



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 2005

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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.

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HIGHLIGHTS

1. Turnover of the Group for the three months ended 30 June 2005 was approximately HK\$4.0 million representing a decrease of approximately 84.6% as compared to the corresponding period in 2004.
2. Net loss of the Group for the three months ended 30 June 2005 was approximately HK\$7.7 million as compared to a net profit of approximately HK\$2.3 million for the corresponding period in 2004.
3. Loss per share of the Group was approximately HK0.96 cents for the three months ended 30 June 2005 (2004: earnings per share of HK0.31 cents).
4. The Board does not recommend the payment of any dividend for the three months ended 30 June 2005 (2004: HK\$ Nil).

UNAUDITED FIRST QUARTERLY RESULTS

The Directors announce the unaudited consolidated results of Milkyway Image Holdings Limited (the "Company") and its subsidiaries (together, the "Group") for the three months ended 30 June 2005 together with the comparative unaudited figures for the corresponding period in 2004 as follows:-

	Notes	Three months ended 30 June	
		2005 Unaudited HK\$'000	2004 Unaudited HK\$'000
Turnover	2	3,977	25,800
Cost of sales		(5,044)	(19,013)
Gross (loss)/profit		(1,067)	6,787
Other revenue		8	8
Other operating expenses		(6,540)	(4,456)
(Loss)/Profit from operations		(7,599)	2,339
Finance costs		(97)	(3)
(Loss)/Profit before taxation		(7,696)	2,336
Taxation	3	-	-
Net (loss)/profit attributable to shareholders		(7,696)	2,336
Dividend	4	-	-
(Loss)/Earnings per share – Basic	5	HK(0.96) cents	HK0.31 cents

Notes

1. Basis of preparation and significant accounting policies adopted

The unaudited consolidated results of the Group have been prepared under the historical cost convention and in accordance with accounting principles generally accepted in Hong Kong and comply with accounting standards issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA") and the applicable disclosure requirements of the GEM Listing Rules.

The HKICPA has issued a number of new and revised Hong Kong Financial Reporting Standards and Hong Kong Accounting Standards (the "new HKFRSs"), which are effective for accounting periods beginning on or after 1 January 2005. The adoption of the new HKFRSs had no material impact on the Group's results of operations.

During the three months period ended 30 June 2005, the Group adopted the following new significant accounting policies:

(a) *Revenue recognition*

Revenue from the distribution of films is recognised when the master materials have been delivered to customers.

(b) *Film rights*

Film rights represent film produced or acquired by the Group and are stated at cost less accumulated amortisation and any identified impairment losses.

The cost of film rights is amortised in the proportion of actual income earned during the period to the total estimated income after taking into account their estimated residual value. Where there is an impairment in value, the unamortised balance is written down to its estimated recoverable amount. The estimated residual value is reported as a non-current asset.

The portion of film rights expect to be amortised within twelve months from the balance sheet date is reported as current asset. The portion of films rights expected not to amortised within twelve months from the balance sheet date is reported as a non-current asset.

Except for the above, the accounting policies adopted for the preparation of the Group's unaudited consolidated results for the period under review are consistent with those followed in the preparation of the Group's annual financial statements for the year ended 31 March 2005.

2. Turnover

Turnover represents revenue arising from film distribution and provision of film production services.

3. Taxation

No provision for Hong Kong Profits Tax has been made for the three months ended 30 June 2005 (2004: Nil) as the Group had no estimated assessable profits for the period.

No deferred tax asset has been recognised in respect of tax losses due to the unpredictability of future profit streams.

4. Dividend

The Directors do not recommend the payment of any dividend for the three months ended 30 June 2005 (2004: Nil).

5. (Loss)/Earnings per share

The calculation of the basic (loss)/earnings per share is based on the loss attributable to shareholders for the three months ended 30 June 2005 of approximately HK\$7,696,000 (2004: profit attributable to shareholders of approximately HK\$2,336,000) and on 805,000,000 (2004: weighted-average number of 760,769,231) ordinary shares in issue during the period.

