NETEL TECHNOLOGY (HOLDINGS) LIMITED

(Incorporated in the Cayman Islands with limited liability)

Annual Report 2004

CHARACTERISTICS OF THE GROWTH ENTERPRISE MARKET ("GEM") OF THE STOCK EXCHANGE OF HONG KONG LIMITED (THE "STOCK EXCHANGE")

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

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

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

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CORPORATE INFORMATION

DIRECTORS

James Ang
Yau Pui Chi Maria
Yeung Kam Yuen Roderick*
Li Chi Wing*

* *Independent Non-executive Directors*

COMPANY SECRETARY

Chan Fai Tai

COMPLIANCE OFFICER

James Ang

QUALIFIED ACCOUNTANT

Chan Fai Tai

AUTHORISED REPRESENTATIVES

James Ang
Chan Fai Tai

AUDIT COMMITTEE

Yeung Kam Yuen Roderick
Li Chi Wing

BANKERS

DBS Bank Limited

AUDITORS

Lau & Au Yeung C.P.A. Limited

REGISTERED OFFICE

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

HEAD OFFICE AND PRINCIPAL PLACE OF BUSINESS IN HONG KONG

Room 4102, 41st Floor
Manulife Plaza
The Lee Gardens
33 Hysan Avenue
Causeway Bay
Hong Kong

REGISTRARS *(in Cayman Islands)*

Bank of Butterfield International (Cayman) Ltd.
Butterfield House
68 Fort Street
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George Town
Grand Cayman
Cayman Islands
British West Indies

REGISTRARS *(in Hong Kong)*

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Services Limited
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WEBSITE

http://www.neteltech.com.hk.

CHAIRMAN'S STATEMENT

The macro market environment for telecom voice services especially for end-user sales in calling card business in last year was very competitive and difficult. The situation was worsened by the changes in consumer behaviour of foreign domestic helpers of using more SIM cards/mobile services than calling cards and shifting from using voice services to text SMS services through SIM application. In short, it was a year of challenges and tested the management team how to react to such changes. On calling card business, in addition to the above changes in the consumer behaviour, the consumption pattern of foreign domestic helpers also changed. In the past they would normally go to a particular location such as Central to do their own purchases but now they will gather at local central business district in different areas of Hong Kong on Sunday to consume.

On the other hand, we decided to start the text, content business on the SIM mobile business to serve our existing customers and potential customers such as visitors from China. This is a new business to the Group and hopefully the result of the business can be reflected in the coming quarters.

Since the company has already set up the regional hub in Hong Kong, ie. voice over IP platform, it is more cost effective now to add multi-media services to our existing facilities in order to generate more revenue for the Group. These content, multi-media services are on one hand serving our existing customers and on the other hand exploring new market segments both in Hong Kong and in foreign markets. These services are provided for different applications catering for the market requirements.

In order to cater for the changes in consumer pattern and have a better coverage to serve our customers, our retail vehicle, Lotus Club, has opened more outlets in Yuen Long, Tuen Mun and Mei Foo. The Group decides to reduce the number of existing outlets in prime areas in order to catch up with these changes.

The carrier sales business is growing and the Group has developed more new operators in foreign countries as business partners during last year. On the other hand, based on the existing carrier sales customer base, the management team will evolve into the content and multi-media business for the Group.

In short, last year was a challenging year to our calling card business but it was also a year of opportunities that helped and pushed us to evolve into a multi-media application telecom provider. We can further utilize our existing equipments, facilities, customer base, business network and the experiences of the management team. So, next year will be a year of changes.

I believe, after the last couple of months of hard works and changes, the Group will be in a better shape heading towards our new direction and growth area and I am optimistic with our potential and future earning capability.

Finally, I would like to thank our colleagues who contributed to the evolution of the business by working very hard, being flexible and reacting to the market changes. I do believe we have now an energetic and experienced team to cater for future growth.

James Ang
Chairman

Hong Kong, 25th August 2004

MANAGEMENT DISCUSSION AND ANALYSIS

RESULTS FOR THE YEAR

During the year ended 31st May 2004, the Group recorded a loss for the year of HK$18.5 million as compared to a loss of HK$9.4 million for the last year. The Group's total turnover was HK$52.8 million, an increase of 14.6% as compared with last year. The increase in loss for the year was the results of the decrease in the total gross profit due to a change of sales mix of end-user direct sales and carrier sales, and the increase in the administrative expenses in anticipation of the business expansion. During the year, the end-user direct sales turnover, which offered a much higher gross profit margin than the carrier sales, decreased by 29% as compared with last year.

The carrier sales business became substantial in the revenue as it accounted for HK$23 million or 43.4% of the Group's turnover for the year, as compared with the HK$3.7 million or 8% for the previous year. The turnover from end-user direct sales business for this year decreased from HK$42.4 million for the last year to HK$29.9 million. As the carrier sales business could only contribute a very thin gross profit margin, the overall gross profit was hence affected.

Despite the provision for doubtful debt was HK$7 million less than the previous year, other administrative expenses increased by HK$4.3 million. The increase was mainly attributable to the increase in depreciation by HK$0.7 million following the addition of a new switch. The rental of outlets and office increased by HK$1.8 million as we opened two more outlets and we moved to a new head office at the beginning of the year. The staff costs also increased by HK$1.7 million as a result of the increase in the number of front line marketing and sales staffs.

BUSINESS REVIEW

During the year, the carrier sales business and end-user direct sales business through prepaid calling cards were the two main business lines for the Group. The mobile SIM card business did not generate significant income as most of the Group's efforts were focused on the calling cards and carrier sales businesses. Total outgoing minutes for the year has risen from 50.7 million minutes in last year to 72.4 million minutes, represented an increase of 42.8%, and was mainly attributable to the increase in the outgoing minutes of carrier sales business.

End-user direct sales

The market for the calling card business was so difficult during the year. Facing fierce competition especially from the Philippines operators, selling price continued to decline and it was difficult to maintain the same profit margin as last year. Total outgoing minutes were 42.2 million minutes in this year, which was slightly higher than the 40 million minutes in last year. However sales turnover decreased from HK$42.4 million of last year to HK$29.9 million of this year, reflecting a significant drop in the unit price.

In response to the change in consumer behaviour of the foreign domestic helpers in Hong Kong, the location strategy of our retail outlets, Lotus Club was adjusted. We have opened and will continue to open Lotus Club outlet in local central districts of different areas in Kowloon, Hong Kong and the New Territories where foreign domestic helpers gathered on their holidays. We have relocated our outlet in Central to a new address with less rental. Operating costs of new outlets at outer districts were comparatively low and the Group could be benefited from having a better coverage on the targeted market.

Carrier Sales

The turnover from carrier sales business was encouraging although the gross profit margin of which was slim. Total outgoing minutes rose from 10.7 million in last year to 29.8 million in this year. Although the outgoing minutes for the fourth quarter was only 4.2 million minutes, being half of the previous quarter, we expect the outgoing minutes will resume to normal and continue to grow at a remarkable rate in the following months. The turnover from carrier sales business also rose from HK$3.7 million in last year to HK$23 million in this year.

FINANCIAL REVIEW

Liquidity and Financing

Although the Group incurred HK$18.5 million loss for the year, the net cash outflow from operations was only HK$1 million, which was attributable to a decrease in receivables by HK$5.8 million and increase in payables by HK$8.3 million. Together with certain repayment of bank financing, the net decrease in cash and cash equivalents was HK$1.7 million for the year.

As a result of the repayment of bank and other loan financing, interest payment for the year decreased from HK$0.4 million in last year to HK$0.3 million. As at 31st May 2004, the Group had a negative cash and cash equivalent balance of HK$1.3 million. The total balance of bank financings as at 31st May 2004 was HK$2.5 million, which comprised of bank overdrafts of HK$1.8 million being secured by pledged bank deposits, and bank term loan of HK$0.7 million being secured by guarantees from certain Directors. In addition, the Group had total obligations under finance lease of HK$1.8 million which was substantially in short-term nature and secured by fixed assets of the Group. The borrowings gearing ratio, defined as total bank and finance lease borrowings divided by the shareholders' fund as at 31st May 2004 was not applicable as there was negative shareholders' fund (0.43 as at 31st May 2003). The net current liabilities position of the Group as at 31st May 2004 was worsened because of the operating loss. The Group had net current liabilities of HK$17.4 million as at 31st May 2004 as compared with net current assets of HK$2.6 million as at 31st May 2003.

