



MILKYWAY IMAGE

Milkyway Image Holdings Limited

銀河映像控股有限公司

(incorporated in the Cayman Islands with limited liability)

Annual Report 2004

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This report, for which the directors of Milkyway Image Holdings Limited collectively and individually accept full responsibility, includes particulars given in compliance with the Rules Governing the Listing of Securities on the GEM of the Stock Exchange for the purpose of giving information with regard to Milkyway Image Holdings Limited. The directors of Milkyway Image Holdings Limited, having made all reasonable enquiries, confirm that, to the best of their knowledge and belief: 1. The information contained in this report is accurate and complete in all material respects and not misleading; 2. There are no other matters the omission of which would make any statement in this report misleading; and 3. All opinions expressed in this report have been arrived at after due and careful consideration and are founded on bases and assumptions that are fair and reasonable.

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Corporate Information

Executive Directors

Mr. Law Sau Yiu, Dennis (*Chairman*)
 Ms. Teng Chia Lin, Chialina
 Mr. To Kei Fung

Independent Non-Executive Directors

Mr. Lau Wai Pun, Raymond
 Ms. Ho Mei Yee

Qualified Accountant

Mr. Lee Wai Ming

Company Secretary

Mr. Lee Wai Ming

Authorised Representatives

Mr. Law Sau Yiu, Dennis
 Mr. Lee Wai Ming

Compliance Officer

Mr. Law Sau Yiu, Dennis

Audit Committee

Mr. Lau Wai Pun, Raymond
 Ms. Ho Mei Yee

Registered Office

Century Yard
 Cricket Square
 Hutchins Drive
 P.O. Box 2681GT
 George Town
 Grand Cayman
 British West Indies

Head Office and Principal Place of

Business

1st Floor, 77 Hung To Road
 Kwun Tong
 Kowloon
 Hong Kong

Company Website

<http://www.milkywayimage.com>

Note: Information contained in this website does not form part of this annual report

Stock Code

8130

Sponsor

Hantec Capital Limited
 45th Floor, COSCO Tower
 183 Queen's Road Central
 Hong Kong

Principal Banker

Hang Seng Bank
 No. 83 Des Voeux Road Central
 Hong Kong

Principal Share Registrar and Transfer Office

Bank of Bermuda (Cayman) Limited
 Strathvale House
 North Church Street
 George Town
 Grand Cayman
 Cayman Islands
 British West Indies

Hong Kong Branch Share Registrar and Transfer Office

Secretaries Limited
 Ground Floor, BEA Harbour View Centre
 56 Gloucester Road
 Wanchai
 Hong Kong

Auditors

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

Legal Advisers to the Company

as to Hong Kong Law
 Gallant Y. T. Ho & Co.
 Jardine House 5th Floor
 1 Connaught Place
 Hong Kong

as to the Cayman Islands Law
 Conyers Dill & Pearman, Cayman
 Century Yard
 Cricket Square
 Hutchins Drive
 George Town
 Grand Cayman
 British West Indies

Chairman's Statement

On behalf of the board (the "Board") of the directors (the "Directors") of Milkyway Image Holdings Limited (the "Company"), I have the pleasure in presenting to the shareholders of the Company (the "Shareholders") the second annual report of the Company and its subsidiaries (the "Group") since our successful listing on the GEM of the Stock Exchange in August 2002.

The financial year ended 31 March 2004 was a challenging year for both Hong Kong and the Group. With the outbreak of the Severe Acute Respiratory Syndrome ("SARS") epidemic during the financial year, the Group's business activities were severely affected. In particular, its film shooting schedules have been adversely affected especially for those outbound shootings originally scheduled in regions and cities where SARS outbreaks were reported. Consequently, only one film titled, "*Running On Karma*" [大隻佬], had been produced and delivered by the Group during the year under review compared with four films last year.

Notwithstanding the weakened local economic conditions during the year, the Group insisted on its corporate philosophy producing high quality films for audience. The film, "*Running On Karma*" [大隻佬], was screened in September 2003 and achieved an encouraging box office record despite of such a poor atmosphere in the consumer market in Hong Kong during that period. The film received several awards from the Hong Kong Film Award and the Hong Kong Film Critics Award including Best Screenplay, Best Film and Best Actor Awards. It was also invited to 2003 Berlin International Film Festival's International Forum of New Cinema and 2004 Udine Far East Film Festival.

Apart from film production, the Group has explored new sources of related productions such as music TV and short movies. During the year under review, the Group produced one such music TV and two short movies.

In the wake of the signing of the Closer Economic Partnership Arrangement ("CEPA") and the supportive measures put forward by both the People's Republic of China ("PRC") authority and the local government to boost Hong Kong economy, strong signs of rebound in the consumer market and the economy as a whole are observed in the last quarter of this financial year. With the abolition of quota for Hong Kong films and the relaxation of investments in PRC cinemas, we foresee demand of quality films in the PRC market will continue to grow. In capturing the opportunities arising from the measures introduced by both the local and the PRC authorities and capitalising on the rebound of the local market, the Group will strive to produce quality film titles while maintaining effective cost management and efficient use of the Group's sophisticated filming equipment invested during this financial year.

Finally, I wish to take this opportunity to express my appreciation and thanks to the Board, management and staff for their commitment and dedication to the Group. I would also like to extend my sincere gratitude to our shareholders, business partners, customers and suppliers for their continuous support.

Law Sau Yiu, Dennis
Chairman

Hong Kong
14 June 2004

Management Discussion and Analysis

FINANCIAL REVIEW

Financial Performance

The Group recorded a turnover for the year ended 31 March 2004 of approximately HK\$22.7 million, representing a decrease of approximately 59% when compared to that of previous financial year. The decrease in turnover was primarily due to the significant reduction of number of films produced by the Group as a result of the outbreak of SARS epidemic during the year. The spread of the epidemic across the Asia Pacific region severely affected the Group's shooting schedules which have been postponed for a couple of months. The total number of films produced by the Group during the year under review was one compared with four in last year. No TV movies were produced during the year due to the outbreak of SARS as compared with six in last year. On the other hand, the Group was engaged to produce music TV and short movies and one such music TV and two short movies were produced and delivered.

For the year ended 31 March 2004, the Group recorded a net loss of approximately HK\$10.8 million. (2003: net profit of approximately HK\$2.5 million). The loss was mainly attributable to the reduction in turnover and the increase in other operating expenses. Gross profit ratio dropped from approximately 27.6% last year to approximately 4.6% this year mainly due to the postponement of production schedules and the temporary cessation of the TV movies productions.

As salaries and wages for production crews and other related costs are of semi-fixed in nature during the postponement period, gross profit ratio inevitably dropped as a result. In addition, the Group produced no TV movies during the year and this also contributed to the drop in the overall gross profit ratio since the margin for TV movies productions is generally higher than that of film productions.

Increase in other operating income was mainly due to a forfeited deposit, net of production cost, of approximately HK\$2.8 million relating to an aborted film production project.

Other operating expenses increased by approximately 37% as compared with last year primarily due to: (i) higher depreciation charges for filming equipment acquired during the year and the full year effect on the leasehold improvement on the office premises where the Group's headquarter relocated in the second half of 2003; (ii) increase in head counts of employees resulted in increased staff-related costs; (iii) increase in fixed operating lease rentals in respect of the Group's office premises and studio and the associated utilities expenses; and (iv) higher compliance fee and related professional fees after listing of the Company's shares on GEM.

Management Discussion and Analysis

Liquidity, Financial Resources and Capital Structure

The shareholders' funds of the Group as at 31 March 2004, amounted to approximately HK\$10.3 million (2003: HK\$20.9 million). Current assets amounted to approximately HK\$29.2 million (2003: HK\$40.7 million), of which approximately HK\$3.5 million (2003: HK\$11.4 million) were bank balances and cash. Current liabilities amounted to approximately HK\$37.7 million (2003: HK\$36.3 million) mainly comprised advanced receipts from film companies and trade and other payables. The Group did not have any bank borrowings as at 31 March 2004.

The Group generally financed its film production activities and other operations with inflow of advanced receipts from film companies. It financed its investing activities partly with funds from internally generated cash flow and partly from the net proceeds raised from the listing of the Company's shares on GEM on 26 August 2002 in the manner as stated in the prospectus dated 13 August 2002 issued by the Company (the "Prospectus").

Apart from the issue of shares upon the exercise by a senior management of his share option rights to subscribe for shares of the Company, there has been no change in the capital structure of the Company during the year. Subsequent to the balance sheet date, the Company issued 161,000,000 shares of HK\$0.01 each of the Company at a subscription price of HK\$0.037 per share. The Directors believed that the issue of shares could strengthen the Group's capital base and improve its financial position. The Directors also believed that the enlarged capital base would support the continuing development of the Group's existing business activities and would allow the shareholders to participate in the growth of the Group.

Taking into account the Group's financial position at 31 March 2004 and the subsequent issue of shares, the Directors believe that the Group has been in good financial position and is able to satisfy its commitments and working capital requirements.

Foreign Exchange Exposure

As the Group's business transactions for the year ended 31 March 2004 were denominated in Hong Kong Dollars, the Group did not expose to any foreign exchange risks.

Material Acquisition, Disposal and Significant Investments

For the year ended 31 March 2004, the Group had made capital investment amounted to approximately HK\$10.9 million (2003: HK\$12.3 million) in which HK\$9.5 million were camera and lighting equipment. The Directors considered that the investment would enable the Group to further enhance the quality of its film production, reduce reliance on third parties in providing filming equipment and hence reduce the production cost of the Group in the long run.

Management Discussion and Analysis

In the prior year, the Group entered into a co-investment agreement with a PRC film company for a film production project. Due to the changes in market condition, the Group terminated the co-investment agreement by disposing of its share of film rights to an independent third party resulting in a gain of approximately HK\$0.1 million.

