



MILKYWAY IMAGE

Milkyway Image Holdings Limited

銀河映像控股有限公司

(incorporated in the Cayman Islands with limited liability)

First Quarterly Report 2004

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

CONTENTS

	<i>Pages</i>
Highlights	3
Financial and Business Review	4
Prospects	5
Unaudited First Quarterly Results	6
Other Information	9

HIGHLIGHTS

1. Turnover of the Group for the three months ended 30 June 2004 was approximately HK\$25.8 million. No turnover was recorded for the Group for the corresponding period in 2003.
2. Net profit of the Group for the three months ended 30 June 2004 was approximately HK\$2.3 million contrary to a net loss of approximately HK\$3.6 million for the corresponding period of the previous year.
3. Earnings per share of the Group was approximately HK0.31 cents for the three months ended 30 June 2004 (2003: loss per share of HK0.57 cents).
4. The Board does not recommend the payment of any dividend for the three months ended 30 June 2004 (2003: HK\$ Nil).

FINANCIAL AND BUSINESS REVIEW

For the three months ended 30 June 2004, Milkyway Image Holdings Limited (the "Company") and its subsidiaries (together, the "Group") recorded a turnover of approximately HK\$25.8 million (2003: nil) and a net profit attributable to shareholders of approximately HK\$2.3 million (2003: a net loss attributable to shareholders of approximately HK\$3.6 million).

Following the implementation of 'Individual Visit Scheme' in July 2003, the economy in Hong Kong, in particular, the consumer market, is picking up its momentum. The restoration of consumers' confidants also boosts up the whole entertainment market. During the period under review, the Group has devoted its available resources to catch up the delayed shooting schedules caused by the outbreak of the Severe Acute Respiratory Syndrome ("SARS") in order to take advantage of the flourishing market. As such, during the three months period ended 30 June 2004, the Group completed two film projects namely, "Breaking News" 「大事件」 and "Throw Down" 「柔道龍虎榜」。No film project was completed in the corresponding period in 2003.

The turn-around from an operating loss of approximately HK\$3.6 million for the three months period ended 30 June 2003 to a net profit of approximately HK\$2.3 million in current period was attributable to the high turnover during the period although other operating expenses increased by approximately HK\$0.7 million as compared to the corresponding period in 2003. The increase in other operating expenses was a result of the combined effect of (i) rise in staff costs due to addition of head count of employees; (ii) increase in depreciation charges due to full quarter effect of filming equipment acquired in the first quarter of the financial year 2003/04; and (iii) reduction of other expenses generally due to effective cost control. Meanwhile, other operating income which mainly consisted of provision of in-house studio post-production service, has dropped, as the in-house studio was occupied for the Group's own production in this quarter leaving insignificant capacity for such kind of service.

Regarding film production, the Group's two productions, titled "Breaking News" 「大事件」 and "Throw Down" 「柔道龍虎榜」 were screened in June and July 2004 respectively and both films achieved encouraging box office receipts. Apart from this, "Breaking News" 「大事件」 has been the Official Selection of 2004 Festival de Cannes held in May 2004 and also been invited to Melbourne International Film Festival and Viennale International Film Festival whereas "Throw Down" 「柔道龍虎榜」 has been invited to Venice Film Festival and Toronto Film Festival.

PROSPECTS

The continuing rebound of the consumer market and the indication of the ending of deflation in the economy as a whole according to recent statistics have impacted favourably on the film industry. The Group will benefit from the promising future of the film industry. However, the ending of deflation also means that greater effort on cost control has to be devoted by the Group. The Group will continue to invest in film production equipment in the foreseeable future in order to enhance its productivity and to reduce the reliance on third parties in providing such equipment. Apart from the cost side, the Group will concentrate on its core business of film production and, at the same time, identify and capture every business opportunity arising which is beneficial to its shareholders.