Most of the transactions of the Group are denominated in US Dollars and HK Dollars. As the exchange rate of US Dollar is fairly stable, the Board is of the view that the exposure to foreign currency exchange risk is limited. Hence, no hedging or other arrangements to reduce the currency risk have been implemented.

BUSINESS OUTLOOK

The end-user direct sales – calling card business for foreign domestic helpers market will still be very competitive, especially for the Philippines calling cards in Hong Kong. However, with anticipation of certain reduction in the IDD traffics costs in the coming year, and more loyalty programs and offerings to be launched in our retail outlets – Lotus Club, we hope both the turnover and gross profit margin for calling card business can be improved.

We are optimistic on the carrier sales business as we have decided to refocus on this business and established a sophisticated business network with our telecom business partners since last year. We hope the carrier sales business can be doubled in the coming year with a better profit margin.

Apart from the existing lines of business, we will start the mobile phone content offering and multi-media service business. By leveraging our strong business relations in the Philippines, we have developed co-operating relationships with relevant the Philippines mobile phone content providers and well established mobile solution software houses for enhancing our SMS and multi-media applications. Supported by our well established retail network in Hong Kong for the foreign domestic workers, we believe there will be a great potential in this new business development.

After the year end, the Company raised HK$6 million by issuing 6,230,000 new shares of the Company to one of the Philippines investors. This indicates that our Group's existing business and new business opportunities are promising.

EMPLOYEE INFORMATION

As at 31st May 2004, the Group employed a total of 35 (2003: 28) employees including Directors. The salaries and benefits of the Group's employees are kept at a competitive level and employees are rewarded on a performance-related basis within the general framework of the Group's salary and bonus system, which is reviewed annually. The Group also operates a share option scheme where options to subscribe for shares of the Company may be granted to the executive Directors and full-time employees of the Group. As at 31st May 2004, no share options have been granted under the share option scheme.

CONTINGENT LIABILITIES

As at 31st May 2004, the Company had given unconditional guarantee to a third party to secure the due payment of rental expenses payable by a subsidiary to the extent of HK$1,668,000 (2003: Nil).

COMPARISON OF BUSINESS OBJECTIVES WITH ACTUAL BUSINESS PROGRESS

Business objectives as stated in the Prospectus		Actual Business Progress
1. Research & development		
Technological advancement	Research on H.323 protocols running with NVP	NVP was tested and was successfully running in the Philippines and Hong Kong.
	Site visits to major telecommunications equipment manufacturers	Taiwan and Korea telecommunication equipment manufacturers had been visited in this financial year.
	Recruitment of 1 additional technical staff in telecommunications field	An additional technical staff was recruited.
2. Products & service enhancement		
Network infrastructure & facilities	Install 2 VoIP gateways in Singapore and Malaysia	The Group had installed 2 VoIP gateways in Singapore and Malaysia.
Customer Premises Equipment (CPE)	Upgrade system to remote video monitoring and image transmission	The Group had deployed a remote video monitoring in Chai Wan site.
	Provide value-added services of conferencing function to current users	Value-added services to current users had been deployed in Lotus Club outlets.
3. Sales & marketing		
Expanding geographical coverage and widening distribution network	Expand and refurnish existing Lotus Club outlets	Existing Lotus Club outlets had been expanded and refurnished. NVP had been upgraded to connect with the switch.
	Maintain number of distributors at approximately 750	As at 31st May 2004, the Group had approximately 800 distributors.

Business objectives as stated in the Prospectus		Actual Business Progress
Product launching	Perform road shows to corporate and retail users in Taiwan, Japan and South Korea to promote NVP	The Group had performed road shows in Taiwan, the Philippines, Indonesia and Malaysia.
	Launch a new series of premium cards	More than 10 series of cards were launched.
	Deploy 2 additional sales staff for product promotion	More than 4 sales staff include Lotus Club shopkeepers were employed.
	Establish NVP dealerships and distributorships in South Korea, Japan and other Asian Countries	The Group had already demonstrated NVP to prospective dealers in Asia.
Strengthening brand image	Perform road shows along KCR stations	Since the Group believed that road shows along KCR stations were not the most effective way to reach the Group's target customers, promotion and marketing programmes were performed in the existing Lotus Club outlets.
	Continuous advertising in different media	The Group had continued advertising through different media, e.g. sponsor of a basketball team in the financial year ended 31st May 2004.
	Participate in at least 1 exhibition in Hong Kong or overseas	The Group did not participate in any exhibition in Hong Kong or overseas.
	Conduct at least 3 seminars	Seminars were conducted in the Philippines.
	Distribution of posters and flyers in Hong Kong	The Group has distributed posters and flyers regularly to its distributors in Hong Kong for the Group's over 100 series of prepaid calling cards.
	Enhance content of Venus newspapers and increase publications	The Group has stopped publishing Venus newspaper as it had a limited contribution to its brand image.

USE OF PROCEEDS

During the period from 20th December 2002 to 31st May 2004, the Group has incurred the following amounts to achieve the business objectives as set out in the Prospectus of the Company dated 16th December 2002:

	As stated in the Prospectus HK$'million	**Actual** HK$'million
– Research and development on telecommunication and VoIP technologies	5.0	4.6
– Products and services enhancement and development, and strategic investments	5.0	4.9
– Sales and marketing activities such as promotion activities, product launching and establishment of sales outlets	4.0	3.9
– Repayment of certain short term payables of telecommunication services providers	2.3	2.3
– General working capital for the Group	1.7	1.7
	18.0	17.4

The remaining net proceeds of HK$0.6 million were placed in licensed banks in Hong Kong for future use as identified by the Group's business plans.

The Group originally planned to utilize approximately HK$12 million to achieve its business objectives during the period from 20th December 2002 to 31st May 2004. As illustrated in the above table, the Group has accelerated its use of proceeds and incurred a total of approximately HK$17.4 million for the same period. Save for the aforesaid accelerated use of proceeds, there is no change in the application of proceeds for implementation of business and development strategies as stated in the prospectus of the Company dated 16th December 2002.

DIRECTORS AND SENIOR MANAGEMENT

EXECUTIVE DIRECTORS

Mr. James Ang ("Mr. Ang"), age 45, is the chairman of the Company and the founder of the Group. Mr. Ang is responsible for the business planning on overall development of the Group. He has around 20 years of experience in telecommunications industry. Prior to joining the Group in 1996, he served as a sales manager of Swire Telecom from 1984 to 1986 and was responsible for the establishment of offices in the PRC. After being employed with Swire Telecom, Mr. Ang served as a Director of the telecom division of AT&T from 1986 to 1995 and took charge of its business development in different countries. He obtained an honours diploma in Business and Management from the Hong Kong Baptist College (now the Hong Kong Baptist University) in 1983. He is also a graduate from the University of London with bachelor degree in laws. He was called to the bar in United Kingdom and Hong Kong in 1991 and 1992 respectively.

Ms. Yau Pui Chi Maria ("Ms. Yau"), aged 44, Mr. Ang's spouse, who has more than 18 years of commercial experience, is the vice president of the customer service department of the Group. Ms. Yau obtained an honours diploma in Business and Management from the Hong Kong Baptist College (now the Hong Kong Baptist University) in 1983. After graduation, she has been working in Airland Mattress Co. in charge of marketing and promotion activities in the People's Republic of China ("PRC") and Hong Kong. She also worked in Inni Company as an assistant manager from 1984 to 1990. Since 1989, she has been the Director of Charmfine Investments Limited and is responsible for the sales of accessory products. Ms. Yau is experienced in direct interface with dealers and end-users. Ms. Yau joined the Group in 1999.

INDEPENDENT NON-EXECUTIVE DIRECTORS

Mr. Yeung Kam Yuen Roderick ("Mr. Yeung"), aged 54, has studied Laws in the University of London and obtained his academic qualification of Bachelor of Laws in 1988. He obtained his post-graduate certificate in Laws in the University of Hong Kong in 1989. In 1995, he commenced his own business and had since been the partner of the firm, Yeung & Chan Solicitors. His major areas of practice are conveyancing, civil and criminal litigation. Mr. Yeung is also a member of the Institute of Housing of the United Kingdom since 1978 and was qualified as a member of the Law Society of England in 1992.