Apart from the aforesaid, the Group made no other material acquisitions or disposals of subsidiaries or any other investments during the year ended 31 March 2004.

Employees and Remuneration Policies

As at 31 March 2004, the Group employed a total of 19 employees (2003: 11), including the executive directors. The Group remunerated its employees in accordance with their work performance and experience. The Directors had their discretions in granting share options and bonuses to the Group's employees depending upon the work performance of particular employee and the financial performance of the Group. No share options were granted during the year. For the year ended 31 March 2004, total staff costs, including Directors' emoluments, amounted to approximately HK\$7.6 million (2003: HK\$6.6 million).

Charges on Group Assets

As at 31 March 2004, the Group did not have any charges on its assets.

Gearing Ratio

As at 31 March 2004, the gearing ratio, expressed as a percentage of total debts over total equity, was 1.5% (2003: 1.3%).

Contingent Liabilities

As at 31 March 2004, the Group did not have any material contingent liabilities.

BUSINESS REVIEW

Segment Information

The Group continued to focus on the provision of film production service during the year. In the mean time, it also explored other new sources of related productions such as music TV and short movies. Although these related productions did not constitute a core business, they did broaden the revenue base. On the other hand, because of the outbreak of SARS and the re-arrangement of production schedules of the Group as a whole, the Group did not produce any TV movies during the year. For the year ended 31 March 2003, the turnover from the production of TV movies was approximately HK\$15.1 million, being approximately 27% to the total turnover of the Group for that year. Nevertheless, the Directors believe that the increasing demand for TV movies in the PRC market remains unchanged and the Group will continue to explore business opportunities in this business segment in the future.

Management Discussion and Analysis

Sales and Marketing

With the aim of raising public awareness and enhancing the sales potential of the films produced by the Group, the Group continued to actively promote and market its films by participating in both local and international film festivals and it became an integral part of the Group's marketing strategy.

The Group has not only earned praises and achieved encouraging box office receipts in local market for the films produced by the Group, but has also proven its competitiveness in international film market. For the year ended 31 March 2004, the films produced by the Group received awards and acclaims as set out below:

Name of Films	Film Festivals	Awards and Acclaims
PTU	2003 Golden Bauhinia Award	Best Film Best Director Best Screenplay Best Actor Best Supporting Actor Best Supporting Actress
	2003 Hong Kong Film Award	Best Director
	2003 Hong Kong Film Critics Award	Best Director
	2003 Taipei Golden Horse Award	Best Screenplay
	2003 Cognac Film Festival	Audience Award
	2003 New York Film Festival	Official Selection
	2003 Tokyo FILMEX Film Festival	Official Selection
	2003 Pusan International Film Festival	Official Selection
	2003 St. Louis Film Festival	Official Selection
	2004 Wisconsin Film Festival	Official Selection
Running On Karma 「大隻佬」	2003 Hong Kong Film Award	Best Film Best Actor Best Screenplay
	2003 Hong Kong Film Critics Award	Best Actor Best Screenplay Best Actress
	2003 Berlin International Film Festival	Official Selection – International Forum of New Cinema
	2004 Udine Far East Film Festival	Official Selection
Turn Left Turn Right 「向左走 • 向右走」	2003 Taipei Golden Horse Award	Best Song
	2004 Udine Far East Film Festival	Closing Film
	2003 Pusan International Film Festival	Official Selection

Management Discussion and Analysis

Film Production

Regarding the film projects signed with One Hundred Years of Films Company Limited (“OHY”), Golden Harvest Film Productions Limited (“Golden Harvest”) and Teamwork Motion Pictures Limited (“Teamwork MP”), the Group had completed the production of the film “*Running On Karma*” [大隻佬] for the year under review and had recorded outstanding box office receipt. The film has received various awards as detailed in the previous section headed “Sales and Marketing”. Another film titled “*Throw Down*” [柔道龍虎榜] has been put into production and expected to be screened in the third quarter of 2004.

During the year, the Group entered into agreements (“Assignments”) with a film company (the “Assignor Company”) and Media Asia Films Limited (“Media Asia”) under which the Assignor Company assigned to Media Asia all its rights, title and interests under a master production agreement entered into with the Group. Pursuant to the Assignments, the Group is required to produce two films for Media Asia. Out of the two films for Media Asia, the Group has substantially completed the production of the film “*Breaking News*” [大事件] at the balance sheet date. This film has been the Official Selection of 2004 Festival de Cannes held in May 2004 and has earned praises among film commentaries. The film has been screening at the date of this report.

Apart from the aforementioned film projects, the Group has entered into agreements with another film company, to provide production resources for three films. One of these films has been put into production at the balance sheet date.

Film Investment

In the prior year, the Group entered into a co-investment agreement with a PRC film production company and has contributed HK\$2 million, being 50% of the total investment cost of HK\$4 million. Pursuant to the co-investment agreement, the Group owned 50% of the film rights and share 50% of the profit from all kinds of income arising from the film. Due to the changes in market condition, the Group terminated the co-investment agreement by disposing of its share of film rights to an independent third party resulting in a gain of approximately HK\$0.1 million.

The Directors consider that film investment would be a lucrative business provided that there are good story concepts which meet the preference of audience and the turn-around of the general investment condition in the market as a whole. The Directors believe that by owning solely or partially the copyrights of films, the Group is able to generate recurring licensing income. In this connection, the Group will engage in film investment activities whenever such opportunities arise under favourable market conditions.

Management Discussion and Analysis

Capital Investments in Studios and Equipment

In order to improve the quality of the films produced by the Group and enhance the efficiency of the film production, the Group has established, in prior year, its own in-house editing and sound mixing studio which has been put into use. In order to further enhance its productivity and production quality, the Group has further made capital investment in certain filming equipment during the year amounted to approximately HK\$9.5 million. The Directors consider that the capital investment will reduce reliance on third parties in providing filming equipment and hence reduce the production cost of the Group in the long run.

Future Plans for Material Investments

Other than those disclosed under the section headed "Statement of Business Objectives" in the Prospectus, the Group does not have any future plans for material investments.

Prospects

In view of the strong signs of rebound in the consumer market and the economy as a whole in the last quarter of this financial year subsequent to the outbreak of SARS, the Directors consider the local consumption power is restoring and this, in turn, boosts up the film industry as a whole. With the signing of CEPA and the abolition of quota for Hong Kong films and the relaxation of investments in PRC cinemas, the Directors believe that the future of the film industry is promising and the Group will make its best endeavour to capitalise on the opportunities arising in the region with respect to the film production as well as all other related business opportunities.

In September 2003, Right Opportune Limited became the substantial shareholder of the Company and new executive directors were appointed by the Board. In April 2004, the Company made open offer to issue new shares to strengthen the Group's capital base and improve its financial position. With the combined effect of the re-designated management team and the enlarged capital base, the Directors believe that it can strengthen the overall business development and strategic planning of the Group.

Comparison of Business Objectives with Actual Business Progress

The following is a summary of the actual progress made in comparison with the business objectives as set out in the Company's prospectus dated 13 August 2002 (the "Prospectus") for the period from the Company's latest practical date being 6 August 2002 ("Latest Practical Date") to 31 March 2004:

For the period from the Latest Practical Date to 30 September 2002:

Business objectives as set out in the Prospectus	Actual business progress
<i>Purchase of filming equipment and establishment of editing and mixing studio</i>	
<ul style="list-style-type: none"> • Acquisition of hardware and software for establishing own editing and sound mixing studio to enhance the quality and efficiency of film production 	Implemented as planned
<ul style="list-style-type: none"> • Employ one personnel for operating the studio 	No new staff was employed in this period. However, three full time staff were employed up to 31 March 2004
<ul style="list-style-type: none"> • Acquisition of camera and lighting equipment 	Not yet implemented in this period. The equipment were acquired during the year ended 31 March 2004
<i>Film production</i>	
<ul style="list-style-type: none"> • Schedule to deliver two films 	One film was delivered
<ul style="list-style-type: none"> • Schedule to enter into contracts with script writers, film directors and producers 	Two scriptwriters, one film director and one artist were engaged. However, the contracts with the two scriptwriters were subsequently cancelled in September 2003 and replaced with contracts on individual film basis. The Directors believed that the new arrangement would be more favourable to the Group.
<ul style="list-style-type: none"> • Employ two persons responsible for assisting daily film production and administrative work 	One full-time staff was employed in July 2003

Comparison of Business Objectives with Actual Business Progress

Business objectives as set out in the Prospectus

Actual business progress

Film investment

- | | |
|--|---|
| <ul style="list-style-type: none"> • Make investment in one film project with other film producers or companies | <p>Implemented as planned. However, the co-investment agreement was subsequently cancelled due to the outbreak of SARS and the Directors considered it was more justifiable to concentrate on its own film production projects.</p> |
|--|---|

For the six-month period from 1 October 2002 to 31 March 2003:

Business objectives as set out in the Prospectus

Actual business progress

Purchase of filming equipment and establishment of editing and mixing studio

- | | |
|---|--|
| <ul style="list-style-type: none"> • Commence to upgrade the editing and mixing studio | <p>The studio had been put into operation in the fourth quarter of the year 2002</p> |
|---|--|

Film production

- | | |
|---|--|
| <ul style="list-style-type: none"> • Schedule to deliver six films | <p>Three films were delivered and six TV movies had been produced</p> |
| <ul style="list-style-type: none"> • Continue to engage production personnel and artists to secure the Group's production capacity | <p>One film director and two artists were engaged</p> |
| <ul style="list-style-type: none"> • Identify possible business opportunities to co-produce films with the US film production companies to expose the Group's awareness to other overseas market | <p>One film had been co-produced with a US film production company</p> |

Film investment

- | | |
|--|---|
| <ul style="list-style-type: none"> • Continue to identify possible film investment opportunities with overseas film companies | <p>One film had been co-invested with a PRC film company. However, the Group disposed of its interest in this investment due to the changes in market conditions.</p> |
|--|---|

Comparison of Business Objectives with Actual Business Progress

For the six-month period from 1 April 2003 to 30 September 2003:

Business objectives as set out in the Prospectus

Actual business progress

Purchase of filming equipment and establishment of editing and mixing studio

- Continue to upgrade the editing and mixing studio

Implemented as planned

Film production

- Five films are scheduled to deliver
- Schedule to engage one film with overseas film company targeting at the US market

One film was delivered
Owing to the influence of SARS, overall production and shooting schedules were postponed

Not yet implemented
Owing to the influence of SARS, overall production and shooting schedules were postponed

Film investment

- Invest in one local film project

Not yet implemented
Due to the outbreak of SARS and the slowdown of the economy, up to 31 March 2004, the Group had terminated a total of two film co-investment projects previously signed and concentrated on its own film production projects.

