

The following is an analysis of the carrying amount of segment assets and capital additions, analysed by the geographical area in which the assets are located:

	Carrying amount of segment assets		Capital additions	
	2003 <i>HK\$'000</i>	2002 <i>HK\$'000</i>	2003 <i>HK\$'000</i>	2002 <i>HK\$'000</i>
PRC	<b>115,342</b>	42,908	<b>5,072</b>	7,754
Hong Kong	<b>9,381</b>	122,855	<b>753</b>	416
	<b>124,723</b>	165,763	<b>5,825</b>	8,170

**NOTES TO THE FINANCIAL STATEMENTS** FOR THE YEAR ENDED 31 DECEMBER 2003

**5. PROFIT (LOSS) FROM OPERATIONS**

	2003 HK\$'000	2002 HK\$'000
Profit (loss) from operations has been arrived at after charging:		
Directors' remuneration other than fees ( <i>note 6</i> )	<b>1,230</b>	1,239
Other staff's retirement benefits scheme contributions	<b>714</b>	679
Other staff costs	<b>14,747</b>	18,033
Less: Staff costs capitalised in software product development costs	<b>(2,230)</b>	(2,510)
	<b>14,461</b>	17,441
Amortisation of software product development costs	<b>1,762</b>	1,441
Auditors' remuneration		
– current year	<b>430</b>	450
– overprovision in prior years	<b>(64)</b>	–
Depreciation of property, plant and equipment	<b>3,372</b>	3,330
Loss on disposal of investments in securities	<b>362</b>	–
Loss on disposal of property, plant and equipment	<b>122</b>	–
Operating lease rentals in respect of land and buildings	<b>2,314</b>	2,823
Research and development costs	<b>–</b>	297
and after crediting:		
Gain on disposal of property, plant and equipment	<b>–</b>	18
Interest income	<b>222</b>	311

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2003

### 6. DIRECTORS' REMUNERATION

	2003 HK\$'000	2002 HK\$'000
Fees for		
– executive director	–	–
– independent non-executive directors	240	160
– other non-executive directors	–	–
	<b>240</b>	160
Other emoluments for non-executive directors	–	–
Other emoluments for executive director		
– basic salaries and allowances	1,218	1,227
– retirement benefits scheme contributions	12	12
	<b>1,230</b>	1,239
<b>Total directors' remuneration</b>	<b>1,470</b>	1,399

The emoluments of the directors were within the following bands:

	Number of directors 2003 & 2002
Up to HK\$1,000,000	5
HK\$1,000,001 to HK\$1,500,000	1

For each of the two years ended 31 December 2003, the details of remuneration for the executive director are set out above. The directors' fees for each of the independent non-executive director is HK\$120,000 (2002: HK\$80,000).

During the year, no emoluments were paid by the Group to the five highest paid individuals (including directors and employees) as an inducement to join or upon joining the Group or as compensation for loss of office. None of the directors has waived any emoluments during the year.



## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2003

### 7. EMPLOYEES' EMOLUMENTS

The aggregate emoluments of the five highest paid individuals included one executive director of the Company, whose emoluments are included in note 6 above. The aggregate emoluments of the remaining four highest paid individuals are as follows:

	2003 HK\$'000	2002 HK\$'000
Basic salaries and allowances	1,812	3,009
Bonus	–	200
Retirement benefits scheme contributions	48	54
Severance payments	–	109
	<b>1,860</b>	<b>3,372</b>

None of the four highest paid individuals received emoluments in excess of HK\$1 million.

### 8. FINANCE COSTS

	2003 HK\$'000	2002 HK\$'000
Interest on bank borrowings wholly repayable within five years	(2,192)	(967)
Amortisation of discount on convertible bonds	(1,015)	(1,219)
	<b>(3,207)</b>	<b>(2,186)</b>

### 9. TAXATION

	2003 HK\$'000	2002 HK\$'000
The (charge) credit comprises:		
Overprovision of Hong Kong Profits Tax in prior years	–	747
PRC income tax	(285)	(196)
	<b>(285)</b>	<b>551</b>

No provision for Hong Kong Profits Tax has been made in the financial statements as the Group had no assessable profit for the year.

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2003

### 9. TAXATION *(Continued)*

Pursuant to the relevant laws and regulations in the PRC, the Company's PRC subsidiaries are entitled to exemption from PRC income tax for two or three years commencing from their first profit-making year of operation and thereafter, these PRC subsidiaries will be entitled to a 50% relief from PRC income tax for the following three years. During the year, only one of the Company's PRC subsidiaries is within its 50% tax relief period, the rest are within their tax exemption period.