There were no potential dilutive ordinary shares in issue during the three months ended 30 June 2005 (2004: Nil). No diluted (loss)/earnings per share is presented.

6. Movement of reserves

	Share premium HK\$'000	Contributed surplus HK\$'000	(Accumulated losses) HK\$'000	Total HK\$'000
At 1 April 2005	15,050	10	(15,908)	(848)
Loss for the three months ended 30 June 2005	–	–	(7,696)	(7,696)
At 30 June 2005	15,050	10	(23,604)	(8,544)
At 1 April 2004	11,387	10	(7,543)	3,854
Issue of shares	4,347	–	–	4,347
Shares issue expenses	(684)	–	–	(684)
Profit for the three months ended 30 June 2004	–	–	2,336	2,336
At 30 June 2004	15,050	10	(5,207)	9,853

FINANCIAL AND BUSINESS REVIEW

For the three months ended 30 June 2005, the Group recorded a turnover of approximately HK\$4.0 million (2004: 25.8 million) and a net loss attributable to shareholders of approximately HK\$7.7 million (2004: a net profit attributable to shareholders of approximately HK\$2.3 million).

During the period under review, the Group completed the production of two film projects titled, "Election" [「黑社會」] and "The Unusual Youth" [「非常青春期」]. The Group owns the film rights of these two films for distribution. The film, "The Unusual Youth" [「非常青春期」] has been released for exhibition in local cinemas in the period under review with satisfactory box office receipts whereas its overseas distribution was also encouraging.

Apart from entering into the 2005 Cannes International Film Festival as 'Competition Film', the Group's production, "Election" [「黑社會」] was also invited to the 2005 Melbourne International Film Festival as a closing film. The film will be released for exhibition in the local market shortly. Up to the date of this report, the overseas pre-sale of this film has been encouraging.

In addition to the investment in film projects, the Group utilised its expertise during the period under review by the provision of production resources and services for another film project, which is owned by other film company.

The Group has been insisted on its corporate philosophy of producing high quality films. Its productions were not compromised with the on-going downturn of the local film industry. As a consequence, the Group experienced a gross loss due to high cost of production without a proportionate increase in revenue generated from this sluggish market condition. Furthermore, the Group has incurred extra marketing and promotion expenses for publicizing the two film projects owned by it. The Group believed that the extra expenditures would add value to the investments as a whole including the quality title of films retained in its film library.

The net loss of approximately HK\$7.7 million for the three months ended 30 June 2005 was mainly attributable to the significant reduction of turnover from that in the corresponding period in 2004 during which two large-scale film projects were completed and recognized as revenue. Other operating expenses have remained fairly constant as compared to that in the corresponding period in 2004 except for the increased marketing and promotion expenses as explained above. Further, during the period under review, the Group incurred interest expenses in respect of bank loan and loans from related companies. No such interest expenses were recorded in the corresponding period in 2004.

PROSPECTS

Looking ahead, the Directors expect the local market is unlikely to experience any significant breakthrough in a short period of time. Coupled with the fierce competitions from both local and overseas, the Group believes that its quality productions enable it to maintain its competitive niche in the industry. In view of the financing of producing quality films, the Group will keep a balance between providing film production service to other film companies and investing in its own productions.

At the date of this report, the Group has entered into a number of film production agreements with different film companies and entertainment conglomerates for the production of several films in the year. Some of these films have commenced their pre-production work. Meanwhile, at the balance sheet date, a film that was invested by the Group was in the production stage and was expected to generate revenue to the Group shortly.

With the film production agreements entered into by the Group and the encouraging feedback of pre-sale of the films produced, the Directors are confident in resuming the profitability of the Group in the future.

RELATED PARTY TRANSACTIONS

During the period under review, Mr. Law Sau Yiu, Dennis ("Mr. Law"), executive director of the Company, continued to provide personal guarantee to a bank to secure banking facility granted to the Group. The facility is also secured by listed securities, other than that of the Company, placed by Mr. Law having discounted market value not less than the amount of banking facility utilized by the Group from time to time. At the balance sheet date, the Group has utilized such banking facility amounted to HK\$5 million.

