



***i*Merchants Limited**

Third Quarterly Report 2005-2006

***i*Merchants**
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CHARACTERISTICS OF THE GROWTH ENTERPRISE MARKET (“GEM”) OF THE STOCK EXCHANGE OF HONG KONG LIMITED (THE “STOCK EXCHANGE”)

GEM has been established as a market designed to accommodate companies to which a high investment risk may be attached. In particular, companies may list on GEM with neither a track record of profitability nor any obligation to forecast future profitability. Furthermore, there may be risks arising out of the emerging nature of companies listed on the 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 issuers.

The Stock Exchange takes no responsibility for the contents of this report, makes no representation as to its accuracy or completeness and expressly disclaims any liability whatsoever for any loss howsoever arising from or in reliance upon the whole or any part of the contents of this report.

This report, for which the directors of iMerchants Limited collectively and individually accept responsibility, includes particulars given in compliance with the Rules Governing the Listing of Securities on the Growth Enterprise Market of the Stock Exchange for the purpose of giving information with regard to iMerchants 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.

SUMMARY

The Group's unaudited consolidated profit for the nine months ended 31 December 2005 was approximately HK\$7,737,000, compared to the unaudited consolidated loss of approximately HK\$2,569,000 of the Group for the corresponding nine-month period in 2004. No interim dividend is recommended for the period.

GROUP BUSINESS REVIEW

iMerchants targets investments in technology ventures in selected market sectors where we can provide added value in business and corporate development to the target companies. In these sectors, we will continue to identify market trends that are likely to lead to significant growth and invest in companies in such markets that can best capture the business opportunities. For the nine months ended 31 December 2005, iMerchants generated a net profit of approximately HK\$7,737,000 compared to a net loss of approximately HK\$2,569,000 for the corresponding nine-month period in 2004. The improvement in operating results is largely attributable to the reduction in operation expenses and to the satisfactory contribution of iMerchants' treasury investments. As iMerchants may or may not hold majority interests in its venture investments, the business turnovers of such investee companies may or may not be consolidated into the group accounts of iMerchants as evidenced by the turnovers of past years. The management team's energies will be focused on enhancing iMerchants' overall value in the future.

FINANCIAL REVIEW

For the nine months ended 31 December 2005, the Group's turnover was approximately HK\$300,000 which mainly comprised of recurring income from maintenance services for custom-made software developed in the past years. The turnover does not include the turnovers of iMerchants' other venture investments in which iMerchants holds minority interests. The decrease in turnover was mainly due to the management decision to streamline the operation of its wholly-owned subsidiaries and transfer the related system integration works to our business partners. We are now focusing on value enhancement of the Group. The Group generated a net profit of approximately HK\$7,737,000 for the nine months ended 31 December 2005, compared to a net loss of approximately HK\$2,569,000 for the corresponding period in 2004. The improvement in operating results is largely attributable to the reduction in operating overheads, and also to the satisfactory contribution from the Group's treasury investments.

CAPITAL REDUCTION

In respect of the Capital Reduction of the Company, as announced by the Company on 14 December 2005, the Board is pleased that the High Court made an order on 13 December 2005 confirming the Capital Reduction pursuant to section 60 of the Companies Ordinance (Cap. 32 of the Laws of Hong Kong). The Registrar of Companies also issued on 3 January 2006 a "Certificate of Registration on Cancellation of Share Premium Account under section 61 of the Companies Ordinance" certifying the filing and registration of the High Court's order by the Company on 16 December 2005. The Company's Capital Reduction has become effective since then. The entire share premium account of the Company of HK\$207,129,706.70 has been cancelled and the credit arising from such cancellation is applied to write off the total accumulated loss of the Company of HK\$146,537,014.05 as at 31 March 2005. The remaining balance of HK\$60,592,692.65 of the Company is transferred to a special capital reserve of the Company. The Capital Reduction of the Company has provided a capital structure that would permit payment of dividends as and when the Directors consider it appropriate in the future. **At this stage, the Board has yet to decide on the future dividend policy of the Company. There can be no assurance that a dividend will be declared, made or paid in the future.**