The charge for the year is reconciled to profit (loss) per income statement as follows:

	2003		2002	
	HK\$'000	%	HK\$'000	%
Profit (loss) before taxation	1,142		(6,400)	
Tax at the applicable income tax rate	(200)	(17.5)	1,024	16.0
Tax effect of expenses not deductible for tax purposes	(15,619)	(1,367.6)	(21,479)	(335.6)
Tax effect of income not taxable for tax purposes	15,232	1,333.5	20,836	325.5
Tax effect of unrecognised tax losses	(284)	(24.9)	(456)	(7.1)
Effect of tax exemption granted to PRC subsidiaries	671	58.9	(25)	(0.4)
Overprovision in prior years	-	-	747	11.7
Others	(85)	(7.4)	(96)	(1.5)
<b>Tax effect and effective tax rate for the year</b>	<b>(285)</b>	<b>(25.0)</b>	551	8.6

**NOTES TO THE FINANCIAL STATEMENTS** FOR THE YEAR ENDED 31 DECEMBER 2003**10. EARNINGS (LOSS) PER SHARE**

The calculation of the basic and diluted earnings (loss) per share is based on the following data:

	2003	2002
Earnings:		
Net profit (loss) attributable to shareholders for the purposes of basic and diluted earnings (loss) per share	<b>HK\$857,000</b>	HK\$(5,849,000)
Number of shares:		
Weighted average number of ordinary shares for the purposes of basic earnings (loss) per share	<b>287,021,272</b>	243,625,000
Effect of dilutive potential ordinary shares – warrants	<b>2,705,303</b>	N/A
Weighted average number of ordinary shares for the purposes of diluted earnings (loss) per share	<b>289,726,575</b>	243,625,000

The computation of diluted earnings per share does not assume the conversion of the Company's outstanding convertible bonds for both years since their exercise would result in an increase in earnings per share from continuing ordinary operations for 2003 and a decrease in loss per share from continuing ordinary operations for 2002.

The effect of share options is excluded from the calculation of diluted earnings (loss) per share for both years because the exercise price of the Company's share options is higher than the average market price of ordinary shares for both years.

The computation of diluted earnings per share did not assume the conversion of the Company's outstanding warrants for 2002 since their exercise would result in a decrease in loss per share from continuing ordinary operations for 2002.

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2003

### 11. PROPERTY, PLANT AND EQUIPMENT

	Computer equipment <i>HK\$'000</i>	Furniture, fixtures and office equipment <i>HK\$'000</i>	Motor vehicles <i>HK\$'000</i>	Tools <i>HK\$'000</i>	Total <i>HK\$'000</i>
<b>THE GROUP</b>					
COST					
At 1 January 2003	7,947	1,459	272	2,763	12,441
Reclassifications	(1,042)	116	–	926	–
Additions	1,276	204	166	1,174	2,820
Disposals	(290)	–	–	(261)	(551)
<b>At 31 December 2003</b>	<b>7,891</b>	<b>1,779</b>	<b>438</b>	<b>4,602</b>	<b>14,710</b>
DEPRECIATION					
At 1 January 2003	4,736	883	171	1,101	6,891
Reclassifications	(833)	65	–	768	–
Provided for the year	1,986	380	83	923	3,372
Eliminated on disposals	(122)	–	–	(37)	(159)
<b>At 31 December 2003</b>	<b>5,767</b>	<b>1,328</b>	<b>254</b>	<b>2,755</b>	<b>10,104</b>
NET BOOK VALUES					
<b>At 31 December 2003</b>	<b>2,124</b>	<b>451</b>	<b>184</b>	<b>1,847</b>	<b>4,606</b>
At 31 December 2002	3,211	576	101	1,662	5,550

**NOTES TO THE FINANCIAL STATEMENTS** FOR THE YEAR ENDED 31 DECEMBER 2003

**12. SOFTWARE PRODUCT DEVELOPMENT COSTS**

HK\$'000

**THE GROUP**

**COST**

At 1 January 2002	4,026
Additions	3,674
At 31 December 2002	7,700
Additions	3,005
At 31 December 2003	10,705

**AMORTISATION**

At 1 January 2002	707
Amortised for the year	1,441
At 31 December 2002	2,148
Amortised for the year	1,762
At 31 December 2003	3,910

**CARRYING VALUES**

At 31 December 2003	6,795
At 31 December 2002	5,552

**13. INVESTMENT IN A SUBSIDIARY**

**THE COMPANY**

**2003 & 2002**

HK\$'000

Unlisted shares, at cost	10
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Details of the Company's principal subsidiaries at 31 December 2003 are set out in note 29.

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2003

### 14. INVESTMENTS IN SECURITIES

	THE GROUP	
	2003 <i>HK\$'000</i>	2002 <i>HK\$'000</i>
Unlisted investments securities, at cost	–	400

### 15. TRADE AND OTHER RECEIVABLES

	THE GROUP	
	2003 <i>HK\$'000</i>	2002 <i>HK\$'000</i>
Trade receivables	<b>44,132</b>	78,919
Other receivables	8,155	13,022
Prepaid maintenance charges	4,203	5,220
	<b>56,490</b>	97,161

Payment terms with customers are mainly on credit together with deposits. Invoices are normally payable from 30 to 90 days of issuance, except for certain well established customers. The following is an aged analysis of trade receivables at the balance sheet date:

	THE GROUP	
	2003 <i>HK\$'000</i>	2002 <i>HK\$'000</i>
Age		
0 to 30 days	<b>15,858</b>	48,452
31 to 60 days	<b>10,611</b>	3,912
61 to 90 days	<b>4,241</b>	5,412
91 to 180 days	<b>4,313</b>	16,440
181 to 365 days	<b>9,942</b>	4,323
Over 365 days	<b>227</b>	3,611
	<b>45,192</b>	82,150
Less: Allowance for bad and doubtful debts	<b>(1,060)</b>	(3,231)
	<b>44,132</b>	78,919

**NOTES TO THE FINANCIAL STATEMENTS** FOR THE YEAR ENDED 31 DECEMBER 2003

**16. TRADE AND OTHER PAYABLES**

	<b>THE GROUP</b>	
	<b>2003</b> <i>HK\$'000</i>	<b>2002</b> <i>HK\$'000</i>
Trade payables	<b>14,772</b>	43,926
Other payables	<b>10,070</b>	8,605
	<b>24,842</b>	52,531

The following is an aged analysis of trade payables at the balance sheet date:

	<b>THE GROUP</b>	
	<b>2003</b> <i>HK\$'000</i>	<b>2002</b> <i>HK\$'000</i>
Age		
0 to 30 days	<b>8,862</b>	39,642
31 to 90 days	<b>2,864</b>	756
91 to 180 days	<b>28</b>	3,287
181 to 270 days	<b>13</b>	241
271 to 365 days	<b>3,002</b>	–
Over 365 days	<b>3</b>	–
	<b>14,772</b>	43,926

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2003

### 17. CONVERTIBLE BONDS

	<b>THE GROUP AND THE COMPANY</b>	
	<b>2003</b>	2002
	<i>HK\$'000</i>	<i>HK\$'000</i>
Convertible bonds with an aggregate face value of HK\$12,460,000 (2002: HK\$20,048,100) discounted at a rate of 7% per annum	<b>10,556</b>	17,438
Add: Accumulated amortisation of discount upon the final redemption of the convertible bonds	<b>1,528</b>	1,219
	<b>12,084</b>	18,657
The convertible bonds mature as follows:		
Within one year	<b>9,280</b>	7,363
Between one to two years	<b>2,804</b>	8,673
Between two to five years	–	2,621
	<b>12,084</b>	18,657
Less: Amount matures within one year shown under current liabilities	<b>9,280</b>	7,363
Amount matures after one year	<b>2,804</b>	11,294

The convertible bonds were issued by the Company in April 2002 to replace 50% of the convertible note issued by the Company's subsidiary which amounted to HK\$17,437,500. The redemption monies of the convertible notes were used to subscribe for these convertible bonds which represent an aggregate face value of HK\$20,048,100 with various maturity dates between 2003 and 2005 discounted at a rate of 7% per annum. The bondholder, the Applied Research Council, which is also a substantial shareholder of the Company, has the right, at any time during the period from 18 May, 2003 up to and including the maturity date of the convertible bond, to convert into ordinary shares of the Company at a conversion price of HK\$0.5267 per share, subject to adjustments. The Company has the right to redeem the convertible bonds prior to its maturity subject to the prior consent of the bondholder.

During the year, the Company redeemed convertible bonds at face value of HK\$7,588,000.



## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2003

### 18. TRUST RECEIPTS AND IMPORT LOANS

	THE GROUP	
	2003 HK\$'000	2002 HK\$'000
Trust receipts and import loans		
– secured	–	12,474
– unsecured	18,103	28,223
	18,103	40,697

### 19. BANK OVERDRAFTS

	THE GROUP	
	2003 HK\$'000	2002 HK\$'000
Bank overdrafts		
– secured	–	335
– unsecured	–	21
	–	356

### 20. SHARE CAPITAL

	Number of shares	Amount HK\$'000
Authorised:		
– at 1 January 2002, 31 December 2002 and 31 December 2003	500,000,000	5,000
Issued and fully paid:		
– at 1 January 2002	177,777,800	1,778
– exercise of conversion rights of a convertible note	35,413,282	354
– exercise of warrants	13,045,000	131
– bonus issue of shares	11,918	–
– issue of new shares on listing	56,020,000	560
– at 31 December 2002	282,268,000	2,823
– exercise of warrants	7,676,745	77
– at 31 December 2003	289,944,745	2,900

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2003

### 20. SHARE CAPITAL *(Continued)*

On 20 May 2003, the warrant holder of subscription rights to subscribe for 7,676,745 shares of HK\$0.01 each had exercised its rights at HK\$0.01 per share. All the shares issued during the year rank pari passu with the then existing shares in all respects.

### 21. WARRANTS

In May 2002, the Company issued warrants to a substantial shareholder of the Company, QPL International Holdings Limited, conferring rights to subscribe 7,676,745 ordinary shares of HK\$0.01 each at HK\$0.01 per share exercisable during the six-month period commencing on 17 May 2003.