Regarding the film projects to be produced under the master production agreements signed with various film companies before the listing of the Company's shares on the GEM of the Stock Exchange, the two film projects completed in this quarter were all related to those under the said master production agreements. At the date of this report, the Group has substantially completed another film project with another film company. Such film project is targeted to be completed in the second quarter of the financial year 2004/05. At present, several other film projects are in the pre-production phases.

Looking ahead, the Group will devote its resources in film production and for the sake of better utilisation of its resources, the Group will provide facilities support service to outsider companies provided that the Group's own production schedules are not affected. The Directors believe that this arrangement will be in the best interest of the Company and its shareholders.

In this quarter, the Group has successfully raised approximately HK\$6 million before deducting expenses by issuing 161 million of new shares of the Company. With the enlarged capital base, the Group's strengthened financial position provides a platform for the Group to identify and undertake other possible film related business opportunities which are value-added to the Group as a whole.

UNAUDITED FIRST QUARTERLY RESULTS

The unaudited consolidated results of the Group for the three months ended 30 June 2004 together with the comparative unaudited figures for the corresponding period in 2003 are set out as follows:–

	Notes	For the three months ended 30 June	
		2004 Unaudited HK\$'000	2003 Unaudited HK\$'000
Turnover	2	25,800	–
Cost of sales and services		(19,013)	–
Gross profit		6,787	–
Other operating income		8	148
Other operating expenses		(4,456)	(3,716)
Profit/(Loss) from operations		2,339	(3,568)
Finance charges on finance leases		(3)	(9)
Profit/(Loss) before taxation		2,336	(3,577)
Taxation	3	–	–
Net profit/(loss) attributable to shareholders		2,336	(3,577)
Dividend	4	–	–
Earnings/(Loss) per share	5		
Basic		HK0.31 cents	(HK0.57 cents)
Diluted		N/A	–

Notes

1. **Basis of preparation**

The unaudited results of the Group have been prepared under the historical cost convention and in accordance with accounting principles generally accepted in Hong Kong and the applicable disclosure requirements of the GEM Listing Rules.

2. **Turnover**

The principal activities of the Group are the provision of film production and TV movies production services. The turnover in both periods represents revenue from film production.

3. **Taxation**

No provision for Hong Kong Profits Tax has been made for the three months ended 30 June 2004 (2003: Nil) as the tax losses brought forward from previous years exceed the estimated assessable profits for the period. The Group had no estimated assessable profits for the three months ended 30 June 2003.

No deferred tax charge/credit was recognised as the amount involved has been insignificant.

4. **Dividend**

The Directors do not recommend the payment of any dividend for the three months ended 30 June 2004 (2003: Nil).

5. Earnings/(Loss) per share

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

	For the three months ended 30 June	
	2004 HK\$'000	2003 HK\$'000
Profit/(loss) for the period		
Profit/(loss) for calculating basic and diluted earnings/(loss) per share	2,336	(3,577)
Number of shares		
Weighted average number of ordinary shares used in the calculation of basic earnings/(loss) per share	760,769,231	627,200,000
Effect of dilutive potential ordinary shares	N/A	–
Weighted average number of ordinary shares used in the calculation of diluted earnings/(loss) per share	N/A	627,200,000

No diluted earnings per share was presented for the period as there were no potential dilutive ordinary shares in issue during the three months ended 30 June 2004. No diluted loss per share for the three months ended 30 June 2003 was presented as the share options exercised during that period would result in a decrease in net loss per share.

6. Movement of reserves

	Share premium HK\$'000	Contributed surplus HK\$'000	Retained earnings/ (Accumulated losses) HK\$'000	Total HK\$'000
At 1 April 2004	11,387	10	(7,543)	3,854
Issue of shares	4,347	-	-	4,347
Shares issue expenses	(683)	-	-	(683)
Profit for the three months ended 30 June 2004	-	-	2,336	2,336
At 30 June 2004	15,051	10	(5,207)	9,854
At 1 April 2003	11,387	10	3,245	14,642
Loss for the three months ended 30 June 2003	-	-	(3,577)	(3,577)
At 31 June 2003	11,387	10	(332)	11,065