RESULTS

The board of Directors (the "Board") of the Company presents the unaudited consolidated results of the Company and its subsidiaries (the "Group") for the three months and the nine months ended 31 December 2005 together with the comparative unaudited figures for the corresponding periods in 2004 as follows:

| | Notes | Three months ended | | Nine months ended | |
|-------------------------------|-------|--------------------------|-------------------|--------------------------|---------------------|
| | | 31 December | | 31 December | |
| | | 2005 | 2004 | 2005 | 2004 |
| | | HK\$'000 | HK\$'000 | HK\$'000 | HK\$'000 |
| Turnover | 2 | 88 | 581 | 300 | 2,174 |
| Other operating income | | 3,721 | 11,123 | 14,866 | 14,147 |
| Staff costs | | (1,019) | (1,613) | (3,378) | (9,274) |
| Depreciation | | (47) | (266) | (267) | (867) |
| Other operating expenses | | (962) | (2,404) | (3,784) | (8,749) |
| Profit/(loss) from operations | 3 | 1,781 | 7,421 | 7,737 | (2,569) |
| Taxation | 4 | - | - | - | - |
| Profit/(loss) for the period | | <u>1,781</u> | <u>7,421</u> | <u>7,737</u> | <u>(2,569)</u> |
| Earnings/(loss) per share | | | | | |
| - basic and diluted | 5 | <u>0.153 cent</u> | <u>0.639 cent</u> | <u>0.666 cent</u> | <u>(0.221) cent</u> |

Notes

1. Basis of preparation

In 2004, the Hong Kong Institute of Certified Public Accountants ("HKICPA") issued a number of new or revised Hong Kong Accounting Standards and Hong Kong Financial Reporting Standards (herein collectively referred to as "HKFRSs") which are effective for accounting periods beginning on or after 1 January 2005.

The financial statements of the Group have been prepared in accordance with all applicable HKFRSs issued by the HKICPA, accounting principles generally accepted in Hong Kong, the disclosure requirements of the Hong Kong Companies Ordinance and the disclosure requirements of the Growth Enterprise Market of The Stock Exchange of Hong Kong Limited.

The measurement basis used in the preparation of the financial statements is historical cost modified by the marking to market of certain investments in securities at the balance sheet date.

2. Turnover

Turnover represents revenue generated from contracts for consultancy and sale of software licenses and the amounts received and receivable for other related services rendered by the Group to customers during the period.

3. Profit/(loss) from operations

Profit/(loss) from operations is arrived at after charging (crediting):

| | Nine months ended 31 December | |
|--|----------------------------------|--------------------------|
| | 2005 | 2004 |
| | HK\$'000 | HK\$'000 |
| Operating lease charges in respect of rented premises | 816 | 1,453 |
| Staff costs including Directors' emoluments | | |
| Salaries and allowances | 3,403 | 8,163 |
| Long service/redundancy payments | 80 | 895 |
| Contributions to retirement benefits schemes, net of forfeiture | (105) | 216 |
| | 3,378 | 9,274 |
| Interest income from bank deposits | (350) | (688) |
| Interest income from debt securities | (3,207) | (3,228) |
| Dividends from listed securities | (2,012) | (1,010) |
| Net realised and unrealised gain on listed trading securities | (9,082) | (9,136) |
| Rental income | (215) | (85) |
| | <u> </u> | <u> </u> |

4. Taxation

No provision for Hong Kong Profits Tax has been made in the financial statements as the Group incurred tax losses for both periods. No provision for taxation in other jurisdictions was made as the Group's subsidiaries operating outside Hong Kong had no assessable profits.

5. Earnings/(loss) per share

The calculation of the basic and diluted earnings/(loss) per share for the three months and the nine months ended 31 December 2005 is based on the profit of the Group of approximately HK\$1,781,000 (2004: profit of approximately HK\$7,421,000) and approximately HK\$7,737,000 (2004: loss of approximately HK\$2,569,000), respectively, and on the number of ordinary shares of 1,161,382,000 (2004: 1,161,382,000).

The computation of diluted earnings/(loss) per share did not assume the exercise of the Company's outstanding share options as their exercise prices were higher than the average market price of the Company's shares for both periods.

6. Interim dividend

The Directors do not recommend the payment of an interim dividend for the nine months ended 31 December 2005 (2004: Nil).