Comparison of Business Objectives with Actual Business Progress

For the six-month period from 1 October 2003 to 31 March 2004:

Business objectives as set out in the Prospectus	Actual business progress
<i>Purchase of filming equipment and establishment of editing and mixing studio</i>	
<ul style="list-style-type: none"> • Continue to upgrade the editing and mixing studio 	Implemented as planned
<ul style="list-style-type: none"> • Seeking advance editing and mixing equipment to replace existing facilities 	Implemented as planned
<ul style="list-style-type: none"> • Employ an additional staff to operate the mixing and editing studio 	Three full time staff were employed up to 31 March 2004
<i>Film production</i>	
<ul style="list-style-type: none"> • Five films are scheduled to deliver 	Owing to the influence of SARS, overall production and shooting schedules were postponed. Accordingly, no film was delivered. The Group has devoted its available resources to catch up the delayed shooting schedules. As at 31 March 2004, two films have been put into production one of which was substantially completed.
<ul style="list-style-type: none"> • Continue to seek opportunities to work with overseas film companies in Taiwan and Malaysia 	Due to the outbreak of SARS, the Group devoted its resources in fulfilling the shooting schedules for existing films which the Group has committed under the production agreements entered into with major film companies.
<ul style="list-style-type: none"> • Continue to identify talented and popular artists and film directors and/or script writers to engage into long-term contracts on project basis 	Two additional artists were engaged
<i>Film investment</i>	
<ul style="list-style-type: none"> • Continue to identify possible investments in any particular films for both local and/or overseas film companies 	Not yet implemented

Comparison of Business Objectives with Actual Business Progress

Use of proceeds from the Company's initial public offering

The proceeds from the Company's issue of new shares at the time of listing on the GEM in August 2002, after deduction of related issue expenses, amounted to approximately HK\$17 million. Of this amount, approximately HK\$16.4 million had been utilised up to 31 March 2004 and approximately HK\$2.6 million has been applied during the year under review in accordance with the proposed application set out in the Prospectus. Details of the application of the proceeds during the period under review are set out as follows:

	Planned amount up to 31 March 2004 <i>HK\$ in million</i>	Actual amount up to 31 March 2004 <i>HK\$ in million</i>	Variance <i>HK\$ in million</i>	Remarks
Film production	5.6	7.8	2.2	The Group has engaged film directors and additional popular artists in order to fulfill the obligations contemplated under the production agreements as stipulated in the Prospectus and other production agreements with other companies
Film investment	5.0	–	(5.0)	Due to the outbreak of SARS and the slowdown of the economy, the Group had terminated the two film co-investment projects previously signed and concentrated on its own film production projects
Purchase of filming equipment and establish editing and mixing studio	4.8	5.2	0.4	No material variance
Working capital	0.8	3.4	2.6	The Group recorded net loss for the year ended 31 March 2004, accordingly, additional funds were utilised to finance its working capital as a temporary measure
Grand total	<u>16.2</u>	<u>16.4</u>	<u>0.2</u>	

Comparison of Business Objectives with Actual Business Progress

Owing to the unpredictable outbreak of SARS, certain milestone events in achieving the Group's business objectives stipulated in the Prospectus have inevitably been postponed resulting in variances as set out above. Nevertheless, the Directors presently do not anticipate any material deviation from the intended use of the net proceeds as disclosed in the Prospectus except the time frame on application of proceeds. To the extent that the net proceeds are not immediately applied for the above purpose, it is the present intention of the Directors to maintain such net proceeds as short term deposits with banks in Hong Kong until such time when they are required.

Profiles of Directors and Senior Management

DIRECTORS

Executive Directors

Mr. Law Sau Yiu, Dennis, aged 41, joined the Group in October 2003 and was appointed as the Chairman. Mr. Law is currently the managing director of Yu Tai Hing Company Limited which is a well-established private property investment and development group in Hong Kong. He has 14 years of experience in property investment and development. Mr. Law is responsible for overall strategic planning and policy making for the Group. He holds a Bachelor of Arts Degree in Communications from Loyola Marymount University of Los Angeles, California in the United States of America.

Ms. Teng Chia Lin, Chialina, aged 39, is a practising dental surgeon. Ms. Teng joined the Group in October 2003. She graduated from Guy's Hospital Medical & Dental School of The United Medical and Dental Schools of Guy's and St. Thomas' (now known as the Guy's, King's and St. Thomas' Schools of Medicine, Biomedical Sciences and the Dental Institute), University of London in the United Kingdom in 1989, with a Bachelor degree in Dental Surgery. She joined The Prince Philip Dental Hospital in 1990, and then started her own private practice in 1991. Ms. Teng also held directorship in a number of property investment companies. She is the spouse of Mr. Law.

Mr. To Kei Fung, aged 49, is the founder of the Group responsible for overseeing and supervising the Group's film production projects. He also acts as film director, producer and consultants of the Group's particular film projects. Mr. To has over 20 years experience in the Hong Kong television and film industries as a producer and director. Prior to establishing the Group in May 1996, Mr. To had worked as a producer for Television Broadcasts Limited for approximately 15 years. He had also held the position of Chief Operational Officer of China Star Laser Disc Co. Ltd. He had produced and/ or directed 25 local films, of which two of them, namely, "*Eight Happiness*" [八星報喜] and "*Justice, My Foot*" [審死官] achieved the highest box office in the years 1988 and 1992 respectively. In 2000, Mr. To produced and directed "*Needing you...*" [孤男寡女] which attained the highest box office in the relevant year.

Independent Non-Executive Directors

Mr. Lau Wai Pun, Raymond, aged 54, was appointed by the Group in March 2004. Mr. Lau is the senior partner of Ford, Kwan & Co. Solicitors & Notaries. He is a solicitor of the Supreme Court of Hong Kong SAR since 1974 and he is also qualified to practise in the United Kingdom and the Australian Capital Territory. Mr. Lau is also a Notary Public and China-appointed Attesting Officer.

Ms. Ho Mei Yee, aged 40, joined Television Broadcasts Limited in 1987 and was later promoted to the Administration Officer position of the drama division. Prior to joining the Group, Ms. Ho was working as the production services controller at China Star I-Content Limited. Ms. Ho was appointed by the Group in November 2001 and has accumulated over 15 years of experience in the entertainment industry.

Profiles of Directors and Senior Management

SENIOR MANAGEMENT

Ms. Chan Dao Ho, aged 40, is the production executive of the Group. Ms. Chan is responsible for overseeing and supervising the administration and film production project of the Group. Prior to joining the Group in May 1996, Ms. Chan worked as an assistant director for Film Workshop Limited and then joined DLO Productions Limited as a production manager. Ms. Chan has over 16 years experience in the Hong Kong film industry.

Mr. Ding Yuin-Shan, aged 29, is the Associate Director-Business of the Group and is in charge of the Group's business development and promotion. He received a master degree in film theory from New York University. Prior to joining the Group in November 2001, he worked for China Star Entertainment Group as film coordinator and was responsible for overseeing film festival activities.

Mr. Lee Wai Ming, aged 37, is the Financial Controller and Company Secretary of the Group. Prior to joining the Group in May 2004, he has over 10 years experience in the auditing and accounting fields. He received a Bachelor of Arts Degree in Accountancy from The Hong Kong Polytechnic University. He is also a fellow member of the Association of Chartered Certified Accountants and an associate member of the Hong Kong Society of Accountants.

Mr. Ng Hung Keung, aged 38, is the treasurer of the Group. Mr. Ng is responsible for the treasury function of the Group. Prior to joining the Group in May 1996, Mr. Ng worked as an accountant for Oriental Harbour Chinese Restaurant. Mr. Ng has over 10 years experience in the accounting field. He holds the Higher Certificate of Accountancy of Hong Kong Technical Colleges.

Report of the Directors

The directors present their annual report and the audited financial statements of the Company for the year ended 31 March 2004.

PRINCIPAL ACTIVITIES

The principal activity of the Company is investment holding. The Group is principally engaged in the provision of film production services and production of television movies. Details of the activities of its subsidiaries are set out in note 12 to the financial statements.

RESULTS

The results of the Group for the year ended 31 March 2004 are set out in the consolidated income statement on page 28.

The directors do not recommend the payment of a dividend.

FINANCIAL SUMMARY

A summary of the results and the assets and liabilities of the Group for the past four financial years is set out on page 60.

PROPERTY, PLANT AND EQUIPMENT

Details of movements during the year in the property, plant and equipment of the Group are set out in note 11 to the financial statements.

SHARE CAPITAL

Details of movements during the year in the share capital of the Company are set out in note 17 to the financial statements.