At the balance sheet date, two private companies in which Mr. Law and Ms. Teng Chia Lin, Chialina, executive director of the Company, are directors and/or shareholders, had advanced HK\$10 million to the Group. The loans are unsecured, bear interest at commercial rate and are repayable within one year from the date of advances.

OTHER INFORMATION

1. Directors' and Chief Executives' Interests and Short Positions in Shares, Underlying Shares and Debentures

At 30 June 2005, the interests and short positions of the Directors and chief executives of the Company and their associates in the shares, underlying shares and debentures of the Company and any of its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance (the "SFO"), which were notified to the Company and the Stock Exchange pursuant to Division 7 and 8 of Part XV of the SFO (including interests or short positions which they have taken or deemed to have taken under such provisions of the SFO); or which are required to be 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 Rule 5.46 of the GEM Listing Rules, were as follows:

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

Name of Director	Personal Interests	Family Interests	Corporate Interests	Other Interests	Total	%
Mr. Law Sau Yiu, Dennis	-	-	370,800,000 (Note)	-	370,800,000	46.06
Ms. Teng Chia Lin, Chialina	-	-	370,800,000 (Note)	-	370,800,000	46.06

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 2005, none of the Directors or chief executives of the Company or their associates 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), which would have to be notified to the Company and the Stock Exchange pursuant to Division 7 and 8 of Part XV of the SFO (including interests or short positions which they have taken or deemed to have taken under such provisions of the SFO); or which were required to be 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 Rule 5.46 of the GEM Listing Rules.

2. Share Option 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 25 to the financial statements as included in the annual report of the Company for the year ended 31 March 2005.

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 2005, no options under the Share Option Scheme had been granted.

3. Directors and Chief Executives' Rights to Acquire Shares or Debentures

Save as disclosed above, at 30 June 2005, neither the Company nor any of its subsidiaries was a party to any arrangements to enable the directors and chief executives of the Company to acquire benefits by means of the acquisition of shares in, or debentures of the Company or any other body corporate, and none of the directors and chief executive of the Company or their spouses or children under the age of 18, had any right to subscribe for the securities of the Company, or had exercised any such rights.

4. Substantial Shareholders

At 30 June 2005, 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	370,800,000 (Note a)	46.06
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 executives' 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 2005, the Company has not been notified of any persons (other than the Directors or chief executives 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.

5. Purchase, Sale or Redemption of Listed Securities of the Company

During the three months period ended 30 June 2005, neither the Company nor any of its subsidiaries purchased, sold or redeemed any of the Company's listed securities.

6. Sponsor's Interest

As at 31 March 2005, Hantec Capital Limited ceased to be the sponsor of the Company upon expiration of the terms of contract entered between Hantec and the Company. The Company has no sponsor since 1 April 2005. Accordingly, no further disclosure is made.

7. Resignation of Executive Director and Appointment of Chief Executive Officer

Mr. To Kei Fung ("Mr. To") had resigned as executive director of the Company with effect from 1 August 2005 and had been appointed as chief executive officer of the Company responsible for the overall development and day-to-day operations of the Group with effect from the same date.

8. Competing Interests

At 30 June 2005, 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 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.

Upon his appointment as chief executive officer of the Company, Mr. To has entered into a service agreement with the Company. The service agreement contained non-competition clauses similar to the above.

9. Board Practices and Procedures

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 2005.

10. Audit Committee

The Company has established an audit committee with written terms of reference in compliance with Rules 5.28 to 5.33 of 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 three independent non-executive directors namely, Mr. Lung Hak Kau, Ms. Wai Lai Yung and Ms. Tsang Kei Ling. The audit committee has reviewed the Group's unaudited consolidated financial statements for the three months ended 30 June 2005.

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

Hong Kong, 12 August 2005