7. Movements of reserves

| | Share | Negative | Capital | Merger | Investment | Accumulated | Total |
|---|----------------|--------------|------------|---------------|-------------|------------------|---------------|
| | premium | goodwill | redemption | reserve | revaluation | losses | |
| | HK\$'000 | HK\$'000 | HK\$'000 | HK\$'000 | HK\$'000 | HK\$'000 | HK\$'000 |
| At 1 April 2004 | 207,130 | 1,884 | 409 | 45,918 | 1,458 | (153,449) | 103,350 |
| Deficit on revaluation of other securities and not recognized in the income statement | - | - | - | - | (1,348) | - | (1,348) |
| Loss for the period | - | - | - | - | - | (2,569) | (2,569) |
| At 31 December 2004 | <u>207,130</u> | <u>1,884</u> | <u>409</u> | <u>45,918</u> | <u>110</u> | <u>(156,018)</u> | <u>99,433</u> |

| | Special | Share | Negative | Capital | Merger | Investment | Accumulated | Total |
|---|---------------|-----------|--------------|------------|---------------|----------------|----------------|---------------|
| | capital | premium | goodwill | redemption | reserve | revaluation | losses | |
| | reserve | HK\$'000 | HK\$'000 | HK\$'000 | HK\$'000 | HK\$'000 | HK\$'000 | HK\$'000 |
| At 1 April 2005 | - | 207,130 | 1,884 | 409 | 45,918 | (734) | (160,823) | 93,784 |
| Capital Reduction of the Company | 60,593 | (207,130) | - | - | - | - | 146,537 | - |
| Deficit on revaluation of other securities and not recognized in the income statement | - | - | - | - | - | (2,541) | - | (2,541) |
| Profit for the period | - | - | - | - | - | - | 7,737 | 7,737 |
| At 31 December 2005 | <u>60,593</u> | <u>-</u> | <u>1,884</u> | <u>409</u> | <u>45,918</u> | <u>(3,275)</u> | <u>(6,549)</u> | <u>98,980</u> |

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

At no time during the nine months ended 31 December 2005 did the Company or its subsidiaries purchase, sell or redeem any of the Company's listed securities.

COMPETING INTERESTS

During the period under review, none of the directors or the management shareholders (as defined in the GEM Listing Rules) of the Company had an interest in a business that competed with the Group or might compete with the business of the Group.

DIRECTORS' INTEREST AND SHORT POSITIONS IN THE SHARES, UNDERLYING SHARES AND DEBENTURES

At 31 December 2005, the interests and short positions of the directors in the shares, underlying shares and debentures of the Company and its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance (the "SFO")) as recorded in the register required to be kept under Section 352 of the SFO or as otherwise notified to the Company and The Stock Exchange of Hong Kong Limited (the "Stock Exchange") pursuant to Rule 5.46 of the GEM Listing Rules were as follows:

Long positions in ordinary shares of HK\$0.10 each of the Company

| Name of director | Number of issued ordinary shares held | | | Total | Percentage of issued share capital of the Company |
|--|---------------------------------------|---------------|--------------------------------|-------------|---|
| | Beneficial owner | Held by trust | Held by controlled corporation | | |
| Mr. Leroy Kung Lin Yuen ("Mr Kung") | - | - | 758,381,000 (Note) | 758,381,000 | 65.30% |
| Mr. Matthew P. Johnston | 100,000 | - | - | 100,000 | <1% |

Note:

The registered shareholder of 758,381,000 shares is iMerchants Group Limited ("iMerchants Group"). iMerchants Group is wholly-owned by Asian Gold Associates Limited ("Asian Gold"), 76% of its issued share capital is owned by Galaface Limited ("Galaface"). Mr Kung is deemed to have interests in the 758,381,000 shares owned by iMerchants Group as he owns the entire interest in Galaface and is entitled to exercise more than one-third of the voting power at general meetings of both Asian Gold and Galaface.

Long positions in underlying shares - share options granted by the Company

No long positions of directors in the underlying shares of the equity derivatives of the Company and its associated corporations were recorded in the register or as otherwise notified to the Company and the Stock Exchange pursuant to Rule 5.46 of the GEM Listing Rules.

Long positions in debentures

No long positions of directors in the debentures of the Company and its associated corporations were recorded in the register or as otherwise notified to the Company and the Stock Exchange pursuant to Rule 5.46 of the GEM Listing Rules.

Short positions in ordinary shares of HK\$0.10 each of the Company

No short positions of directors in the shares of the Company and its associated corporations were recorded in the register or as otherwise notified to the Company and the Stock Exchange pursuant to Rule 5.46 of the GEM Listing Rules.