Report of the Directors

PROPOSED OPEN OFFER OF SHARES OF THE COMPANY

On 15 March 2004, the Company proposed to raise approximately HK\$5,957,000 before expenses by issuing 161,000,000 shares of HK\$0.01 each of the Company at a subscription price of HK\$0.037 per share on the basis of one offer share for every four shares held on 2 April 2004 ("Open Offer"). The proceeds from the Open Offer will be used as general working capital of the Group. Mr. Law Sau Yiu, Dennis, the Chairman and a controlling shareholder of the Company, has undertaken to subscribe for or procure subscription for 71,400,000 shares of HK\$0.01 each of the Company offered under the Open Offer. The remaining 89,600,000 shares of HK\$0.01 each of the Company offered under the Open Offer have been fully underwritten by Kingston Securities Limited pursuant to the underwriting agreement dated 15 March 2004 entered into between the Company, Kingston Securities Limited and Mr. Law Sau Yiu, Dennis. The Open Offer became unconditional and completed on 22 April 2004.

RESERVES

Movements during the year in the reserves of the Group and the Company are set out in note 18 to the financial statements.

DISTRIBUTABLE RESERVES

At 31 March 2004, the amount of the Company's reserves available for distribution to shareholders was approximately HK\$3,591,000, comprising the share premium of approximately HK\$11,387,000, contributed surplus of approximately HK\$78,000 and the accumulated losses of approximately HK\$7,874,000.

Report of the Directors

DIRECTORS

The directors of the Company during the year and up to the date of this report were:

Executive directors:

Mr. Law Sau Yiu, Dennis (<i>Chairman</i>)	(appointed on 9 October 2003)
Ms. Teng Chia Lin, Chialina	(appointed on 9 October 2003)
Mr. To Kei Fung	
Ms. Chan Dao Ho	(resigned on 30 October 2003)
Mr. Ng Hung Keung	(resigned on 30 October 2003)

Independent non-executive directors:

Mr. Lau Wai Pun, Raymond	(appointed on 15 March 2004)
Ms. Ho Mei Yee	
Mr. Tam Kwok Fai, Jasper	(resigned on 15 March 2004)

In accordance with articles 86 and 87 of the Company's articles of association, Ms. Teng Chia Lin, Chialina and Mr. Lau Wai Pun, Raymond shall hold office only until the forthcoming annual general meeting and, being eligible, offer themselves for re-election. Mr. Law Sau Yiu, Dennis, being the Chairman, will continue to hold office.

DIRECTORS' SERVICE CONTRACTS

Mr. Law Sau Yiu, Dennis and Ms. Teng Chia Lin, Chialina, both of whom are executive directors, have entered into service agreements with the Company for an initial fixed term of three years commencing from 9 October 2003. Mr. To Kei Fung, an executive director, has entered into a service agreement with the Company for an initial fixed term of three years commencing from 26 August 2002.

Report of the Directors

DIRECTORS' SERVICE CONTRACTS *(continued)*

Under the said service agreements, Mr. Law Sau Yiu, Dennis and Ms. Teng Chia Lin, Chialina are entitled to an annual salary of HK\$1,800,000 and HK\$456,000 respectively, subject to any increment at such rate as the board of directors may in its absolute discretion determine and Mr. Law Sau Yiu, Dennis and Ms. Teng Chia Lin, Chialina shall abstain from voting in respect of the resolution regarding such increase. Mr. To Kei Fung is entitled to an annual salary of HK\$2,160,000, a housing provision at the rate of HK\$960,000 per annum and a performance bonus to be determined by the board of directors at its absolute discretion provided that Mr. To Kei Fung shall abstain from voting and not be counted towards the quorum in respect of the resolution regarding such performance bonus. The annual salary and housing provision payable to Mr. To Kei Fung under his service agreement with the Company are subject to annual increment at such rate as the board of directors may in its absolute discretion determine and Mr. To Kei Fung shall abstain from voting in respect of the resolution regarding such increase.

Ms. Ho Mei Yee entered into a letter of appointment with the Company on 22 April 2002 for an initial term of one year commencing on 26 August 2002 and will continue thereafter unless and until terminated by either the Company or Ms. Ho Mei Yee and such appointment is subject at all times to the articles of association of the Company.

Mr. Lau Wai Pun, Raymond entered into a letter of appointment with the Company on 15 March 2004 for a term of one year commencing on 15 March 2004 and will continue thereafter unless and until terminated by either the Company or Mr. Lau Wai Pun, Raymond and such appointment is subject at all times to the articles of association of the Company.

Save as disclosed above, none of the directors had any existing or proposed service contract with any member of the Group (excluding contracts expiring or determinable by the employer within one year without payment of compensation (other than statutory compensation)).

Report of the Directors

DIRECTORS' INTERESTS IN SHARES

At 31 March 2004, the interests of the directors and their associates in the shares and underlying shares 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 the Model Code for Securities Transactions by Directors of Listed Companies ("Model Code") were as follows:

Long positions in the ordinary shares of HK\$0.01 each of the Company

Name of director	Capacity	Number of issued ordinary shares held as at 31 March 2004	Number of shares offered under the Open Offer and to subscribe for	Aggregate long position in shares	Aggregate	Aggregate
					long position in shares as a percentage of the issued share capital of the Company as at 31 March 2004	long position in shares as a percentage of the issued share capital of the Company immediately after the Open Offer
Mr. Law Sau Yiu, Dennis	Interest of controlled corporation (Note)	285,600,000	71,400,000	357,000,000	55.4	44.3
Ms. Teng Chia Lin, Chialina	Interest of controlled corporation (Note)	285,600,000	71,400,000	357,000,000	55.4	44.3

Note: These shares are held by and are undertaken to subscribe for by Right Opportune Limited, the entire issued share capital of which is wholly and beneficially owned by Mr. Law Sau Yiu, Dennis. Ms. Teng Chia Lin, Chialina is the spouse of Mr. Law Sau Yiu, Dennis and thus is deemed to be interested in the shares held by or undertaken to subscribe for by Right Opportune Limited.

Other than as disclosed above, at 31 March 2004, none of the directors of the Company or their associates had any interests or short positions in any shares, underlying shares or debentures of the Company or any of its associated corporations (within the meaning of Part XV of the SFO) as recorded in the register required to be kept under Section 352 of the SFO or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code.

Report of the Directors

SHARE OPTION SCHEMES

Particulars of the Company's share option schemes and details of movements during the year in the share options to subscribe for shares of HK\$0.01 each of the Company granted under the share option schemes are set out in note 22 to the financial statements.

ARRANGEMENTS TO PURCHASE SHARES OR DEBENTURES

Other than the share option schemes disclosed above and in note 22 to the financial statements, at no time during the year was the Company or any of its subsidiaries a party to any arrangements to enable the directors of the Company to acquire benefits by means of the acquisition of shares in, or debentures of, the Company or any other body corporate.

DIRECTORS' INTEREST IN CONTRACTS

No contracts of significance to which the Company or 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.

COMPETING INTERESTS

At 31 March 2004, none of the directors, the substantial shareholders nor their respective associates had any interests in any business which competes or may compete with the business of the Group pursuant to Rule 11.04 of the Rules Governing the Listing of Securities on the Growth Enterprise Market ("GEM") of the Stock Exchange (the "GEM Listing Rules").

As disclosed in the prospectus of the Company dated 13 August 2002 in relation to the listing of the Company's shares on GEM, Mr. To Kei Fung, an executive director, has unconditionally and irrevocably undertaken to the Company that he will not at any time during which the Company is listed on GEM and so long as he and/or his associates hold, whether individually or altogether, 10% or more direct or indirect interest of the Company, or he is a director, directly or indirectly carry on, participate in or be engaged, concerned or interested in any business which competes or may compete with the business of the Group from time to time including the provision of film director, producer and/or consultant services to companies whose business shall compete, or may compete, from time to time with any members of the Group.

Report of the Directors

SUBSTANTIAL SHAREHOLDERS

At 31 March 2004, the register of substantial shareholders maintained by the Company under Section 336 of the SFO showed that, other than the interests disclosed above in respect of certain directors, the following shareholders had an interest of 5% or more in the issued share capital of the Company:

Long positions in the ordinary shares of HK\$0.01 each of the Company

Name of shareholder	Capacity	Number of issued ordinary shares held as at 31 March 2004	Number of shares offered under the Open Offer and were undertaken to subscribe for	Aggregate long position		Aggregate long position in shares as a percentage of the issued share capital of the Company immediately after the Open Offer
				Aggregate long position in shares as a percentage of the issued share capital of the Company as at 31 March 2004	Aggregate long position in shares as a percentage of the issued share capital of the Company as at 31 March 2004	
Right Opportune Limited	Beneficial owner	285,600,000	71,400,000	357,000,000	55.4	44.3
Kingston Securities Limited ("Kingston")	Beneficial owner	–	89,600,000 <i>(note 1)</i>	89,600,000	13.9	11.1
Ms. Ma Siu Fong	Interest of controlled corporation	–	89,600,000 <i>(note 1)</i>	89,600,000	13.9	11.1
Ms. Chu Yuet Wah	Interest of controlled corporation	–	89,600,000 <i>(note 1)</i>	89,600,000	13.9	11.1
Grand Sum Assets Limited	Beneficial owner	59,500,000	–	59,500,000	9.2	7.4
Ms. Lee Po Yi, Shirley Anne	Interest of controlled corporation <i>(note 2)</i>	59,500,000	–	59,500,000	9.2	7.4

Notes:

- Reference is made to the prospectus in relation to the Open Offer. Assuming no qualifying shareholders other than Right Opportune Limited has taken up his/her/its entitlement under the Open Offer and the balance of the new shares in respect of the Open Offer have been taken up by Kingston. These shares represent the number of shares offered under the Open Offer to be underwritten by Kingston pursuant to the underwriting agreement, to which Kingston is deemed to be interested under the SFO. Kingston is owned as to 49% by Ms. Ma Siu Fong and as to 51% by Ms. Chu Yuet Wah. Accordingly, Ms. Ma Siu Fong and Ms. Chu Yuet Wah are deemed to be interested in these shares. Details of the Open Offer are set out in page 19 and note 17 to the financial statements.
- Grand Sum Assets Limited is a company wholly and beneficially owned by Ms. Lee Po Yi, Shirley Anne. Accordingly, Ms. Lee Po Yi, Shirley Anne is deemed to be interested in the 59,500,000 shares held by Grand Sum Assets Limited.