On 20 May 2003, all the outstanding warrants were exercised to subscribe for 7,676,745 ordinary shares in the Company at a subscription price of HK\$0.01 per share.

### 22. SHARE OPTIONS

#### (a) Pre-Initial Public Offering ("IPO") share option scheme

Pursuant to the pre-IPO share option scheme adopted by the Company on 20 April 2002, the Company may grant options to any director, employee, adviser or business consultant of the Company or its subsidiaries, for the primary purpose of providing incentives to them, to subscribe for shares in the Company with the payment of HK\$1 per offer.

Details of the movements in the number of share options during the year under the Company's pre-IPO share option scheme were as follows:

Type of participants	Exercisable period	Exercise price per share <i>HK\$</i>	Number of share options						
			Outstanding at 1.1.2002	Granted during the year	Cancelled during the year	Outstanding at 1.1.2003	Cancelled during the year	Outstanding at 31.12.2003	
Directors	17th November, 2002 to 29th April, 2012	0.55	–	3,750,000	–	–	3,750,000	–	3,750,000
Others	17th November, 2002 to 29th April, 2012	0.55	–	8,163,000	1,500,000	–	6,663,000	440,000	6,223,000
			–	11,913,000	1,500,000	–	10,413,000	440,000	9,973,000

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2003

### 22. SHARE OPTIONS (Continued)

#### (b) Post-IPO share option scheme

Pursuant to the post-IPO share option scheme adopted by the Company on 20th April, 2002, the Company may grant options to any director, employee, advisor or business consultant of the Company or its subsidiaries, for the primary purpose of providing incentives to them, to subscribe for shares in the Company with the payment of HK\$1 per offer. The exercise price of the share option will be determined at the higher of the average of the closing prices of the Company's shares quoted on the Stock Exchange on the five trading days immediately preceding the date of grant of the options; the closing price of the shares on the Stock Exchange on the date of grant; and the nominal value of the shares.

These grants under the post-IPO share option scheme are exercisable, starting from the first anniversary of the grant date at stepped annual increments of 25% of the total options granted, for a period not later than 10 years from the date of grant.

The total number of shares in respect of which options are issuable under this scheme shall not in aggregate exceed 10% of the number of issued shares.

Details of the movements in the number of share options during the year under the Company's post-IPO share option scheme were as follows:

Type of participants	Exercisable period	Exercise price per share HK\$	Number of share options						
			Outstanding at 1.1.2002	Granted during the year	Cancelled during the year	Outstanding at 1.1.2003	Granted during the year	Cancelled during the year	Outstanding at 31.12.2003
Directors	20th February, 2004 to 19th February, 2013	0.138	-	-	-	-	3,825,000	-	3,825,000
Others	12th July, 2003 to 11th July, 2012	0.384	-	5,277,000	270,000	5,007,000	-	1,588,000	3,419,000
	10th October, 2004 to 9th October, 2013	0.142	-	-	-	-	385,000	-	385,000
	20th February, 2004 to 19th February, 2013	0.138	-	-	-	-	4,034,000	383,000	3,651,000
			-	5,277,000	270,000	5,007,000	8,244,000	1,971,000	11,280,000

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2003

### 22. SHARE OPTIONS *(Continued)*

#### (b) Post-IPO share option scheme *(Continued)*

The financial impact of share options granted is not recorded in the Company's or the Group's balance sheet until such time as the options are exercised, and no charge is recognised in the income statement in respect of the value of options granted during the year. Upon the exercise of the share options, the resulting shares issued are recorded by the Company as additional share capital at the nominal value of the shares, and the excess of the exercise price per share over the nominal value of the shares is recorded by the Company in the share premium account. Options which lapsed or are cancelled prior to their exercise date are deleted from the register of outstanding options.

### 23. RESERVES

	Share premium <i>HK\$'000</i>	Deficit <i>HK\$'000</i>	Total <i>HK\$'000</i>
<b>THE COMPANY</b>			
At 1 January 2002	20,059	(99)	19,960
Exercise of conversion rights of a convertible note	17,084	–	17,084
Exercise of warrants	73	–	73
Issue of new shares on listing	30,251	–	30,251
Expenses incurred in connection with the issues of shares	(11,643)	–	(11,643)
Net loss attributable to shareholders	–	(24,558)	(24,558)
At 31 December 2002	55,824	(24,657)	31,167
Net profit attributable to shareholders	–	8,498	8,498
At 31 December 2003	55,824	(16,159)	39,665

### 24. MAJOR NON-CASH TRANSACTIONS

In 2002, the amount due from a related business agent of HK\$5,020,000 in which a director of the Company Mr. Chan Sek Keung, Ringo has a beneficial interest was satisfied by the right to use certain property, plant and equipment of HK\$2,081,000, and prepaid maintenance charges of HK\$2,939,000 held by this related business agent.

In April 2002, the redemption monies of the convertible note of HK\$17,438,000 were used to subscribe for the convertible bonds detailed in note 17.