Mr. Li Chi Wing ("Mr. Li"), aged 45, obtained an honours diploma in Business and Management from the Hong Kong Baptist College (now the Hong Kong Baptist University) in 1983. After graduation, he worked as a sales executive in RCL Semiconductors Limited until 1986. He then joined Wellchem Pharmaceutical Limited and worked as a medical retailer for a year. From 1987 to 1990, he served as a senior marketing executive in KCL Electronics Co. and was responsible for promoting products and formulating marketing plans and proposals. From 1991 to 2004, Mr. Li was appointed as the assistant marketing manager in Ling Kee Publishing Company Limited. Since April 2004, Mr. Li became a consultant of a local trading company.

SENIOR MANAGEMENT

Mr. Lam Chiu Wai ("Mr. Lam"), aged 36, is the vice president of the technical department of the Group. Mr. Lam oversees the research and development division of the Group and is responsible for the development of and the integration of the Group's telecommunication system. He has almost 10 years of experience in the development and the integration of telecommunication platform. Prior to joining the Group in 1996, he joined EIZO Corporation Ltd. in Japan in 1992 as a research and development engineer. In 1993, he worked as a software engineer in Kontel Engineering & Consultants. Mr. Lam obtained a bachelor degree in electronic engineering from the Hong Kong Polytechnic (now The Hong Kong Polytechnic University) in 1992.

Mr. Woo Moon Yuen ("Mr. Woo"), aged 28, is the vice president of the sales department of the Group and is responsible for the sales development of telecommunication services with the telecommunication carriers and the sales activities of the Group's prepaid telephone cards business. Prior to joining the Group in November 2000, Mr. Woo was responsible for the sales and marketing management of telephone cards business, in a local ETS operator, Asia Touch International Co., Ltd. since April 2000. He obtained a bachelor degree in business administration from Clayton University in 1999.

Mr. Chan Fai Tai ("Mr. Chan"), aged 34, is the qualified accountant and the Company Secretary of the Group. He is responsible for the accounting and finance functions of the Group. He is an associate member of the Association of Chartered Certified Accountants, United Kingdom and associate member of the Hong Kong Society of Accountants. Mr. Chan has over ten years' working experience in auditing , accounting and finance fields. He joined the Group in April 2003.

REPORT OF THE DIRECTORS

The Directors have pleasure in submitting their report with the audited accounts for the year ended 31st May 2004.

PRINCIPAL ACTIVITIES AND GEOGRAPHICAL ANALYSIS OF OPERATIONS

The principal activity of the Company is investment holding. The activities of the subsidiaries are set out in note 12 to the accounts.

An analysis of the Group's performance for the year by business and geographical segments is set out in note 3 to the accounts.

RESULTS AND APPROPRIATIONS

The results of the Group for the year are set out in the consolidated profit and loss account on page 21.

The Directors do not recommend the payment of a dividend.

RESERVES

Movements in the reserves of the Group and the Company during the year are set out in note 20 to the accounts.

FIXED ASSETS

Details of the movements in fixed assets of the Group are set out in note 11 to the accounts.

SHARE CAPITAL

Details of the movements in share capital of the Company are set out in note 19 to the accounts.

DISTRIBUTABLE RESERVES

Distributable reserves, including share premium, of the Company at 31st May 2004, amounted to HK$1,828,000 (2003: HK$8,599,000). Under Section 34 of the Cayman Companies Law and the Articles of Association of the Company, the share premium is available for distribution to shareholders subject to the provisions of the Articles of Association of the Company, and a distribution may be paid to shareholders when the Company shall be able to pay its debt as they fall due in the ordinary course of business.

PRE-EMPTIVE RIGHTS

There is no provision for pre-emptive rights under the Company's Articles of Association and there is no restriction against such rights under the laws of the Cayman Islands.

FIVE YEAR FINANCIAL SUMMARY

A summary of the results and of the assets and liabilities of the Group for the last five financial years is set out on page 54.

PURCHASE, SALE OR REDEMPTION OF SECURITIES

The Company has not redeemed any of its shares during the year. Neither the Company nor any of its subsidiaries has purchased or sold any of the Company's shares during the year.

SHARE OPTIONS

Pursuant to written resolution of the sole shareholder of the Company dated 4th December 2002, the Company has conditionally adopted the Share Option Scheme whereby eligible participants of the scheme who the Board considers, in its sole discretion, have contributed to the Group, may be granted option to subscribe for shares.

As at 31st May 2004, no share option was granted under the Share Option Scheme.

DIRECTORS

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

Mr. James Ang
Ms. Yau Pui Chi Maria
Mr. Yeung Kam Yuen Roderick
Mr. Li Chi Wing

In accordance with Article 87 of the Company's Article of Association, Mr. James Ang retires by rotation and, being eligible offer himself for re-election.

Mr. Yeung Kam Yuen Roderick and Mr. Li Chi Wing are independent non-executive Directors and were appointed for a two-year term expiring on 23rd November 2004 and 25th November 2004 respectively.

DIRECTORS' SERVICE CONTRACTS

Each of Mr. James Ang and Ms. Yau Pui Chi Maria has entered into a service contract with the Company for an initial term of three years commencing from 25th November 2002, and which may be terminated by either party not less than three months' prior notice in writing so as to expire not earlier than 31st May 2005.

Under the above service contracts, each of Mr. James Ang and Ms. Yau Pui Chi Maria are entitled to a fixed salary of HK$600,000 and HK$480,000 per annum subject to an annual increment as approved by the Board. Each of the executive Directors will also be entitled to all reasonable out-of-pocket expenses.

During the year, total emoluments, including bonus, paid and payable to the executive Directors amounted to approximately HK$1,504,000 (2003: HK$1,430,000).

Save as disclosed above, none of the Directors has entered into any service agreements with any members of the Group.

DIRECTORS' INTERESTS IN CONTRACTS

Apart from those disclosed in note 24 to the accounts, no contracts of significance in relation to the Group's business to which the Company, its subsidiaries or its holding company 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.

DIRECTORS' INTERESTS AND CHIEF EXECUTIVES' INTERESTS IN AND SHORT POSITIONS IN THE SHARES, UNDERLYING SHARES AND DEBENTURES OF THE COMPANY OR ANY ASSOCIATED CORPORATION

At 31st May 2004, apart from the details as follows, the Directors and chief executive do not have any other interests and short positions in the shares, underlying shares and debentures of the Company and its associated corporations (within the meaning of the Securities and Futures Ordinance ("SFO")), as recorded in the register maintained by the Company under Section 352 of the SFO or as notified to the Company:

Ordinary shares of HK$0.01 each in the Company

		Number of Share held		
Name of Directors		**Family interest**	**Corporate interest**	**Percentage**
Mr. James Ang	Long position	–	204,272,000 *(Note)*	53.76%
Ms. Yau Pui Chi, Maria	Long position	204,272,000 *(Note)*	–	53.76%

Note: These Shares are registered as to 192,200,000 Shares in the name of Nanette Profits Limited ("Nanette"), 5,692,000 Shares in the name of Benevolent Trading Limited ("Benevolent") and 6,380,000 Shares in the name of Cyber Wealth Company Group Limited ("Cyber Wealth"). Mr. Ang is the beneficial owner of the entire issued share capital of Nanette, Benevolent and Cyber Wealth and is deemed to be interested in the shares registered in the name of such companies.

SUBSTANTIAL SHAREHOLDERS' INTERESTS AND SHORT POSITIONS IN THE SHARES, UNDERLYING SHARES OF THE COMPANY

The register of substantial shareholders maintained by the Company under Section 336 of the SFO shows that as at 31st May 2004, the Company had been notified of the following substantial shareholders' interests, being 5% or more of the Company's issued share capital. These interests are in addition to those disclosed above in respect of the Directors and Chief Executives.