Other than as disclosed above, the Company had not been notified of any other interests or short positions representing 5% or more of the Company's issued share capital at 31 March 2004.

Report of the Directors

RETIREMENT BENEFITS SCHEME

Particulars of the retirement benefits scheme of the Group are set out in note 21 to the financial statements.

PURCHASE, SALE OR REDEMPTION OF LISTED SECURITIES OF THE COMPANY

During the year ended 31 March 2004, 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 Companies Laws, Cap. 22 (Law 3 of 1961, as consolidated and revised) of Cayman Islands, which would oblige the Company to offer new shares on a pro-rata basis to existing shareholders.

MAJOR CUSTOMERS AND SUPPLIERS

Major customers

The directors are of the view that the film industry in Hong Kong is largely dominated by a few major film companies. The Group's five largest customers accounted for 100% (2003: 100%) of the Group's turnover. The largest customer accounted for approximately 94% (2003: 41%) of the Group's turnover.

Major suppliers

The only raw material required by the Group's operations is film negatives supplied by a number of film manufacturers in Hong Kong.

Total purchases of the Group amounted to approximately HK\$0.93 million (2003: HK\$0.88 million) representing approximately 4.3% (2003: 2.1%) of the Group's cost of production.

Purchases from the four (2003: three) largest suppliers accounted for 100% (2003: 100%) of the Group's purchases. Purchases from the largest supplier accounted for approximately 36% (2003: 51%) of the Group's purchases.

At no time during the year did the directors, an associate of a director or a shareholder of the Company (which to the knowledge of the directors owns more than 5% of the Company's issued share capital) had an interest in the Group's five largest customers or four largest suppliers during the year.

Report of the Directors

AUDIT COMMITTEE

The Company has established an audit committee on 2 August 2002 with written terms of reference in compliance with the GEM Listing Rules. The primary duties of the audit committee are to review and supervise the financial reporting process and internal control procedures of the Group. The audit committee comprises the two independent non-executive directors. During the year, the audit committee held four meetings to review the Group's annual report, half-year report and quarterly reports.

BOARD PRACTICES AND PROCEDURES

The Company has complied with Board Practices and Procedures as set out in Rules 5.34 to 5.45 of the GEM Listing Rules throughout the year ended 31 March 2004.

SPONSOR'S INTERESTS

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

As notified to the Company by Hantec, at 31 March 2004, neither Hantec, its directors, employees nor their associates had any interests in any class of securities (including options or rights to subscribe for such securities) of the Company or any other companies of the Group.

AUDITORS

Moores Rowland, who acted as auditors of the Company for the past three years, merged with Mazars Hong Kong and has practiced under the name of Moores Rowland Mazars with effect from 1 October 2003.

During the year, Messrs. Moores Rowland Mazars resigned and Messrs. Deloitte Touche Tohmatsu were appointed as auditors of the Company.

A resolution will be submitted to the forthcoming annual general meeting to re-appoint Messrs. Deloitte Touche Tohmatsu as auditors of the Company.

On behalf of the Board

Law Sau Yiu, Dennis

Chairman

Hong Kong, 14 June 2004

Report of the Auditors

Deloitte. 德勤

To the shareholders of
Milkyway Image Holdings Limited
(Incorporated in the Cayman Islands with limited liability)

We have audited the financial statements on pages 28 to 59 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 March 2004 and of the loss 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
Certified Public Accountants
Hong Kong
14 June 2004

Consolidated Income Statement

For the year ended 31 March 2004

	Notes	2004 HK\$'000	2003 HK\$'000
Turnover	4	22,696	55,743
Cost of sales and services		(21,654)	(40,355)
Gross profit		1,042	15,388
Other operating income		4,977	790
Other operating expenses		(17,586)	(12,835)
(Loss) profit from operations	6	(11,567)	3,343
Finance charges on finance leases		(10)	(22)
(Loss) profit before taxation		(11,577)	3,321
Taxation credit (charge)	9	789	(790)
Net (loss) profit for the year	18	(10,788)	2,531
(Loss) earnings per share	10		
Basic		(HK1.70 cents)	HK0.45 cents
Diluted		(HK1.70 cents)	HK0.44 cents

Consolidated Balance Sheet

At 31 March 2004

	Notes	2004 HK\$'000	2003 HK\$'000
Non-current assets			
Property, plant and equipment	11	18,760	11,472
Deposit for purchase of property, plant and equipment		–	6,000
		18,760	17,472
Current assets			
Production in progress		16,508	5,414
Film in progress		–	2,000
Trade debtors	13	8	8,599
Deposits, prepayments and other debtors		9,179	13,278
Bank balances and cash		3,546	11,364
		29,241	40,655
Current liabilities			
Trade creditors	14	4,017	5,957
Other creditors and accruals		647	2,156
Receipt in advance		31,888	27,703
Amounts due to directors	15	1,005	–
Obligations under finance leases – due within one year	16	111	107
Taxation payable		–	344
		37,668	36,267
Net current (liabilities) assets		(8,427)	4,388
		10,333	21,860
Capital and reserves			
Share capital	17	6,440	6,272
Reserves	18	3,854	14,642
		10,294	20,914
Non-current liabilities			
Obligations under finance leases – due after one year	16	39	156
Deferred taxation	19	–	790
		39	946
		10,333	21,860

The financial statements on pages 28 to 59 were approved and authorised for issue by the Board of Directors on 14 June 2004 and are signed on its behalf by:

Law Sau Yiu, Dennis
Director

To Kei Fung
Director

Balance Sheet

At 31 March 2004

	Notes	2004 HK\$'000	2003 HK\$'000
Non-current assets			
Interests in subsidiaries	12	10,009	16,489
Current assets			
Deposits, prepayments and other debtors		154	112
Bank balances and cash		35	35
		189	147
Current liabilities			
Other creditors and accruals		101	137
Amounts due to directors	15	66	–
		167	137
Net current assets		22	10
		10,031	16,499
Capital and reserves			
Share capital	17	6,440	6,272
Reserves	18	3,591	10,227
		10,031	16,499

Law Sau Yiu, Dennis

Director

To Kei Fung

Director

Consolidated Statement of Changes in Equity

For the year ended 31 March 2004

	Total equity HK\$'000
At 1 April 2002	724
Net profit for the year	2,531
Shares issued for cash	25,872
Share issue expenses	(8,213)
At 31 March 2003 and 1 April 2003	20,914
Net loss for the year	(10,788)
Shares issued for cash	168
At 31 March 2004	<u>10,294</u>

Consolidated Cash Flow Statement

For the year ended 31 March 2004

	2004 HK\$'000	2003 HK\$'000
OPERATING ACTIVITIES		
(Loss) profit before taxation	(11,577)	3,321
Adjustments for:		
Interest income	(1)	(6)
Forfeited deposits relating to aborted film production	(2,757)	(117)
Gain on disposal of film in progress	(100)	–
Allowance for production in progress	111	–
Depreciation	3,565	1,227
Finance charges on finance leases	10	22
Loss on disposal of property, plant and equipment	–	125
Operating cash flows before movements in working capital	(10,749)	4,572
Increase in production in progress	(12,798)	(325)
Increase in film in progress	–	(2,000)
Decrease (increase) in trade debtors	8,591	(6,938)
Decrease (increase) in deposits, prepayments and other debtors	4,099	(10,833)
(Decrease) increase in trade creditors	(1,940)	4,199
Decrease in other creditors and accruals	(1,509)	(137)
Increase in receipt in advance	8,535	8,540
Increase in amounts due to directors	1,005	–
Cash used in operations	(4,766)	(2,922)
Hong Kong Profits Tax paid	(345)	(186)
NET CASH USED IN OPERATING ACTIVITIES	(5,111)	(3,108)
INVESTING ACTIVITIES		
Interest received	1	6
Purchase of property, plant and equipment	(4,853)	(12,037)
Proceeds from disposal of film in progress	2,100	–
Deposit for purchase of property, plant and equipment	–	(6,000)
Proceeds from disposal of property, plant and equipment	–	326
Decrease in amount due from a director	–	7,881
NET CASH USED IN INVESTING ACTIVITIES	(2,752)	(9,824)

Consolidated Cash Flow Statement *(continued)*

For the year ended 31 March 2004

	2004 HK\$'000	2003 HK\$'000
FINANCING ACTIVITIES		
Finance charges on finance leases paid	(10)	(22)
Proceeds from issue of shares	168	25,872
Repayment of obligations under finance leases	(113)	(258)
Share issue expenses	–	(8,213)
NET CASH FROM FINANCING ACTIVITIES	45	17,379
NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	(7,818)	4,447
CASH AND CASH EQUIVALENTS AT THE BEGINNING OF THE YEAR	11,364	6,917
CASH AND CASH EQUIVALENTS AT THE END OF THE YEAR		
Bank balances and cash	3,546	11,364

Notes to the Financial Statements

For the year ended 31 March 2004

1. GENERAL

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

The principal activities of the Group are the provision of film production services and production of television movies.

2. ADOPTION OF HONG KONG FINANCIAL REPORTING STANDARDS

In the current year, the Group has adopted, for the first time, the following Hong Kong Financial Reporting Standard ("HKFRS") issued by the Hong Kong Society of Accountants ("HKSA"). The term HKFRS is inclusive of Statements of Standard Accounting Practice ("SSAP(s)") and Interpretations approved by the HKSA.

SSAP 12 (Revised)	Income Taxes
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The principal effect of the implementation of SSAP 12 (Revised) is in relation to deferred tax. In previous years, provision was made for deferred tax using the income statement liability method, i.e. a liability was recognised in respect of timing differences arising, except where those timing differences were not expected to reverse in the foreseeable future. SSAP 12 (Revised) requires the adoption of a balance sheet liability method, whereby deferred tax is recognised in respect of all temporary differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit, with limited exceptions. The adoption of SSAP 12 (Revised) has had no effect on the results for the current or prior accounting years. Accordingly, no prior year adjustment has been required.