**NOTES TO THE FINANCIAL STATEMENTS** FOR THE YEAR ENDED 31 DECEMBER 2003**25. UNRECOGNISED DEFERRED TAXATION**

At the balance sheet date, the Group has unutilised tax losses of HK\$10,149,000 (2002: HK\$6,831,000) available for offset against future profits. No deferred tax asset has been recognised in respect of the unutilised tax losses due to the unpredictability of future profit streams. These tax losses may be carried forward indefinitely.

**26. OPERATING LEASE COMMITMENTS**

While the Company had no outstanding operating lease commitments at the balance sheet date, its subsidiaries were committed to make the following future minimum lease payments in respect of land and buildings rented under non-cancellable operating leases which fall due as follows:

	<b>THE GROUP</b>	
	<b>2003</b>	2002
	<i>HK\$'000</i>	<i>HK\$'000</i>
Within one year	<b>2,540</b>	2,643
In the second to fifth year inclusive	<b>1,503</b>	2,320
	<b>4,043</b>	4,963

**27. CONTINGENT LIABILITIES**

At the balance sheet date, the Company has given corporate guarantees totalling HK\$52,000,000 (2002: HK\$103,190,000) to banks to secure the credit facilities granted to its subsidiaries.

**28. RETIREMENT BENEFITS SCHEME**

The Group operates a Mandatory Provident Fund Scheme (the "Scheme") for all qualifying employees in Hong Kong. The assets of the Scheme are held separately from those of the Group in funds under the control of trustee. The Group contributes 5% of relevant payroll costs to the Scheme, which contribution is matched by employees.

The employees of the Company's PRC subsidiaries are members of the state-managed retirement benefits scheme operated by the PRC government. The Company's PRC subsidiaries are required to contribute a certain percentage of their payroll to the retirement benefits scheme to fund the benefits. The only obligation of the Group with respect to the retirement benefits scheme is to make the required contributions under the scheme.

The total cost charged to income statement of HK\$726,000 (2002: HK\$691,000) represents contributions payable to these schemes by the Group in respect of the current accounting period.

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2003

### 29. PRINCIPAL SUBSIDIARIES

Details of the Company's principal subsidiaries, all of which are wholly-owned by the Company, at 31 December 2003 are as follows:

Name of subsidiary	Place of incorporation/ establishment/ operations	Nominal value of issued/ registered capital	Principal activities
Wafer Systems Holdings Limited*	Hong Kong	HK\$10,000	Investment holding
北京威發新世紀信息技術有限公司 (Beijing Wafer New Century Information Technology Co., Ltd.)	PRC for a term of 15 years commencing 12th January, 2001#	US\$1,500,000	Operation of businesses in network infrastructure, provision of network professional services and sales of proprietary network software
上海滬威網絡系統有限公司 (Wafer Network Systems (Shanghai) Co. Ltd.)	PRC for a term of 15 years commencing 28th July, 1999#	US\$210,000	Operation of businesses in network infrastructure, provision of network professional services and sales of proprietary network software
Wafer Systems (China) Limited	Hong Kong	HK\$10,000	Operation of businesses in network infrastructure, provision of network professional services and sales of proprietary network software
Wafer Systems (Hong Kong) Limited	Hong Kong	HK\$10,000	Operation of businesses in network infrastructure, provision of network professional services and sales of proprietary network software
威發(西安)軟件有限公司 (Wafer (Xi'an) Software Co., Ltd.)	PRC for a term of 15 years commencing 26th July, 2001#	US\$100,950	Research and development

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## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2003

### 29. PRINCIPAL SUBSIDIARIES *(Continued)*

\* *Directly held by the Company.*

# *These are wholly foreign owned enterprises established in the PRC.*

The above table lists the subsidiaries of the Company which, in the opinion of the directors, principally affect the results or assets of the Group. To give details of other subsidiaries would, in the opinion of the directors, result in particulars of excessive length.

None of the subsidiaries had any debt securities outstanding at the end of the year, or at any time during the year.

## FINANCIAL SUMMARY

	26.11.1998 to 31.12.1999 <i>HK\$'000</i>	1.1.2000 to 31.12.2000 <i>HK\$'000</i>	1.1.2001 to 31.12.2001 <i>HK\$'000</i>	1.1.2002 to 31.12.2002 <i>HK\$'000</i>	1.1.2003 to 31.12.2003 <i>HK\$'000</i>
<b>RESULTS</b>					
Turnover	124,328	85,339	149,579	180,333	<b>165,879</b>
Profit (loss) before taxation	(7,162)	474	8,198	(6,400)	<b>1,142</b>
Taxation	(1,193)	403	(191)	551	<b>(285)</b>
Net profit (loss) attributable to shareholders	(8,355)	877	8,007	(5,849)	<b>857</b>
<b>As at 31 December</b>					
	1999 <i>HK\$'000</i>	2000 <i>HK\$'000</i>	2001 <i>HK\$'000</i>	2002 <i>HK\$'000</i>	2003 <i>HK\$'000</i>
<b>ASSETS AND LIABILITIES</b>					
Total assets	54,901	70,495	103,280	165,763	<b>124,723</b>
Total liabilities	(59,875)	(74,591)	(80,915)	(112,437)	<b>(70,463)</b>
(Deficiency) balance of shareholders' funds	(4,974)	(4,096)	22,365	53,326	<b>54,260</b>