Name of Shareholders		Corporate interest	Percentage
LeeMah Holdings, Ltd	Long position	11,244,000	2.96%
Mr. Mah Bing Hong	Long position	11,244,000	2.96%
		22,488,000	5.92%

Note: LeeMah Holdings, Ltd is wholly owned by LeeMah Corporation which is owned as to 98.62% by Mah Family Partnership in which Mr. Mah Bing Hong is the beneficial owner. Mr. Mah Bing Hong is deemed to be interested in 11,244,000 shares held by LeeMah Holdings, Ltd.

MANAGEMENT CONTRACTS

No contracts concerning the management and administration of the whole or any substantial part of the business of the Company were entered into or existed during the year.

MAJOR CUSTOMERS AND SUPPLIERS

The percentages of purchases and sales for the year attributable to the Group's major suppliers and customers are as follows:

Purchases	
– the largest supplier	14.9%
– five largest suppliers combined	50.7%

During the year, the Group sold less than 30% of its goods and services to its 5 largest customers.

None of the Directors, their associates or any shareholders (which to the knowledge of the Directors owns more than 5% of the Company's share capital) had an interest in the major suppliers noted above.

CONNECTED TRANSACTIONS

Significant related party transactions entered by the Group during the year ended 31st May 2004, which constitute exempted connected transactions under the Rules Governing the Listing of Securities on the GEM ("GEM Listing Rules"), are disclosed in note 18 and 24 to the accounts.

BOARD PRACTICES AND PROCEDURES

Throughout the year, the Company was in compliance with the Board Practices and Procedures as set out in rules 5.28 to 5.39 of the GEM Listing Rules.

AUDIT COMMITTEE

The written terms of reference which describe the authority and duties of the Audit Committee were prepared and adopted with reference to "A Guide for the Formation of An Audit Committee" published by the Hong Kong Society of Accountants.

The Audit Committee provides an important link between the Board and the Company's auditors in matters coming within the scope of the Group's audit. It also reviews the effectiveness of both the external and internal audit and of internal controls and risk evaluation. The Committee comprises two independent non-executive Directors, namely, Mr. Yeung Kam Yuen Roderick and Mr. Li Chi Wing. Four meetings were held up to the date of this report.

DIRECTORS' INTEREST IN COMPETING BUSINESS

None of the Directors has an interest in a business which compete or may compete with the business of the Group.

PENSION SCHEMES

The Group did not operate any retirement scheme up to 30th November 2000. With effect from 1st December 2000, a Mandatory Provident Fund scheme (the "MPF scheme") has been set up for employees, including executive Directors, in Hong Kong, in accordance with the Mandatory Provident Fund Scheme Ordinance (the "MPF Ordinance"). Under the MPF scheme, the Group's contributions are at 5% of employees' relevant income as defined in the MPF Ordinance up to a maximum of HK$1,000 per employee per month. The employees also contribute a corresponding amount to the MPF scheme from 31st December 2000 if their relevant income is more than HK$4,000 per month. The contributions are fully and immediately vested with the employees as accrued benefits once they are paid.

SPONSORS' INTEREST

Subsequent to 20th December 2002, the Company's sponsor, Tai Fook Capital Limited ("Tai Fook"), its Directors, employees or associates did not have any interest in the shares of the Company, or any right to subscribe for or to nominate persons to subscribe for the share.

Pursuant to the sponsor's agreement dated 16th December 2002 entered into between the Company and Tai Fook, Tai Fook will receive fee for acting as the Group's retained sponsor for the period from 20th December 2002 to 31st May 2005.

AUDITORS

PricewaterhouseCoopers resigned as joint auditors of the Company on 19th February 2004. Lau & Au Yeung C.P.A. Limited remained as the Company's auditors from that date.

On behalf of the Board
James Ang
Chairman

Hong Kong, 25th August 2004

REPORT OF THE AUDITORS

LAU
AU YEUNG
劉歐陽會計師事務所有限公司
LAU & AU YEUNG C.P.A. LIMITED

Lau & Au Yeung C.P.A. Limited
Room 2701, 27th Floor, Wing On House
71 Des Voeux Road Central
Hong Kong

AUDITORS' REPORT TO THE SHAREHOLDERS OF
NETEL TECHNOLOGY (HOLDINGS) LIMITED
(incorporated in the Cayman Islands with limited liability)

We have audited the accounts on pages 21 to 53 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 accounts which give a true and fair view. In preparing accounts 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 accounts 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 accounts. It also includes an assessment of the significant estimates and judgments made by the Directors in the preparation of the accounts, 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 accounts are free from material misstatement. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the accounts. We believe that our audit provides a reasonable basis for our opinion.

FUNDAMENTAL UNCERTAINTY

In forming our opinion, we have considered the adequacy of the disclosures made in note 1 to the accounts which explains the basis of preparation of the accounts. The accounts have been prepared on a going concern basis, the validity of which depends upon the generation of sufficient working capital from the Group's future operations and the completion of a share subscription agreement as explained in note 25 to the accounts. The Directors, after careful review of the cash generated from the subscription of the Company's shares by an investor and other significant factors that would affect the future cash flows of the Group, have concluded that the preparation of the accounts on a going concern basis is appropriate. We consider that appropriate disclosures have been made and our opinion is not qualified in this respect.

OPINION

In our opinion, the accounts give a true and fair view of the state of affairs of the Company and of the Group as at 31st May 2004 and of the Group's loss and cash flows for the year then ended and have been properly prepared in accordance with the disclosure requirement of the Hong Kong Companies Ordinance.

Lau & Au Yeung C.P.A. Limited
Certified Public Accountants
Hong Kong, 25th August 2004

Franklin Lau Shiu Wai
Director
Practising Certificate Number P1886

CONSOLIDATED PROFIT AND LOSS ACCOUNT

For the year ended 31st May 2004

	Note	**2004** **HK$'000**	2003 HK$'000
Turnover	3	**52,829**	46,096
Cost of sales		**(50,937)**	(31,583)
Gross profit		**1,892**	14,513
Other revenues	3	**235**	50
Selling and marketing expenses		**(1,261)**	(1,818)
Administrative expenses		**(19,075)**	(21,704)
Operating loss	4	**(18,209)**	(8,959)
Finance costs	5	**(272)**	(399)
Loss for the year		**(18,481)**	(9,358)
Loss per share	8	**(4.9 cents)**	(2.6 cents)

CONSOLIDATED BALANCE SHEET

As at 31st May 2004

	Note	2004 HK$'000	2003 HK$'000
Fixed assets	11	**10,458**	9,888
Current assets			
Inventories	13	**463**	456
Accounts and other receivables	14	**4,949**	10,702
Pledged bank deposits	18	**1,936**	3,936
Bank balances and cash		**585**	2,291
		7,933	17,385
Current liabilities			
Accounts and other payables	15	**21,450**	11,937
Due to a Director	16	**328**	15
Current portion of long-term liabilities	17	**1,687**	1,012
Bank overdrafts, secured	18	**1,850**	1,824
		25,315	14,788
Net current (liabilities)/assets		**(17,382)**	2,597
Total assets less current liabilities		**(6,924)**	12,485
Financed by:			
Share capital	19	**3,800**	3,800
Reserves	20(a)	**(11,555)**	6,926
Shareholders' (deficit)/fund		**(7,755)**	10,726
Non-current liabilities			
Long-term liabilities	17	**831**	1,759
		(6,924)	12,485

Approved and authorised for issue by the Board of Directors on 25th August 2004

James Ang
Director

Yau Pui Chi Maria
Director

BALANCE SHEET

As at 31st May 2004

	Note	2004 HK$'000	2003 HK$'000
Investments in subsidiaries	12	**6,712**	11,013
Current assets			
Other receivables	14	**74**	976
Bank balances and cash		**–**	753
		74	1,729
Current liabilities			
Other payables	15	**1,158**	343
Net current (liabilities)/assets		**(1,084)**	1,386
Total assets less current liabilities		**5,628**	12,399
Financed by:			
Share capital	19	**3,800**	3,800
Reserves	20(b)	**1,828**	8,599
		5,628	12,399