Notes to the Financial Statements

For the year ended 31 March 2004

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 March each year.

The results of subsidiaries acquired or disposed of during the year are included in the consolidated income statement from the effective date of acquisition or up to the effective date of disposal, as appropriate.

Revenue recognition

Income from the production of films and television movies is recognised when the production is completed, which is usually upon delivery of the film negatives to the customers.

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

Impairment

At each balance sheet date, the Group reviews the carrying amounts of its tangible and intangible 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 loss is 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, such 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.

Notes to the Financial Statements

For the year ended 31 March 2004

3. SIGNIFICANT ACCOUNTING POLICIES *(continued)*

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 of income or expense that are never taxable and deductible.

Deferred tax is the tax expected to be payable or recoverable on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases 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 goodwill (or negative goodwill) or from the initial recognition (other than in a business combination) 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 subsidiaries, 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.

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 profits 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 year when the liability is settled or the asset is realised. Deferred tax is charged or credited in 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.

Notes to the Financial Statements

For the year ended 31 March 2004

3. SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Property, plant and equipment

Property, plant and equipment is stated at cost less depreciation and any accumulated impairment losses.

Depreciation is provided to write off the cost of items of property, plant and equipment over their estimated useful lives and after taking into account their estimated residual value, using the straight-line method, at the following rates per annum:

Leasehold improvements	20%
Furniture and fixtures	20%
Machinery and equipment	10% – 20%
Motor vehicles	20%
Office equipment	20%

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

Property, plant and equipment held under finance leases are depreciated over their expected useful lives on the same basis as owned assets or, where shorter, the terms of the relevant leases.

Investments in subsidiaries

Investments in subsidiaries are included in the Company's balance sheet at cost, less any identified impairment loss.

Production in progress

Production in progress represents films and television series under production and is stated at production costs incurred to date, less foreseeable losses. Such production costs are carried forward as production in progress in the balance sheet and are transferred to film production costs in the income statement upon completion.

Film in progress

Film in progress represents films and television series under production and is stated at production costs incurred to date, less any identified impairment loss. Such production costs are transferred to film rights upon completion of production.

Notes to the Financial Statements

For the year ended 31 March 2004

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

Leased assets

Leases are classified as finance leases when the terms of the lease transfer substantially all the risks and rewards of ownership of the assets concerned to the Group. Assets held under finance leases are capitalised at their fair values at the date of acquisition. The corresponding liability to the lessor, net of interest charges, is included in the balance sheet as a finance lease obligation. Finance costs, which represent the difference between the total leasing commitments and the fair value of the assets acquired, are charged to the income statement over the term of the relevant lease so as to produce a constant periodic rate of charge on the remaining balance of the obligations for each accounting period.

All other leases are classified as operating leases and the annual rentals are charged to income statement on a straight-line basis over the relevant lease terms.

Receipt in advance

Receipt in advance represents deposits received from film companies before the completion of production of films and television movies pursuant to the production agreements and will be recognised as income when the production has been completed.

Foreign currencies

Transactions in currencies other than Hong Kong dollars are initially recorded at the rates ruling on the dates of the transactions. Monetary assets and liabilities denominated in currencies other than Hong Kong dollars are re-translated at the rates ruling on the balance sheet date. Profits and losses arising on exchange are included in net profit or loss for the year.

Retirement benefits costs

Payments to the Group's retirement benefits scheme are charged as an expense as they fall due.

4. TURNOVER

	2004 HK\$'000	2003 HK\$'000
Film production	22,696	40,643
Television movies production	–	15,100
	22,696	55,743

Notes to the Financial Statements

For the year ended 31 March 2004

5. BUSINESS AND GEOGRAPHICAL SEGMENTS

Business segments

For management purposes, the Group is currently organised into two operating divisions, namely, film production and television movies production. These divisions are the basis on which the Group reports its primary segment information.

Income statement

	Film production		Television movies production		Consolidated	
	2004 HK\$'000	2003 HK\$'000	2004 HK\$'000	2003 HK\$'000	2004 HK\$'000	2003 HK\$'000
Turnover	22,696	40,643	–	15,100	22,696	55,743
RESULT						
Segment profit (loss)	1,042	5,288	(111)	10,100	931	15,388
Unallocated operating income					4,977	790
Unallocated operating expenses					(17,475)	(12,835)
(Loss) profit from operations					(11,567)	3,343
Finance charges on finance leases					(10)	(22)
(Loss) profit before taxation					(11,577)	3,321
Taxation credit (charge)					789	(790)
Net (loss) profit for the year					(10,788)	2,531

Notes to the Financial Statements

For the year ended 31 March 2004

5. BUSINESS AND GEOGRAPHICAL SEGMENTS (continued)

Balance sheet

	Film production		Television movies production		Consolidated	
	2004	2003	2004	2003	2004	2003
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Segment assets	22,014	16,506	2,300	7,515	24,314	24,021
Unallocated corporate assets					23,687	34,106
Consolidated total assets					48,001	58,127
Segment liabilities	35,905	32,910	–	750	35,905	33,660
Unallocated corporate liabilities					1,802	3,553
Consolidated total liabilities					37,707	37,213

Other information

	Film production		Television movies production		Unallocated	
	2004	2003	2004	2003	2004	2003
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Allowance for production in progress	–	–	111	–	–	–
Additions of property, plant and equipment	–	–	–	–	10,853	12,337
Depreciation	–	–	–	–	3,565	1,227
Loss on disposal of property, plant and equipment	–	–	–	–	–	125

Notes to the Financial Statements

For the year ended 31 March 2004

5. BUSINESS AND GEOGRAPHICAL SEGMENTS *(continued)*

Geographical segments

All of the Group's revenue are derived from Hong Kong and all of the Group's assets are located in Hong Kong. Accordingly, no analysis by geographical segment is presented.

6. (LOSS) PROFIT FROM OPERATIONS

	2004 HK\$'000	2003 HK\$'000
(Loss) profit from operations has been arrived at after charging (crediting):		
Auditors' remuneration	280	229
Contributions to retirement benefits scheme (included in staff costs)	135	81
Depreciation of property, plant and equipment	3,565	1,227
Allowance for production in progress (included in other operating expenses)	111	–
Loss on disposal of property, plant and equipment	–	125
Operating lease rental in respect of land and buildings	1,800	1,310
Staff costs including directors' emoluments	7,635	6,606
Interest earned on bank deposits	(1)	(6)
Forfeited deposits relating to aborted film production net of production costs	(2,757)	(117)
Gain on disposal of film in progress	(100)	–

Notes to the Financial Statements

For the year ended 31 March 2004

7. DIRECTORS' EMOLUMENTS

	2004 HK\$'000	2003 HK\$'000
Directors' fees:		
Executive directors	–	–
Independent non-executive directors	77	48
Other emoluments of executive directors:		
Salaries and other allowances	4,669	4,164
Discretionary bonus	–	375
Retirement benefits scheme contributions	26	36
	4,772	4,623

The directors' emoluments for the year ended 31 March 2004 included the emoluments received during the directorship by two directors who resigned as directors during the year and remain as employees of the Group.

The five executive directors of the Company received emoluments of approximately HK\$750,000 (2003: nil), HK\$190,000 (2003: nil), HK\$3,132,000 (2003: HK\$3,507,000), HK\$427,000 (2003: HK\$732,000) and HK\$196,000 (2003: HK\$336,000) respectively.

The three independent non-executive directors of the Company received directors' fees of HK\$61,500 (2003: HK\$40,000), HK\$4,000 (2003: nil) and HK\$11,500 (2003: HK\$8,000) respectively.

During the year, no emolument was paid by the Group to the directors 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 March 2004

8. EMPLOYEES' EMOLUMENTS

The five highest paid individuals of the Group include two (2003: three) directors, details of whose emoluments are set out in note 7 above. The emoluments of the remaining three highest paid individuals included two directors who resigned during the year and remain as employees of the Group (2003: nil) following their resignation as directors of the Company. Details of the emoluments received by them during their directorship for the year are included above. The total amount received by them during the year together with the emoluments of the remaining one individual (2003: two individuals) are as follows:

	2004 HK\$'000	2003 HK\$'000
Salaries and other allowances	1,344	542
Retirement benefits scheme contributions	36	19
	1,380	561

The aggregate emoluments of each of these remaining three (2003: two) individuals were less than HK\$1,000,000 in both years.

9. TAXATION CREDIT (CHARGE)

	2004 HK\$'000	2003 HK\$'000
The credit (charge) comprises:		
Underprovision of Hong Kong Profits Tax in prior years	(1)	–
Deferred taxation (note 19)	790	(790)
	789	(790)

No provision for Hong Kong Profits Tax has been made in the financial statements as the Company and its subsidiaries incurred a loss for taxation purpose for the year.

Notes to the Financial Statements

For the year ended 31 March 2004

9. TAXATION CREDIT (CHARGE) (continued)

The taxation credit (charge) for the year can be reconciled to the (loss) profit before taxation per the consolidated income statement as follows:

	2004 HK\$'000	2003 HK\$'000
(Loss) profit before taxation	(11,577)	3,321
Taxation credit (charge) at domestic income tax rate of 17.5% (2003: 16%)	2,026	(531)
Tax effect of income not taxable for tax purpose	–	2
Tax effect of estimated tax losses not recognised	(1,119)	(192)
Underprovision in prior years	(1)	–
Tax effect of expenses not deductible for tax purpose	(25)	(56)
Increase in opening deferred taxation resulting from an increase in tax rate	(74)	–
Others	(18)	(13)
Taxation credit (charge) for the year	789	(790)

10. (LOSS) EARNINGS PER SHARE

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

	2004 HK\$'000	2003 HK\$'000
Net (loss) profit for the year	(10,788)	2,531

Notes to the Financial Statements

For the year ended 31 March 2004

10. (LOSS) EARNINGS PER SHARE (continued)

	Number of shares	
	2004	2003
Weighted average number of shares for the purpose of basic (loss) earnings per share	636,288,525	564,050,411
Effect of dilutive potential ordinary shares – share options	–	10,208,030
Weighted average number of shares for the purpose of diluted (loss) earnings per share	636,288,525	574,258,441

The computation of diluted loss per share for the year did not assume the exercise of the Company's outstanding share options existed during the year since their exercise would reduce loss per share.