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## NOTICE OF ANNUAL GENERAL MEETING

**NOTICE IS HEREBY GIVEN THAT** the annual general meeting of Wafer Systems Limited (the "Company") will be held at Units 901-7, 9th Floor, MLC Millennia Plaza, 663 King's Road, North Point, Hong Kong on Wednesday, 28 April 2004 at 3:30 p.m. for the following purposes:

1. To receive and consider the audited consolidated financial statements and reports of the directors and auditors for the year ended 31 December 2003;
2. To re-elect a director Mr. Alasdair Gordon Nagle retiring by rotation;
3. To re-appoint auditors and to authorize the board of directors to fix their remuneration;
4. As special business, to consider and, if thought fit, pass with or without amendments the following resolutions as special and/or ordinary resolutions respectively:

### ORDINARY RESOLUTIONS

- (1) **"THAT:**
  - (a) subject to paragraph (c) of this resolution, and pursuant to the Rules Governing the Listing of Securities on the Growth Enterprise Market of The Stock Exchange of Hong Kong Limited, the exercise by the directors of the Company during the Relevant Period (as hereinafter defined) of all the powers of the Company to allot, issue and deal with additional shares in the capital of the Company and to make or grant, whether conditionally or unconditionally, offers, agreements and options (including warrants, bonds, debentures, notes and any securities which carry rights to subscribe for or are convertible into shares in the Company) which would or might require the exercise of such powers be and is hereby generally and unconditionally approved;
  - (b) the approval in paragraph (a) of this resolution shall authorize the directors of the Company during the Relevant Period to make or grant offers, agreements and options (including warrants, bonds, debentures, notes and any securities which carry rights to subscribe for or are convertible into the shares in the Company) which would or might require the exercise of such powers after the end of the Relevant Period;
  - (c) the aggregate nominal amount of share capital allotted, issued or dealt with or agreed conditionally or unconditionally to be allotted, issued or dealt with (whether pursuant to options or otherwise) by the directors of the Company pursuant to the approval in paragraph (a) of this resolution, otherwise than pursuant to (i) a Rights Issue (as hereinafter defined); or (ii) the grant or exercise of any option under any share option scheme of the Company or any other option, scheme or similar arrangement for the time being adopted for the grant or issue to officers and/or employees of the Company and/or any of its subsidiaries of shares in the Company or rights to acquire shares in the Company; or (iii) any scrip dividend or similar arrangement providing for the allotment of shares in lieu of the whole or part of a dividend on shares in the Company in accordance with the Articles of Association of the Company in force from time to time; or (iv) any issue of shares in the Company upon the exercise of rights of subscription or conversion under the terms of any warrants or convertible bonds issued by the Company or any securities which carry rights to subscribe for or are convertible into shares in the Company,

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## NOTICE OF ANNUAL GENERAL MEETING

shall not exceed 20 per cent. of the aggregate nominal amount of the share capital of the Company in issue on the date of the passing this resolution and the authority pursuant to paragraph (a) of this resolution shall be limited accordingly; and

- (d) for the purpose of this resolution,

“Relevant Period” means the period from the date of the passing this resolution until whichever is the earliest of:

- (i) the conclusion of the next annual general meeting of the Company;
- (ii) the expiration of the period within which the next annual general meeting of the Company is required by the Articles of Association of the Company or any applicable law of the Cayman Islands to be held; and
- (iii) the passing of an ordinary resolution by the shareholders of the Company in general meeting revoking or varying the authority given to the directors of the Company by this resolution.

“Rights Issue” means an offer of shares in the Company, or offer or issue of warrants, options or other securities giving rights to subscribe for shares open for a period fixed by the directors of the Company to holders of shares in the Company on the register on a fixed record date in proportion to their then holdings of such shares (subject to such exclusions or other arrangements as the directors of the Company may deem necessary or expedient in relation to fractional entitlements, or having regard to any restrictions or obligations under the laws of, or the requirements of, or the expense or delay which may be involved in determining the existence or extent of any restrictions or obligations under the laws of, or the requirements of, any jurisdiction applicable to the Company, or any recognized regulatory body or any stock exchange in any territory applicable to the Company.)”