James Ang
Director

Yau Pui Chi Maria
Director

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

As at 31st May 2004

	Note	**2004** **HK$'000**	2003 HK$'000
Total equity as at 1st June		**10,726**	364
Loss for the year	20(a)	**(18,481)**	(9,358)
Waiver of amount due to RGL	20(a)	**–**	1,989
Issuance of shares by the Company	19	**–**	22,800
Share issuance expenses	20(a)	**–**	(5,069)
Total equity as at 31st May		**(7,755)**	10,726

CONSOLIDATED CASH FLOW STATEMENT

For the year ended 31st May 2004

	Note	2004 HK$'000	2003 HK$'000
Net cash outflow incurred by operations	21(a)	**(725)**	(17,941)
Interest paid		**(272)**	(399)
Net cash outflow from operating activities		**(997)**	(18,340)
Investing activities			
Purchase of fixed assets		**(1,664)**	(1,898)
Proceeds from sale of fixed assets		**–**	252
Interest received		**43**	50
Decrease/(increase) in pledged bank deposits		**2,000**	(936)
Net cash inflow/(outflow) from investing activities		**379**	(2,532)
Net cash outflow before financing		**(618)**	(20,872)
Financing activities	21(b)		
Issuance of shares		**–**	29,357
Inception of bank loans		**500**	259
Repayment of bank loans		**(328)**	(2,255)
Decrease in trust receipt loans		**–**	(2,241)
Repayment of capital elements of finance leases		**(1,286)**	(1,814)
Net cash (outflow)/inflow from financing		**(1,114)**	23,306
(Decrease)/increase in cash and cash equivalents		**(1,732)**	2,434
Cash and cash equivalents at 1st June		**467**	(1,967)
Cash and cash equivalents at 31st May		**(1,265)**	467
Analysis of balances of cash and cash equivalents			
Bank balances and cash		**585**	2,291
Bank overdrafts		**(1,850)**	(1,824)
		(1,265)	467

1. BASIS OF PREPARATION AND GROUP REORGANISATION

(a) The accounts have been prepared on a going concern basis, the Group had incurred a loss attributable to shareholders of HK$18.5 million and net cash outflow of HK$1 million from operations for the year ended 31st May 2004, and as at 31st May 2004, the Group had net current liabilities and net liabilities of HK$17.4 million and HK$7.8 million respectively. In preparing the accounts, the Directors have carefully reviewed the Group's cash position as at the balance sheet date and the cash flow forecast for the next twelve months. In reviewing the Group's cash flows, the Directors have considered the following factors:

- funds to be generated from the subscription of new shares of the Company pursuant to a subscription agreement date 23rd August 2004 as detailed in note 25 to the accounts;
- cash to be generated from new revenue source and new business development;
- commitment on continuous development and improvement of the Group's products and services; and
- the cost control measures.

The Directors believe that the Group is able to meet its financial obligations in full as and when they fall due and consider that the preparation of accounts on a going concern basis is appropriate.

(b) The Company was incorporated in the Cayman Islands on 9th September 2002 as an exempted Company with limited liability under the Companies Law, Cap. 22 (Law 3 of 1961, as consolidated and revised), of the Cayman Islands (the "Cayman Companies Law").

(c) Pursuant to a group reorganisation (the "Reorganisation") in preparation for the listing of the shares of the Company on the Growth Enterprise Market of The Stock Exchange of Hong Kong Limited ("GEM"), the Company acquired the entire issued share capital of Netel Phone Limited through a share swap and became the holding Company of the Group. Details of the Reorganisation are set out in the prospectus of the Company dated 16th December 2002. The Company's shares were listed on GEM on 20th December 2002.

(d) The Reorganisation is accounted for using merger accounting as permitted by Statement of Standard Accounting Practice ("SSAP") 2.127, "Accounting for group reconstructions". The consolidated accounts of the Group for the year ended 31st May 2003, are prepared as if the Company had been the holding company of the Group from the beginning of the earliest period presented.

(e) The accounts have been prepared in accordance with accounting principles generally accepted in Hong Kong and comply with accounting standards issued by the Hong Kong Society of Accountants ("HKSA"). They have been prepared under the historical cost convention.

1. BASIS OF PREPARATION AND GROUP REORGANISATION *(Continued)*

(f) In the current year, the Group adopted the following revised SSAPs issued by the HKSA which are effective for accounting periods commencing on or after 1st January 2003.

SSAP 12 (revised)	:	Income taxes
SSAP 34 (revised)	:	Employee's benefits

The principal accounting policies adopted in the preparation of these accounts and the changes to the Group's accounting policies and the effect of adopting these revised SSAPs are set out in the following paragraphs.

2. PRINCIPAL ACCOUNTING POLICIES

The principal accounting policies adopted in the preparation of these accounts are set out below:

(a) Consolidation

The consolidated accounts include the accounts of the Company and its subsidiaries made up to 31st May.

Subsidiaries are those entities in which the Company, directly or indirectly, controls more than one half of the voting power; has the power to govern the financial and operating policies; to appoint or remove the majority of the members of the board of Directors; or to cast majority of votes at the meetings of the board of Directors.

Apart from the Reorganisation referred to in note 1 above, the results of subsidiaries acquired or disposed of during the year are included in the consolidated profit and loss account from the effective date of acquisition or up to the effective date of disposal, as appropriate.

In the Company's balance sheet, the investments in subsidiaries are stated at cost less provision for impairment losses. The results of subsidiaries are accounted for by the Company on the basis of dividends received and receivable.

(b) Revenue recognition

Revenue in respect of long distance call services provided to customers is recognised upon delivery of the services.

Interest income is recognised on a time proportion basis, taking into account the principal amounts outstanding and the interest rates applicable.

Promotion income is recognised when services are rendered.

2. PRINCIPAL ACCOUNTING POLICIES *(Continued)*

(c) Fixed assets

Fixed assets are stated at cost less accumulated depreciation and accumulated impairment losses, if any, and are depreciated at rates sufficient to write off their cost less accumulated impairment losses over their estimated useful lives to the Group on a straight-line basis. The principal annual rates are as follows:

Leasehold improvements	20%
Furniture and office equipment	20%
Computers and software	33 ⅓ %
Telecommunication equipment	10%

Improvements are capitalised and depreciated over their expected useful lives to the Group.

The gain or loss on disposal of a fixed asset is the difference between the net sales proceeds and the carrying amount of the relevant asset, and is recognised in the profit and loss account.

At each balance sheet date, both internal and external sources of information are considered to assess whether there is any indication that fixed assets are impaired. If any such indication exists, the recoverable amount of the asset is estimated and where relevant, an impairment loss is recognised to reduce the asset to its recoverable amount. Such impairment losses are recognised in the profit and loss account.

(d) Assets under leases

(i) Finance leases

Leases that substantially transfer to the Group all the risks and rewards of ownership of assets are accounted for as finance leases. Finance leases are capitalised at the inception of the leases at the lower of the fair value of the leased assets or the present value of the minimum lease payments. Each lease payment is allocated between the capital and finance charges so as to achieve a constant rate on the capital balances outstanding. The corresponding rental obligations, net of finance charges, are included in long-term liabilities. The finance charge are charged to the profit and loss account over the lease periods.

Assets held under finance leases are depreciated over the shorter of their estimated useful lives or the lease periods.

2. PRINCIPAL ACCOUNTING POLICIES *(Continued)*

(d) Assets under leases *(Continued)*

(ii) Operating leases

Leases where substantially all the risks and rewards of ownership of assets remain with the leasing company are accounted for as operating leases. Payments made under operating leases net of any incentives received from the leasing company are charged to the profit and loss account on a straight-line basis over the lease periods.

(e) Inventories

Inventories comprise telecommunication equipment and long distance call cards and are stated at the lower of cost and net realisable value. Cost, comprises purchase costs, is assigned to individual items on the first-in, first-out basis. Net realisable value is determined on the basis of anticipated sales proceeds less estimated selling expenses.

(f) Accounts receivable

Provision is made against accounts receivable to the extent they are considered to be doubtful. Accounts receivable in the balance sheet are stated net of such provision.

(g) Cash and cash equivalents

Cash and cash equivalents are carried in the balance sheet at cost. For the purposes of the cash flow statement, cash and cash equivalents comprise cash on hand, deposits held at call with banks and bank overdrafts.