11. PROPERTY, PLANT AND EQUIPMENT

	Leasehold improvements HK\$'000	Furniture and fixtures HK\$'000	Machinery and equipment HK\$'000	Motor vehicles HK\$'000	Office equipment HK\$'000	Total HK\$'000
THE GROUP						
COST						
At 1 April 2003	3,205	671	6,964	459	1,503	12,802
Additions	893	36	9,699	–	225	10,853
At 31 March 2004	4,098	707	16,663	459	1,728	23,655
DEPRECIATION						
At 1 April 2003	196	39	763	69	263	1,330
Charge for the year	713	136	2,301	92	323	3,565
At 31 March 2004	909	175	3,064	161	586	4,895
NET BOOK VALUES						
At 31 March 2004	3,189	532	13,599	298	1,142	18,760
At 31 March 2003	3,009	632	6,201	390	1,240	11,472

Notes to the Financial Statements

For the year ended 31 March 2004

11. PROPERTY, PLANT AND EQUIPMENT (continued)

The net book values of motor vehicles of approximately HK\$298,000 (2003: HK\$390,000) and office equipment of approximately HK\$1,142,000 (2003: HK\$1,240,000) include amounts of approximately HK\$298,000 (2003: HK\$390,000) and HK\$18,000 (2003: HK\$27,000) respectively in respect of assets held under finance leases.

12. INTERESTS IN SUBSIDIARIES

	THE COMPANY	
	2004 HK\$'000	2003 HK\$'000
Unlisted shares, at cost	78	78
Amounts due from subsidiaries	15,031	16,411
Allowance for amounts due from subsidiaries	(5,100)	–
	9,931	–
	10,009	16,489

The amounts due from subsidiaries are unsecured, non-interest bearing and have no fixed repayment terms. In the opinion of the directors, the amount will not be repayable in the next twelve months.

Notes to the Financial Statements

For the year ended 31 March 2004

12. INTERESTS IN SUBSIDIARIES (continued)

The details of the subsidiaries of the Company, all of which are wholly-owned subsidiaries, at 31 March 2004 are as follows:

Name of subsidiary	Country/ place of incorporation	Form of business structure	Issued and fully paid share capital	Principal activities
Galaxy Image (BVI) Limited	British Virgin Islands	Incorporated	Ordinary shares of US\$10,000	Investment holding
Milkyway Image (Hong Kong) Limited	Hong Kong	Incorporated	Ordinary shares of HK\$10,000	Provision of film production and television movies production
Milkyway Image Limited (formerly known as Jetway International Limited)	Hong Kong	Incorporated	Ordinary shares of HK\$2	Production of television movies

Galaxy Image (BVI) Limited is directly held by the Company. The other subsidiaries are indirectly held by the Company.

The principal place of operation of the subsidiaries is Hong Kong.

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

Notes to the Financial Statements

For the year ended 31 March 2004

13. TRADE DEBTORS

The Group has not granted any credit terms to its customers or dealers. The aged analysis of the trade debtors is as follows:

	THE GROUP	
	2004 HK\$'000	2003 HK\$'000
Within 30 days	8	8,599

14. TRADE CREDITORS

The aged analysis of the trade creditors is as follows:

	THE GROUP	
	2004 HK\$'000	2003 HK\$'000
Within six months	4,017	5,957

15. AMOUNTS DUE TO DIRECTORS

THE GROUP AND THE COMPANY

The amounts represent accrued salaries to directors. They are unsecured, non-interest bearing and have no fixed repayment terms.

Notes to the Financial Statements

For the year ended 31 March 2004

16. OBLIGATIONS UNDER FINANCE LEASES

At the balance sheet date, the Group had obligations under finance leases repayable as follows:

	THE GROUP			
	Minimum leases payments		Present value of minimum leases payments	
	2004 HK\$'000	2003 HK\$'000	2004 HK\$'000	2003 HK\$'000
Amount payable under finance leases:				
Within one year	123	123	111	107
More than one year but not exceeding two years	44	123	39	115
More than two years but not exceeding five years	–	44	–	41
	167	290	150	263
Less: Future finance charges	(17)	(27)	–	–
Present value of lease obligations	150	263	150	263
Less: Amount due for payment within one year			(111)	(107)
			39	156

The average lease term is 4 years and leases are repayable in fixed monthly instalments. There is no arrangement for contingent rent payments.

Notes to the Financial Statements

For the year ended 31 March 2004

17. SHARE CAPITAL

	Number of shares	Amount HK\$'000
Authorised:		
At 1 April 2002, ordinary shares of HK\$0.1 each	3,900,000	390
Subdivision of ordinary shares into HK\$0.01 each	35,100,000	–
Increase in authorised share capital, ordinary shares of HK\$0.01 each	9,961,000,000	99,610
<hr/>		
At 31 March 2003 and 31 March 2004, ordinary shares of HK\$0.01 each	10,000,000,000	100,000
<hr/>		
Issued and fully paid:		
At 1 April 2002, ordinary shares of HK\$0.1 each	1	–
Subdivision of ordinary shares into HK\$0.01 each	9	–
Share issued upon reorganisation, ordinary shares of HK\$0.01 each	9,990	–
Issue of shares by capitalisation of share premium account, ordinary shares of HK\$0.01 each	475,990,000	4,760
Issue of shares by placement, ordinary shares of HK\$0.01 each	69,410,000	694
Issue of shares by a public offer, ordinary shares of HK\$0.01 each	14,590,000	146
Issue of shares upon exercise of pre-initial public offering share options, ordinary shares of HK\$0.01 each	67,200,000	672
<hr/>		
At 31 March 2003, ordinary shares of HK\$0.01 each	627,200,000	6,272
Issue of shares upon exercise of pre-initial public offering share options, ordinary shares of HK\$0.01 each	16,800,000	168
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At 31 March 2004, ordinary shares of HK\$0.01 each	644,000,000	6,440

Notes to the Financial Statements

For the year ended 31 March 2004

17. SHARE CAPITAL *(continued)*

On 16 September 2003, a senior management exercised his share option rights to subscribe for 16,800,000 shares in the capital of the Company at an exercise price of HK\$0.01 per share in an aggregate amount of HK\$168,000.

On 15 March 2004, the Company proposed to raise approximately HK\$5,957,000 before expenses by issuing 161,000,000 shares of HK\$0.01 each of the Company at a subscription price of HK\$0.037 per share on the basis of one offer share for every four shares held on 2 April 2004 ("Open Offer"). Mr. Law Sau Yiu, Dennis, a director and a controlling shareholder of the Company, has undertaken to subscribe for or procure subscription for 71,400,000 shares of HK\$0.01 each of the Company offered under the Open Offer. The remaining 89,600,000 shares of HK\$0.01 each of the Company offered under the Open Offer have been fully underwritten by Kingston Securities Limited pursuant to the underwriting agreement dated 15 March 2004 entered into between the Company, Kingston Securities Limited and Mr. Law Sau Yiu, Dennis. The Open Offer became unconditional and completed on 22 April 2004.

Notes to the Financial Statements

For the year ended 31 March 2004

18. RESERVES

	Share premium HK\$'000	Contributed surplus HK\$'000	Retained profits (accumulated losses) HK\$'000	Total HK\$'000
THE GROUP				
At 1 April 2002	–	10	714	724
Net profit for the year	–	–	2,531	2,531
Issue of shares	24,360	–	–	24,360
Capitalisation	(4,760)	–	–	(4,760)
Share issue expenses	(8,213)	–	–	(8,213)
<hr/>				
At 31 March 2003 and 1 April 2003	11,387	10	3,245	14,642
Net loss for the year	–	–	(10,788)	(10,788)
<hr/>				
At 31 March 2004	11,387	10	(7,543)	3,854
<hr/>				
THE COMPANY				
At 1 April 2002	–	–	(72)	(72)
Arising on acquisition of subsidiaries	–	78	–	78
Issue of shares	24,360	–	–	24,360
Capitalisation	(4,760)	–	–	(4,760)
Share issue expenses	(8,213)	–	–	(8,213)
Net loss for the year	–	–	(1,166)	(1,166)
<hr/>				
At 31 March 2003 and 1 April 2003	11,387	78	(1,238)	10,227
Net loss for the year	–	–	(6,636)	(6,636)
<hr/>				
At 31 March 2004	11,387	78	(7,874)	3,591

The contributed surplus of the Group represents the difference between the nominal value of the shares of the subsidiaries acquired and the nominal value of the shares of the Company issued for the acquisition at the time of the reorganisation of the Group.

Notes to the Financial Statements

For the year ended 31 March 2004

18. RESERVES (continued)

The contributed surplus of the Company represents the difference between the nominal value of the shares of the subsidiaries acquired and the nominal value of the shares of the Company issued in exchange pursuant to the reorganisation of the Group.

In accordance with the Companies Law, Cap. 22 (Law 3 of 1961, as consolidated and revised) of the Cayman Islands, the Company's share premium and contributed surplus are distributable to the shareholders of the Company subject to the Company's articles of association and provided that immediately following the distribution of dividends, the Company will be in a position to pay off its debts as and when they fall due in the ordinary course of business.