(2) **“THAT:**

- (a) subject to paragraph (b) of this resolution, the exercise by the directors of the Company during the Relevant Period (as hereinafter defined) of all the powers of the Company to repurchase shares in the capital of the Company on the Growth Enterprise Market of The Stock Exchange of Hong Kong Limited or any other stock exchange on which the shares in the Company may be listed and recognized by the Securities and Futures Commission and The Stock Exchange of Hong Kong Limited for such purpose, subject to and in accordance with the rules and regulations of the Securities and Future Commission, The Stock Exchange of Hong Kong Limited, the Companies Law of the Cayman Islands and all other applicable laws in this regard, be and the same is hereby generally and unconditionally approved;
- (b) the aggregate nominal amount of shares in the Company which the Company is authorised to repurchase pursuant to the approval in paragraph (a) of this resolution during the Relevant Period shall not exceed 10 per cent. of the aggregate nominal amount of the issued share capital of the Company as at the date of the passing of this resolution and the authority pursuant to paragraph (a) of this resolution shall be limited accordingly;

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## NOTICE OF ANNUAL GENERAL MEETING

- (c) for the purpose of this resolution,

“Relevant Period” means the period from the date of the passing of this resolution until whichever is the earliest of:

- (i) the conclusion of the next annual general meeting of the Company;
- (ii) the expiration of the period within which the next annual general meeting of the Company is required by the Articles of Association of the Company or any other applicable law of the Cayman Islands to be held; and
- (iii) the passing of an ordinary resolution by the shareholders of the Company in general meeting revoking or varying the authority given to the directors of the Company by this resolution.”

- (3) **“THAT** conditional upon resolution nos. (1) and (2) set out in item 4. of the notice convening this meeting being passed, the general mandate granted to the directors of the Company to allot, issue and deal with additional shares in the Company pursuant to the said resolution no. (1) be and is hereby extended by the addition thereto of an amount representing the aggregate nominal amount of shares in the capital of the Company which are repurchased by the Company under the authority granted to the directors of the Company pursuant to the said resolution no. (2), provided that the amount of shares so repurchased by the Company shall not exceed 10 per cent. of the aggregate nominal amount of the issued share capital of the Company on the date of this resolution.”

### SPECIAL RESOLUTION

- (4) **“THAT** the articles of association of the Company be and are hereby amended as follows:

- (a) That the following definition be added immediately after the definition of “Articles” in Article 2(1):

““associate” the meaning attributed to it in the rules of the Designated Stock Exchange.”

- (b) That the definition of “clearing house” in Article 2(1) be amended as follows:

““clearing house” a recognised clearing house within the meaning of the Securities and Futures Ordinance of Hong Kong (Chapter 571 of the Laws of Hong Kong) or a clearing house recognised by the laws of the jurisdiction in which the shares of the Company are listed or quoted on a stock exchange in such jurisdiction.”

- (c) That the wordings of Article 6 be deleted in its entirety and be substituted with the following wordings:

“The Company may from time to time by special resolution, subject to any confirmation or consent required by the Law, reduce its share capital or any capital redemption reserve or other undistributable reserve in any manner permitted by law.”

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## NOTICE OF ANNUAL GENERAL MEETING

- (d) That Article 76(2) be added immediately after the existing Article 76 as follows:
- “76. (2) Where the Company has knowledge that any Member is, under the rules of the Designated Stock Exchange, required to abstain from voting on any particular resolution of the Company or restricted to voting only for or only against any particular resolution of the Company, any votes cast by or on behalf of such Member in contravention of such requirement or restriction shall not be counted.”
- (e) That the existing Article 76 be re-numbered as Article 76(1).
- (f) That the wordings of Article 84(1) be deleted in its entirety and be substituted with the following wordings:
- “Any corporation which is a Member may by resolution of its directors or other governing body authorise such person as it thinks fit to act as its representative at any meeting of the Company or at any meeting of any class of Members. The person so authorised shall be deemed to have been duly authorized without further evidence of the facts and be entitled to exercise the same powers on behalf of such corporation as the corporation could exercise if it were an individual Member and such corporation shall for the purposes of these Articles be deemed to be present in person at any such meeting if a person so authorised is present thereat.”
- (g) That the wordings of Article 88 be deleted in its entirety and be substituted with the following wordings:
- “No person other than a Director retiring at the meeting shall, unless recommended by the Directors for election, be eligible for election as a Director at any general meeting unless a Notice signed by a Member (other than the person to be proposed) duly qualified to attend and vote at the meeting for which such notice is given of his intention to propose such person for election and also a Notice signed by the person to be proposed of his willingness to be elected shall have been lodged at the head office or at the Registration Office provided that the minimum length of the period, during which such Notice(s) are given, shall be at least seven (7) days and that the period for lodgment of such Notice(s) shall commence no earlier than the day after the dispatch of the notice of the general meeting appointed for such election and end no later than seven (7) days prior to the date of such general meeting.”
- (h) That the wordings of Article 89(1) be deleted in its entirety and be substituted with the following wordings:
- “resigns his office by notice in writing delivered to the Company at the Office or tendered at a meeting of the Board;”
- (i) That the wordings of Article 103(1) be deleted in its entirety and be substituted with the following wordings:
- “A Director shall not vote (nor be counted in the quorum) on any resolution of the Board approving any contract or arrangement or any other proposal in which he or any of his associates is materially interested, but this prohibition shall not apply to any of the following matters namely:
- (i) any contract or arrangement for the giving to such Director or his associate(s) any security or indemnity in respect of money lent by him or any of his associates or obligations incurred or undertaken by him or any of his associates at the request of or for the benefit of the Company or any of its subsidiaries;