(h) Deferred taxation

Deferred taxation is provided in full, using the liability method, on temporary differences arising between the tax bases and their carrying amounts in the accounts. Taxation rates enacted or substantively enacted by the balance sheet date are used to determine deferred taxation.

Deferred tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

In prior years, deferred taxation was accounted for at the current taxation rate in respect of timing differences between profit as computed for taxation purposes and profit as stated in the accounts to the extent that a liability or an asset was expected to be payable or recoverable in the foreseeable future. The adoption of revised SSAP 12 represents a change in accounting policy, which has no significant effect on the Group's results for the prior accounting years.

2. PRINCIPAL ACCOUNTING POLICIES *(Continued)*

(i) Research and development costs

Research costs are expensed as incurred. Costs incurred on development projects relating to the design and testing of new or improved products are recognised as an intangible asset where the technical feasibility and intention of completing the product under development has been demonstrated and the resources are available to do so, costs are identifiable and there is an ability to sell or use the asset that will generate probable future economic benefits. Development costs that do not meet the above criteria are expensed as incurred.

All development costs for the year were charged to the profit and loss account.

(j) Employee benefits

(i) Employee leave entitlements

Employee entitlements to annual leave and long service leave are recognised when they accrue to employees. A provision is made for the estimated liability for annual leave and long-service leave as a result of services rendered by employees up to the balance sheet date.

Employee entitlements to sick leave and maternity leave are not recognised until the time of leave.

(ii) Pension obligations

The Group contributes to a defined contribution retirement scheme which is available to all employees. Contributions to the scheme by the Group and employees are calculated as a percentage of employees' basic salaries. The retirement benefit scheme cost charged to the profit and loss account represents contributions payable by the Group to the scheme. The Group's contributions to the defined contribution retirement scheme are expensed as incurred.

The assets of the scheme are held separately from those of the Group in an independently administered fund.

2. PRINCIPAL ACCOUNTING POLICIES *(Continued)*

(k) Segment reporting

In accordance with the Group's internal financial reporting, the Group has determined that business segments are presented as the primary reporting format and geographical as the secondary reporting format.

Unallocated costs represent corporate expenses. Segment assets consist primarily of fixed assets, inventories, receivables and operating cash. Segment liabilities comprise operating liabilities and exclude items such as taxation and certain corporate borrowings. Capital expenditure comprises additions to fixed assets.

In respect of geographical segment reporting, sales are based on the country in which the customer is located. Total assets and capital expenditure are where the assets are located.

(l) Translation of foreign currencies

Transactions in foreign currencies are translated at exchange rates ruling at the transaction dates. Monetary assets and liabilities expressed in foreign currencies at the balance sheet date are translated at rates of exchange ruling at the balance sheet date. Exchange differences arising in these cases are dealt with in the profit and loss account.

(m) Borrowing costs

All borrowing costs are charged to the profit and loss account during the period in which they are incurred.

3. TURNOVER AND REVENUES

The Group is principally engaged in the provision of long distance call services. Revenues recognised during the year are as follows:

	2004 HK$'000	2003 HK$'000
Turnover		
Long distance call services	**52,829**	46,033
Sale of equipment	**–**	63
	52,829	46,096
Other revenues		
Bank interest income	**43**	50
Promotion income	**155**	–
Sundry income	**37**	–
	235	50
Total revenues	**53,064**	46,146

3. TURNOVER AND REVENUES *(Continued)*

Primary report format – business segments

	2004			
		Long distance call services		
	Sale of equipment	End-user direct sales	Carrier sales	Group
	HK$'000	HK$'000	HK$'000	HK$'000
Turnover	–	29,875	22,954	52,829
Segment results	–	(12,660)	(2,186)	(14,846)
Other revenues				235
Operating loss				(14,611)
Unallocated costs				(3,598)
Finance costs				(272)
Loss attributable to shareholders				(18,481)
Segment assets	–	13,869	3,604	17,473
Unallocated assets				918
				18,391
Segment liabilities	–	14,585	9,258	23,843
Unallocated liabilities				2,303
				26,146
Capital expenditures	–	1,189	1,324	2,513
Unallocated capital expenditures				12
				2,525
Depreciation	–	1,473	344	1,817
Unallocated depreciation				100
				1,917

3. TURNOVER AND REVENUES *(Continued)*

Primary report format – business segments *(Continued)*

		2003 Long distance call services		
	Sale of equipment HK$'000	End-user direct sales HK$'000	Carrier sales HK$'000	Group HK$'000
Turnover	63	42,352	3,681	46,096
Segment results	39	(3,121)	(2,975)	(6,057)
Other revenues				50
Operating loss				(6,007)
Unallocated costs				(2,952)
Finance costs				(399)
Loss attributable to shareholders				(9,358)
Segment assets	46	19,121	3,488	22,655
Unallocated assets				4,618
				27,273
Segment liabilities	–	10,846	4,558	15,404
Unallocated liabilities				1,143
				16,547
Capital expenditures	–	3,404	795	4,199
Unallocated capital expenditures				490
				4,689
Depreciation	–	1,036	177	1,213
Unallocated depreciation				8
				1,221

3. TURNOVER AND REVENUES *(Continued)*

Secondary reporting format – geographical segments

	2004			
	Turnover HK$'000	**Segment results HK$'000**	**Total assets HK$'000**	**Capital expenditures HK$'000**
Hong Kong	**42,685**	**(17,819)**	**17,934**	**1,453**
Mainland China	**47**	**(3)**	**–**	**–**
Other countries	**10,097**	**(622)**	**457**	**1,072**
	52,829	**(18,444)**	**18,391**	**2,525**
Other revenues		**235**		
Loss from operations		**(18,209)**		

	2003			
	Turnover HK$'000	Segment results HK$'000	Total assets HK$'000	Capital expenditures HK$'000
Hong Kong	44,486	(8,809)	26,823	4,689
Mainland China	65	(8)	30	–
Other countries	1,545	(192)	420	–
	46,096	(9,009)	27,273	4,689
Other revenues		50		
Loss from operations		(8,959)		

4. OPERATING LOSS

Operating loss is stated after crediting and charging the following:

	2004 HK$'000	2003 HK$'000
Crediting		
Gain on disposal of fixed assets	–	115
Net exchange gain	8	–
Charging		
Auditors' remuneration	360	860
Cost of inventories sold	3,448	2,661
Depreciation		
– owned fixed assets	1,501	986
– leased fixed assets	416	235
Loss on disposal of fixed assets	38	–
Net exchange losses	–	2
Operating leases in respect of land and buildings	4,349	2,558
Provision for doubtful debts	43	7,029
Staff costs (including Directors' emoluments) *(Note 9)*	7,562	5,846

5. FINANCE COSTS

	2004 HK$'000	2003 HK$'000
Interest on bank loans and overdrafts	93	275
Interest element of finance leases	179	124
	272	399

6. TAXATION

(a) No provision for Hong Kong profits tax has been made in current year as the Group has no estimated assessable profits for the year (2003: Nil).

(b) No deferred taxation has been provided as the Group has no material unprovided deferred tax assets/liabilities which are expected to be crystallized in the foreseeable future (2003: Nil).

(c) The taxation on the Group's profit before taxation differs from the theoretical amount that would arise using taxation rate of the home country of the Group as follows:

	2004	2003
	HK$'000	HK$'000
Loss for the year	**(18,481)**	(9,358)
Calculated at the taxation rate of 17.5%	**(3,234)**	(1,637)
Income not subject to taxation	**(42)**	(1,030)
Expenses not deductible for taxation purposes	**187**	1,809
Tax losses not recognised	**3,050**	1,114
Accelerated depreciation not recognised	**39**	(256)
Taxation charge	**–**	–

7. LOSS ATTRIBUTABLE TO SHAREHOLDERS

The loss attributable to shareholders is dealt with in the accounts of the Company to the extent of HK$6,771,000 (2003: 11,831,000).

8. LOSS PER SHARE

The calculation of basic loss per share is based on the Group's loss for the year of approximately HK$18,481,000 (2003: HK$9,358,000) and the weighted average of 380,000,000 shares in issued during the year (2003: 367,381,918 shares).

Diluted loss per share for the current and prior year is not presented as there is no dilutive instrument granted by the Company.