OTHER INFORMATION

1. DIRECTORS' AND CHIEF EXECUTIVE'S INTERESTS AND SHORT POSITIONS IN SHARES, UNDERLYING SHARES AND DEBENTURES

At 30 June 2004, the interests and short positions of the Directors and the chief executive of the Company in the shares of the Company and any of its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance (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 required standards of dealing by directors of the listed issuer as referred to in Rule 5.46 of the GEM Listing Rules, were as follows:

Name of Director	Personal Interests	Family Interests	Corporate Interests	Other Interests	Total	%
Mr. Law Sau Yiu, Dennis	-	-	357,000,000 (Note)	-	357,000,000	44.35
Ms. Teng Chia Lin, Chialina	-	-	357,000,000 (Note)	-	357,000,000	44.35

Note:

These shares are held 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 Right Opportune Limited.

Save as disclosed above, at 30 June 2004, none of the Directors or chief executives of the Company had any interests or short positions in the 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 required standards of dealing by directors of the listed issuer as referred to in Rule 5.46 of the GEM Listing Rules.

2. SHARE OPTIONS SCHEMES

The Company adopted two share option schemes on 2 August 2002, namely, the pre-IPO share option scheme ("Pre-IPO Share Option Scheme") and the share option scheme ("Share Option Scheme"). The principal terms of the two share option schemes have been set out in the note 22 to the financial statements as included in the annual report of the Company for the year ended 31 March 2004.

Pre-IPO Share Option Scheme

Following the exercise in prior years of all the share options granted to option holders, there are no outstanding share options granted under the Pre-IPO Share Option Scheme. In addition, the right to offer or grant further share options under the Pre-IPO Share Option Scheme was terminated upon the listing of the Company's shares on the GEM. Accordingly, the Pre-IPO Share Option Scheme was effectively terminated upon the exercise of all share options by all the option holders.

Share Option Scheme

At 30 June 2004, no options under the Share Option Scheme had been granted.

3. SUBSTANTIAL SHAREHOLDERS

At 30 June 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:

Name of shareholder	Number of shares held	% of the Company's issued share capital
Right Opportune Limited	357,000,000 (Note a)	44.35
Grand Sum Assets Limited	59,500,000	7.39
Ms. Lee Po Yi, Shirley Anne	59,500,000 (Note b)	7.39

Notes:

- (a) Please refer to note disclosed above in respect of Directors and chief executive's interests or short positions in shares, underlying shares and debentures.
- (b) 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.

Save as disclosed above, at 30 June 2004, the Company has not been notified of any persons (other than the Directors or chief executive of the Company) who had interests or short positions in the shares and underlying shares of the Company which were to be recorded in the register required to be kept under Section 336 of the SFO and/or who were directly or indirectly interested in 5% or more of the issued share capital carrying rights to vote in all circumstances at general meetings of any other members of the Group.

4. SPONSOR'S INTEREST

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

As updated and notified by Hantec, neither Hantec nor any of its directors, employees or their associates (as referred to in Note 3 to Rule 6.35 of the GEM Listing Rules) had any interests in the share capital of the Company at 30 June 2004.

5. COMPETING INTERESTS

At 30 June 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 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 irrecoverably 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.

6. COMPLIANCE WITH RULES 5.34 TO 5.45 OF THE GEM LISTING RULES

In the opinion of the Directors, the Company has complied with Rules 5.34 to 5.45 of the GEM Listing Rules concerning board practices and procedures throughout the three months period ended 30 June 2004.

7. PURCHASE, SALE OR REDEMPTION OF LISTED SECURITIES OF THE COMPANY

During the three months ended 30 June 2004, neither the Company nor any of its subsidiaries purchased, sold or redeemed any of the Company's listed securities.

8. AUDIT COMMITTEE

The Company 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. The audit committee has reviewed the Group's unaudited consolidated financial statements for the three months ended 30 June 2004.

By order of the Board
Milkyway Image Holdings Limited
Law Sau Yiu Dennis
Chairman

Hong Kong, 12 August 2004