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## NOTICE OF ANNUAL GENERAL MEETING

- (ii) any contract or arrangement for the giving of any security or indemnity to a third party in respect of a debt or obligation of the Company or any of its subsidiaries for which the Director or his associate(s) has himself/themselves assumed responsibility in whole or in part whether alone or jointly under a guarantee or indemnity or by the giving of security;
  - (iii) any contract or arrangement concerning an offer of shares or debentures or other securities of or by the Company or any other company which the Company may promote or be interested in for subscription or purchase, where the Director or his associate(s) is/are or is/are to be interested as a participant in the underwriting or sub-underwriting of the offer;
  - (iv) any contract or arrangement in which the Director or his associate(s) is/are interested in the same manner as other holders of shares or debentures or other securities of the Company or any of its subsidiaries by virtue only of his/their interest in shares or debentures or other securities of the Company;
  - (v) any contract or arrangement concerning any other company in which the Director or his associate(s) is/are interested only, whether directly or indirectly, as an officer or executive or a shareholder other than a company in which the Director and/or his associate(s) is/are beneficially interested in five (5) per cent. or more of the issued shares or of the voting rights of any class of shares of such company (or any third company through which his interest or that any of his associates is derived); or
  - (vi) any proposal concerning the adoption, modification or operation of a share option scheme, a pension fund or retirement, death or disability benefits scheme or other arrangement which relates both to directors, his associates and employees of the Company or of any of its subsidiaries and does not provide in respect of any Director or his associate(s), as such any privilege or advantage not accorded to the employees to which such scheme or fund relates.”
- (j) That the wordings of Article 103(2) be deleted in its entirety and be substituted with the following wordings:

“A company shall be deemed to be a company in which a Director and/or his associate(s) owns five (5) per cent. or more if and so long as (but only if and so long as) he and/or his associates are the holders of or beneficially interested in five (5) per cent. or more of any class of the equity share capital of such company or of the voting rights available to members of such company (or of any third company through which his interest or that of his associate(s) is derived). For the purpose of this paragraph there shall be disregarded any shares held by a Director or his associate(s) as bare or custodian trustee and in which he or his associate(s) has no beneficial interest, any shares comprised in a trust in which the interest of the Director or his associate(s) is/are in reversion or remainder if and so long as some other person is entitled to receive the income thereof, and any shares comprised in an authorised unit trust scheme in which the Director or his associate(s) is/are interested only as a unit holder and any shares which carry no voting right at general meetings and very restrictive dividend and return of capital right.”

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## NOTICE OF ANNUAL GENERAL MEETING

- (k) That the wordings of Article 103(3) be deleted in its entirety and be substituted with the following wordings:

“Where a company in which a Director and/or his associate(s) holds five (5) per cent. or more is materially interested in a transaction, then that Director and/or his associate(s) shall also be deemed materially interested in such transaction.”

- (l) That the wordings of Article 146(1) be deleted in its entirety and be substituted with the following wordings:

“The Board shall establish an account to be called the share premium account and shall carry to the credit of such account from time to time a sum equal to the amount or value of the premium paid on the issue of any share in the Company. Unless otherwise provided by the provisions of these Articles, the Board may apply the share premium account in any manner permitted by the Law. The Company shall at all times comply with the provisions of the Law in relation to the share premium account.”

By Order of the Board

**Chan Sek Keung, Ringo**

*Chairman and Chief Executive Officer*

Hong Kong, 25 March 2004

*Notes:*

1. A member of the Company entitled to attend and vote at the above meeting is entitled to appoint another person as his proxy to attend and vote instead of him. A member who is holder of two or more shares may appoint more than one proxy to attend and vote instead of him. A proxy need not be a member of the Company.
2. In order to be valid, a form of proxy together with the power of attorney or other authority (if any) under which it is signed, or a certified copy thereof, must be deposited at the Company’s branch share registrar in Hong Kong, Computershare Hong Kong Investor Services Limited at Shops 1712–1716, 17th Floor, Hopewell Centre, 183 Queen’s Road East, Hong Kong no later than 48 hours before the time appointed for the meeting (or any adjournment thereof).
3. With regard to ordinary resolution no. (2) set out in item 4 of this notice, an explanatory statement containing information regarding the repurchase by the Company of its own shares will be sent to shareholders of the Company together with the 2003 Annual Report of the Company.
4. The Directors wish to state that the above proposed Special Resolution is to mainly facilitate the compliance with the recent changes of the Rules Governing the Listing of Securities on the Growth Enterprise Market of the Stock Exchange of Hong Kong Limited.
5. The translation into Chinese language of this notice (including without limitation the Special Resolution which contains the proposed amendments to the articles of association of the Company) is for reference only. In case of any inconsistency, the English version shall prevail.