9. STAFF COSTS (INCLUDING DIRECTORS' EMOLUMENTS)

	2004	2003
	HK$'000	HK$'000
Wages and salaries	**7,329**	5,642
Pension cost – defined contribution plans	**233**	204
	7,562	5,846

10. EMOLUMENTS FOR DIRECTORS AND HIGHEST PAID INDIVIDUALS

(a) Directors' emoluments

The aggregate amount of emoluments paid and payable to the Directors of the Company are as follows:

	2004	**2003**
	HK$'000	HK$'000
Fees	**100**	52
Salaries, allowances and benefits in kind	**1,480**	1,406
Retirement benefit scheme contributions	**24**	24
	1,604	1,482

Each of the two executive Directors of the Company received emoluments for the year ended 31st May 2004 of approximately HK$812,000 (2003: HK$737,000) and HK$692,000 (2003: HK$693,000) respectively.

Each of the two independent non-executive Directors of the Company received emoluments for the year ended 31st May 2004 of HK$50,000 (2003: HK$26,000) and HK$50,000 (2003: HK$26,000) respectively.

None of the directors of the Company waived any emoluments during the current and prior year.

10. EMOLUMENTS FOR DIRECTORS AND HIGHEST PAID INDIVIDUALS *(Continued)*

(b) Five highest paid individuals

The five individuals whose emoluments were the highest in the Group for the year include two (2003: two) Directors whose emoluments are reflected in the analysis presented above. The emoluments payable to the remaining three (2003: three) individuals during the year are as follows:

	2004	**2003**
	HK$'000	HK$'000
Salaries and allowances	**1,175**	992
Retirement benefit scheme contributions	**29**	36
	1,204	1,028

The emoluments fall within the following bands:

	Number of individuals	
	2004	2003
Nil to HK$1,000,000	**3**	3

(c) During the current and prior year, no emoluments were paid by the Group to any of the above Directors or the five highest paid individuals as an inducement to join or upon joining the Group or as compensation for loss of office.

11. FIXED ASSETS

	Group				
	Leasehold improvement HK$'000	Furniture and office equipment HK$'000	Computer and software HK$'000	Telecom-munication equipment HK$'000	Total HK$'000
At cost					
At 1st June 2003	746	1,138	889	10,403	13,176
Additions	105	111	196	2,113	2,525
Disposals	(43)	(20)	–	–	(63)
At 31st May 2004	**808**	**1,229**	**1,085**	**12,516**	**15,638**
Accumulated depreciation					
At 1st June 2003	162	339	340	2,447	3,288
Charge for the year	159	245	282	1,231	1,917
Disposals	(17)	(8)	–	–	(25)
At 31st May 2004	**304**	**576**	**622**	**3,678**	**5,180**
Net book value					
At 31st May 2004	**504**	**653**	**463**	**8,838**	**10,458**
At 31st May 2003	584	799	549	7,956	9,888
Net book value of leased assets:					
At 31st May 2004	**–**	**363**	**–**	**2,700**	**3,063**
At 31st May 2003	–	483	–	2,575	3,058

12. INVESTMENTS IN SUBSIDIARIES

	Company 2004 HK$'000	Company 2003 HK$'000
Unlisted investments at costs *(note (a))*	**6,499**	6,499
Due from subsidiaries *(note (b))*	**14,713**	14,514
Less: Provision for investments in and amounts due from subsidiaries	**(14,500)**	(10,000)
	6,712	11,013

(a) The following is a list of the principal subsidiaries at 31st May 2004:

Name	Place of incorporation	Principal activities and place of operation	Particulars of issued and fully paid share capital	Interest held
Shares held directly:				
Netel Phone Limited ("NPL")	British Virgin Islands ("BVI")	Investment holding in Hong Kong	1,786,000 ordinary shares of US$1 each	100%
Shares held indirectly:				
Netel Technology Limited	Hong Kong	Provision of long distance call services in Hong Kong	10,000 ordinary shares of HK$1 each	100%
Think Gold Assets Limited	BVI	Investment holding in Hong Kong	100 ordinary shares of US$1 each	100%
Pacific Long Distance Telephone Corporation Limited	Hong Kong	Provision of long distance call services and sale of long distance call cards in Hong Kong	10,000 ordinary shares of HK$1 each	100%
Silver Holdings Limited	Hong Kong	Sale of long distance call cards in Hong Kong	2 ordinary shares of HK$1 each	100%

(b) The amounts due are unsecured, interest-free and not repayable within the next twelve months from the balance sheet date.

13. INVENTORIES

	Group	
	2004	2003
	HK$'000	HK$'000
Telecommunication equipment	**28**	200
Long distance call cards	**435**	442
	463	642
Less: provision for slow moving inventories	**–**	(186)
	463	456

As at 31st May 2004, the inventories were stated at cost. As at 31st May 2003, the inventories were stated at net realisable value.

14. ACCOUNTS AND OTHER RECEIVABLES

	Group		Company	
	2004	2003	**2004**	2003
	HK$'000	HK$'000	**HK$'000**	HK$'000
Accounts receivable *(note)*	**2,877**	5,356	**–**	–
Prepayments and deposits	**2,072**	5,346	**74**	976
	4,949	10,702	**74**	976

Note:

The majority of the Group's turnover are entered into on credit terms ranging from 30 to 90 days. The ageing analysis of trade receivable at the respective balance sheet dates is as follows:

	Group	
	2004	2003
	HK$'000	HK$'000
0-30 days	**1,041**	3,426
31-60 days	**634**	1,236
61-90 days	**426**	1,117
91-180 days	**596**	2,503
181-365 days	**478**	1,547
Over 365 days	**6,664**	2,885
	9,839	12,714
Less: provision for doubtful debt	**(6,962)**	(7,358)
	2,877	5,356

15. ACCOUNTS AND OTHER PAYABLES

	Group		Company	
	2004	2003	**2004**	2003
	HK$'000	HK$'000	**HK$'000**	HK$'000
Accounts payable *(note)*	**13,943**	8,492	**–**	–
Accruals and other payables	**5,349**	2,459	**1,158**	343
Receipt in advance	**2,158**	986	**–**	–
	21,450	11,937	**1,158**	343

Note:

The ageing analysis of the accounts payable were as follows:

	Group	
	2004	2003
	HK$'000	HK$'000
0-30 days	**2,994**	2,052
31-60 days	**3,011**	1,411
61-90 days	**1,633**	1,175
91-180 days	**3,456**	1,749
181-365 days	**729**	141
Over 365 days	**2,120**	1,964
	13,943	8,492

16. DUE TO A DIRECTOR

The amount due is unsecured, interest-free and has no fixed terms of repayment.

17. LONG-TERM LIABILITIES

	Group	
	2004	2003
	HK$'000	HK$'000
Bank loans, secured *(note (a))*	**651**	479
Obligations under finance leases *(note (b))*	**1,867**	2,292
	2,518	2,771
Less: current portion of long-term liabilities	**(1,687)**	(1,012)
	831	1,759
The analysis of the above is as follows:		
Wholly repayable within five years	**2,518**	2,771
Current portion of long-term liabilities	**(1,687)**	(1,012)
	831	1,759

(a) At 31st May 2004, the Group's bank loans were repayable as follows:

	Group	
	2004	2003
	HK$'000	HK$'000
Within one year	**396**	130
In the second year	**192**	138
In the third to fifth year	**63**	211
	651	479

Details of securities for banking facilities are set out in note 18 below.

17. LONG-TERM LIABILITIES *(Continued)*

(b) At 31st May 2004, the Group's finance lease liabilities were repayable as follows:

	Group	
	2004	2003
	HK$'000	HK$'000
Within one year	**1,374**	972
In the second year	**525**	827
In the third to fifth year	**60**	637
	1,959	2,436
Future finance charges on finance leases	**(92)**	(144)
	1,867	2,292
The present value of finance lease liabilities is as follows:		
Within one year	**1,291**	882
In the second year	**516**	782
In the third to fifth year	**60**	628
	1,867	2,292

Obligations under finance leases are repayable by equal monthly instalments to 1st November 2006. Interest is charged on the outstanding balances at 7.22% to 9.01%.