19. DEFERRED TAXATION

THE GROUP

The followings are the deferred tax liability and asset recognised by the Group and movements thereon:

	Accelerated tax depreciation	Estimated tax losses	Total
	HK\$'000	HK\$'000	HK\$'000
At 1 April 2002	–	–	–
Charge (credit) to income statement	1,270	(480)	790
At 31 March 2003 and 1 April 2003	1,270	(480)	790
Charge (credit) to income statement	584	(1,448)	(864)
Effect of change in tax rate	119	(45)	74
At 31 March 2004	<u>1,973</u>	<u>(1,973)</u>	–

At 31 March 2004, the Group has unused estimated tax losses of approximately HK\$18,862,000 (2003: HK\$4,191,000) available for offset against future profits. A deferred tax asset has been recognised in respect of approximately HK\$11,274,000 (2003: HK\$3,000,000) of such losses. No deferred tax asset has been recognised in respect of the remaining balance of approximately HK\$7,588,000 (2003: HK\$1,191,000) due to the unpredictability of future profit streams.

Notes to the Financial Statements

For the year ended 31 March 2004

19. DEFERRED TAXATION (continued)

THE COMPANY

No deferred tax asset has been recognised in respect of estimated tax losses of approximately HK\$2,704,000 (2003: HK\$1,168,000) due to the unpredictability of future profits streams.

20. COMMITMENTS

(a) Operating lease commitments

At 31 March 2004, the Group had commitments for future minimum lease payments under non-cancellable operating leases in respect of rented premises which fall due as follows:

	THE GROUP	
	2004 HK\$'000	2003 HK\$'000
Within one year	1,800	1,810
In the second to fifth year inclusive	600	2,400
	2,400	4,210

Operating lease payments represented rentals payable by the Group for its office premises. Lease was negotiated for a term of 3 years and rentals were fixed for the period.

The Company had no significant lease commitments at the balance sheet date.

(b) Capital commitments

	THE GROUP	
	2004 HK\$'000	2003 HK\$'000
Capital expenditure in respect of the acquisition of property, plant and equipment contracted for but not provided in the financial statements	—	3,627

Notes to the Financial Statements

For the year ended 31 March 2004

20. COMMITMENTS *(continued)*

(b) Capital commitments *(continued)*

The Company had no significant capital commitments at the balance sheet date.

(c) Other commitments

At 31 March 2004, the Group had contracted for production service but not provided in the financial statements amounting to approximately HK\$19,055,000 (2003: HK\$24,449,000).

The Company had no other commitments at the balance sheet date.

21. RETIREMENT BENEFITS SCHEME

The Group participates in a mandatory provident fund scheme ("MPF Scheme") operated by an approved trustee in Hong Kong and makes contributions for its eligible employees. Under the MPF Scheme, the Group and its employees are each required to make contributions to the MPF Scheme at 5% of the employees' relevant income, subject to the cap of HK\$20,000. Contributions to the MPF Scheme vested immediately.

22. SHARE OPTION SCHEMES

Pursuant to the written resolutions of the shareholders of the Company dated 2 August 2002, two share option schemes, namely the pre-initial public offering share option scheme ("Pre-IPO Share Option Scheme") and the share option scheme ("Share Option Scheme"), were approved and adopted.

Share Option Scheme

The major terms of the Share Option Scheme are summarised as follows:

- (a) The purpose of the Share Option Scheme is to enable the Group to grant share options to selected participants as incentives or rewards for their contribution to the Group.

Notes to the Financial Statements

For the year ended 31 March 2004

22. SHARE OPTION SCHEMES *(continued)*

Share Option Scheme *(continued)*

(b) The participants include:

- (i) (1) any employee or proposed employee of the Company, any of its subsidiaries or any entity ("Invested Entity") in which the Group holds an equity interest, including any executive director of the Company, any of such subsidiaries or any Invested Entity;
- (2) any non-executive director (including independent non-executive directors) of the Company, any of its subsidiaries or any Invested Entity;
- (3) any supplier of goods or services to any member of the Group or any Invested Entity;
- (4) any customer of the Group or any Invested Entity;
- (5) any person or entity that provides research, development or other technological support to the Group or any Invested Entity;
- (6) any shareholder of any member of the Group or any Invested Entity or any holder or any securities issued by any member of the Group or any Invested Entity; and
- (7) any joint venture partner or counter-party to business transactions of the Group.
- (ii) any company wholly owned by one or more persons belonging to any of the above classes of participants.

(c) The exercise price of a share option shall be a price determined by the directors and shall at least be the higher of:

- (i) the closing price of a share of the Company as stated in the Stock Exchange's daily quotations sheet on the date of grant, which must be a business day; and
- (ii) the average closing price of a share of the Company as stated in the Stock Exchange's daily quotations sheets for the five business days immediately preceding the date of grant.

Notes to the Financial Statements

For the year ended 31 March 2004

22. SHARE OPTION SCHEMES *(continued)*

Share Option Scheme *(continued)*

- (d) Maximum number of shares:
- (i) The total number of shares which may be issued upon exercise of all outstanding share options granted and yet to be exercised under the Share Option Scheme and any other share option schemes of the Company must not exceed 30% of the shares in issue from time to time; and
 - (ii) The total number of shares which may be issued upon exercise of all share options to be granted under the Share Option Scheme and any other schemes must not in aggregate, exceed 10% of the shares in issue at the date of adoption of the Share Option Scheme (the "Limit") provided that share options lapsed in accordance with the terms of the Share Option Scheme will not be counted for the purpose of calculating the Limit.
- (e) The total number of shares issued and to be issued upon the exercise of share options granted and to be granted to each participant (including both exercised and outstanding options) in any 12-month period up to and including the date of grant must not exceed 1% of the shares in issue.
- (f) The exercisable period should be determined by the board of directors upon grant of the share option but in any event should not exceed 10 years from the date of grant of the share option.

No share option under the Share Option Scheme has been granted since its adoption on 2 August 2002.

Notes to the Financial Statements

For the year ended 31 March 2004

22. SHARE OPTION SCHEMES (continued)

Pre-IPO Share Option Scheme

The purpose of the Pre-IPO Share Option Scheme is to recognise the contribution of the senior management and independent contractors of the Group to its growth. The principal terms of the Pre-IPO Share Option Scheme conditionally approved by written resolutions of the shareholders of the Company dated 2 August 2002 were substantially the same as the terms of the Share Option Scheme described above except that:

- (a) the subscription price per share was HK\$0.01 representing a discount of approximately 96.67% of the offer price of HK\$0.30 under the placement and public offer of the Company's shares on 19 August 2002;
- (b) the total number of shares subject to the Pre-IPO Share Option Scheme was 84,000,000, representing 15% of the total issued share capital of the Company immediately following completion of the share offer and the capitalisation (but before enlargement by the allotment and issue of shares pursuant to the exercise of the over-allotment option and any share option granted under the Pre-IPO Share Option Scheme); and
- (c) save for the share options which have been granted under the Pre-IPO Share Option Scheme, no further share option was offered or granted under the Pre-IPO Share Option Scheme, as the right to do so was terminated upon the listing of the Company's shares on GEM.

Details of the movement of Pre-IPO Share Options are as follows:

Category of grantees	Date of grant of share options	Exercisable period	Exercise price HK\$	Number of share options					
				At 1.4.2002	Granted during the year	Exercised during the year	At 31.3.2003 and 1.4.2003	Exercised during the year	At 31.3.2004
One senior management	2.8.2002	26.8.2002 to 25.8.2007	0.01	-	16,800,000	-	16,800,000	(16,800,000)	-
Six independent contractors	2.8.2002	26.8.2002 to 25.8.2007	0.01	-	67,200,000	(67,200,000)	-	-	-
				-	84,000,000	(67,200,000)	16,800,000	(16,800,000)	-

The closing price of the Company's shares immediately before the date on which the share options were exercised was HK\$0.039 per share (2003: HK\$0.250, HK\$0.212 and HK\$0.200).

Notes to the Financial Statements

For the year ended 31 March 2004

22. SHARE OPTION SCHEMES *(continued)*

Pre-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 share options are exercised, and no charge is recognised in the income statement in respect of the value of share options granted in 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 as share premium. Share options which lapse or are cancelled prior to their exercise date are deleted from the register of outstanding share options.

23. COMPARATIVE FIGURES

In previous year, deposit for purchase of property, plant and equipment was included in deposits, prepayments and other debtors in the balance sheet and classified as a current asset. This amount has been reclassified as a non-current asset.

Summary of Financial Information

For the year ended 31 March 2004

RESULTS

	Year ended 31 March			
	2001	2002	2003	2004
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
	(Note 1)	(Note 1)	(Note 2)	(Note 2)
Turnover	29,260	96,109	55,743	22,696
Profit (loss) from operations	3,501	8,229	3,343	(11,567)
Finance costs	(19)	(43)	(22)	(10)
Profit (loss) before taxation	3,482	8,186	3,321	(11,577)
Taxation (charge) credit	–	(530)	(790)	789
Profit (loss) attributable to shareholders	3,482	7,656	2,531	(10,788)

ASSETS AND LIABILITIES

	At 31 March			
	2001	2002	2003	2004
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
	(Note 1)	(Note 1)	(Note 2)	(Note 2)
Non-current assets	399	813	17,472	18,760
Current assets	48,219	23,876	40,655	29,241
Current liabilities	53,342	23,834	36,267	37,668
Non-current liabilities	–	131	946	39

Notes:

- (1) The results and assets and liabilities of the Group for each of the two years ended 31 March 2002 have been extracted from the prospectus dated 13 August 2002 issued by the Company. These have been prepared on a combined basis as if the group structure on 22 April 2002 had been in existence throughout the years concerned.
- (2) The results and assets and liabilities of the Group for each of the two years ended 31 March 2004 have been extracted from the consolidated income statement and consolidated balance sheet as set out on pages 28 and 29 of this annual report respectively.