These finance leases are secured by corporate guarantees given by the Company, a subsidiary of the Group and personal guarantees given by Mr. Ang and Ms. Yau Pui Chi, Maria ("Ms. Yau"), Directors of the Company. Ms. Yau is the spouse of Mr. Ang.

18. BANKING FACILITIES

As at 31st May 2004, the Group's banking facilities of approximately HK$3,147,000 (2003: HK$4,310,000) were secured by the followings:

(a) joint and several personal guarantees from Mr. Ang and Ms. Yau for HK$6,000,000 (2003: HK$8,000,000);

(b) legal charges over two properties held by Richmond Group Limited ("RGL") and Charmfine Investment Limited ("Charmfine") respectively. Mr. Ang has beneficial interests in RGL and Charmfine is beneficially owned by Mr. Ang and Ms. Yau; and.

(c) a charge over fixed deposits of HK$1,936,000 (2003: HK$3,936,000) held by the Group.

19. SHARE CAPITAL

	Authorised ordinary shares of HK$0.01 each	
	No. of shares	HK$'000
At 31st May 2004	**1,000,000,000**	**10,000**
At incorporation, 9th September 2002	**38,000,000**	380
Increase in authorised share capital	**962,000,000**	9,620
At 31st May 2003	**1,000,000,000**	10,000

	Issued and fully paid ordinary shares of HK$0.01 each	
	No. of shares	HK$'000
At 31st May 2004	**380,000,000**	**3,800**
Issuance of Subscriber's share at incorporation, 9th September 2002	1	–
Issuance of shares for share swap pursuant to the Reorganisation on 4th December 2002	1,785,999	18
Issuance of shares on 19th December 2002	22,800,000	228
Capitalisation issues on 19th December 2002	355,414,000	3,554
At 31st May 2003	380,000,000	3,800

20. RESERVES

(a) Group

	Share premium HK$'000	Merger reserve HK$'000 *(Note)*	Accumulated losses HK$'000	Total HK$'000
At 1st June 2003	13,949	39,307	(46,330)	6,926
Loss for the year	–	–	(18,481)	(18,481)
At 31st May 2004	13,949	39,307	(64,811)	(11,555)
At 1st June 2002	–	39,307	(38,961)	346
Issuance of shares	22,572	–	–	22,572
Share issuance expenses	(5,069)	–	–	(5,069)
Capitalisation issues	(3,554)	–	–	(3,554)
Waiver of amount due to RGL	–	–	1,989	1,989
Loss for the year	–	–	(9,358)	(9,358)
At 31st May 2003	13,949	39,307	(46,330)	6,926

Note: Merger reserve represents the difference between the nominal value of the share capital of subsidiaries acquired and the nominal value of shares issued by the Company. The merger reserve is deemed to have been in existence throughout the accounting periods presented in the consolidated balance sheet in accordance with the basis of presentation referred to in note 1.

20. RESERVES *(Continued)*

(b) Company

	Share premium HK$'000	Accumulated losses HK$'000	Total HK$'000
At 1st June 2003	20,430	(11,831)	8,599
Loss for the year	–	(6,771)	(6,771)
At 31st May 2004	**20,430**	**(18,602)**	**1,828**
At 9th September 2002 *(date of incorporation)*	–	–	–
Amount arising from the Reorganisation *(Note)*	6,481	–	6,481
Issuance of shares	22,572	–	22,572
Share issuance expenses	(5,069)	–	(5,069)
Capitalisation issues	(3,554)	–	(3,554)
Loss for the period	–	(11,831)	(11,831)
At 31st May 2003	20,430	(11,831)	8,599

Note: The amount arising from the Reorganisation of HK$6,481,000 of the Company represents the difference between the consolidated net assets of the subsidiaries and the nominal value of the Company's share issued pursuant to the Reorganisation, and has been credited to the share premium account of the Company.

21. CONSOLIDATED CASH FLOW STATEMENT

(a) Reconciliation of loss for the year to net cash outflow incurred by operations

	2004	2003
	HK$'000	HK$'000
Loss for the year	**(18,481)**	(9,358)
Interest expense	**272**	399
Interest income	**(43)**	(50)
Depreciation	**1,917**	1,221
Loss/(gain) on disposal of fixed assets	**38**	(115)
Operating loss before working capital changes	**(16,297)**	(7,903)
Increase in inventories	**(7)**	(34)
Decrease/(increase) in accounts and other receivables	**5,753**	(1,032)
Increase/(decrease) in accounts and other payables	**8,341**	(9,112)
Increase in amount due to a Director	**313**	15
Increase in receipt in advance	**1,172**	125
Net cash outflow incurred by operations	**(725)**	(17,941)

21. CONSOLIDATED CASH FLOW STATEMENT *(Continued)*

(b) Analysis of changes in financing during the year

	Share capital including share premium and merger reserve	Bank loans and obligations under finance leases	Trust receipt loans
	HK$'000	HK$'000	HK$'000
At 1st June 2003	57,056	2,771	–
Inception of finance leases	–	861	–
Inception of bank loans	–	500	–
Net cash outflow from financing	–	(1,614)	–
At 31st May 2004	**57,056**	**2,518**	**–**
At 1st June 2002	39,325	3,790	2,241
Paid up of shares issued by NPL in last year	(11,626)	–	–
Inception of finance leases	–	2,791	–
Net cash inflow/(outflow) from financing	29,357	(3,810)	(2,241)
At 31st May 2003	57,056	2,771	–

(c) Major non-cash transactions

During the year, the Group entered into finance lease arrangements in respect of assets with a total capital value at the inception of the lease of HK$861,000 (2003: HK$2,791,000).

22. COMMITMENTS UNDER OPERATING LEASES

At 31st May 2004, the Group had future aggregate minimum lease payments under non-cancellable operating leases as follows:

	2004	2003
	HK$'000	HK$'000
Within one year	**3,491**	1,735
In the second to fifth year	**1,969**	1,697
	5,460	3,432

23. CONTINGENT LIABILITIES

At 31st May 2004, the Company had the following contingent liabilities.

(a) The Company had given unconditional guarantee to a third party to secure the due payment of rental expenses payable by a subsidiary to the extent of HK$1,668,000 (2003: Nil).

(b) The Company had contingent liabilities of HK$1,137,000 (2003: Nil) in respect of guarantees for due performance of a subsidiary under finance lease obligations.

24. RELATED PARTY TRANSACTIONS

Save as disclosed in other notes to the accounts, significant related party transactions, which were carried out in the normal course of the Group's business, are as follows:

		Group	
		2004	2003
	Note	**HK$'000**	HK$'000
Rental expenses paid to Charmfine	*(i)*	120	120

Note:

(i) Rental expenses were charged in accordance with the terms of the underlying agreements.

25. POST BALANCE SHEET EVENTS

On 23rd August 2004, the Company entered into a subscription agreement (the "Subscription Agreement") with an existing shareholder of the Company (the "Subscriber") of which the completion is conditional upon the approval by the GEM Listing Committee of the Stock Exchange of Hong Kong Limited. Pursuant to the Subscription Agreement, the Subscriber will subscribe for 6,230,000 new shares at a subscription price of HK$1.00 per share. The net proceeds of approximately HK$6 million are intended to be used for general working capital of the Group.

26. ULTIMATE HOLDING COMPANY

The Directors regard Nanette Profits Limited, a company incorporated in the British Virgin Islands, as being the ultimate holding company.

27. APPROVAL OF ACCOUNTS

The accounts were approved by the board of Directors on 25th August 2004.

FIVE YEAR FINANCIAL SUMMARY

	2004	2003	2002	2001	2000
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Turnover	**52,829**	46,096	69,016	39,437	2,798
(Loss)/profit attributable to shareholders	**(18,481)**	(9,358)	4,599	(13,701)	(29,859)
Assets and liabilities					
Total assets	**18,391**	27,273	31,377	16,074	48
Total liabilities	**(26,146)**	(16,547)	(31,013)	(52,599)	(29,674)
Shareholders' (deficit)/fund	**(7,755)**	10,726	364	(36,525)	(29,626)

The Reorganisation referred to in note 1 to the accounts has been reflected in the five year financial summary by regarding the Company as having been the holding company of the Group from the earliest period presented.