Short positions in underlying shares

No short positions of directors in the underlying shares of the equity derivatives of the Company and its associated corporations were recorded in the register or as otherwise notified to the Company and the Stock Exchange pursuant to Rule 5.46 of the GEM Listing Rules.

Short positions in debentures

No short positions of directors in the debentures of the Company and its associated corporations were recorded in the register or as otherwise notified to the Company and the Stock Exchange pursuant to Rule 5.46 of the GEM Listing Rules.

Save as disclosed above, as at 31 December 2005, none of the directors had any interest in any shares, underlying shares and debentures of the Company and its associated corporations (within the meaning of Part XV of the SFO) as recorded in the register required to be kept under Section 352 of the SFO or as otherwise notified to the Company and the Stock Exchange pursuant to Rule 5.46 of the GEM Listing Rules.

INTEREST DISCLOSEABLE UNDER THE SFO AND SUBSTANTIAL SHAREHOLDERS

At 31 December 2005, the following person (other than the interests disclosed above in respect of certain directors of the Company) had interests and short positions in the shares and underlying shares of the Company as recorded in the register required to be kept under Section 336 of the SFO.

Long positions in ordinary shares of HK\$0.10 each of the Company

| Name | Capacity | Number of ordinary shares | Percentage of issued share capital |
|---------------------------|------------------|--------------------------------------|---|
| GEM Global Yield Fund Ltd | Beneficial owner | 58,125,000 | 5.00% |

Long positions in underlying shares

No long positions of other persons and substantial shareholders in the underlying shares of equity derivatives of the Company were recorded in the register.

Short positions in shares

No short positions of other persons and substantial shareholders in the shares of the Company were recorded in the register.

Short positions in underlying shares

No short positions of other persons and substantial shareholders in the underlying shares of equity derivatives of the Company were recorded in the register.

Save as disclosed above, as at 31 December 2005, the directors were not aware of any other person who had an interest or a short position in the shares or underlying shares of the Company as recorded in the register required to be kept under Section 336 of the SFO.

ARRANGEMENTS TO PURCHASE SHARES OR DEBENTURES

The following share options to purchase shares of the Company were granted to a former executive director, Mr Edward Un Ding Bong ("Mr Un"). Mr Un resigned as an executive director of the Company with effect from 30 June 2005. These options were lapsed when he ceased to be employed by the Company on the same date.

| Name of director | Capacity | Date of grant | Exercise price | Exercisable period | Number of options held |
|------------------|------------------|-------------------|----------------|---|-------------------------------|
| Mr Un | Beneficial owner | 23 August 2000 | HK\$0.53 | In various stages from 1 April 2001 to 23 August 2010 | 2,000,000 <i>(note i)</i> |
| | | 27 September 2002 | HK\$0.172 | In various stages from 1 September 2003 to 28 August 2012 | 8,000,000 <i>(note ii)</i> |

Notes:

- (i) 2,000,000 share options were granted on 23 August 2000 under the 2000 Share Option Scheme, which was approved by the written resolution of the shareholders of the Company dated 15 March 2000. Share options granted under the 2000 Share Option Scheme may be exercised in accordance with the terms of the scheme as to:
 - a. one quarter of the share options would be exercisable from 1 April 2001 ("First Exercise Date");
 - b. an additional one eighth of the share options would be exercisable after the expiry of each successive six-month period from the First Exercise Date; and
 - c. the balance of the share options would be exercisable after the expiry of a period of 48 months from 1 April 2001.

- (ii) 8,000,000 share options were granted on 27 September 2002 under the 2002 Share Option Scheme, which was approved by the shareholders of the Company in the special general meeting dated 2 August 2002. Share options granted under the 2002 Share Option Scheme may be exercisable in accordance with the terms of the scheme as to:
 - a. Share options to subscribe for 4,000,000 shares of the Company would be exercisable from 1 September 2003 to 28 August 2012; and
 - b. The balance of 4,000,000 share options would be exercisable from 1 September 2004 to 28 August 2012.

Other than the share option schemes as described above, at no time during the period was the Company, its holding companies, fellow subsidiaries or subsidiaries a party to any arrangement to enable the directors of the Company to acquire benefits by means of the acquisition of shares in, or debentures of, the Company or any other body corporate.

DIRECTORS' INTERESTS IN CONTRACTS OF SIGNIFICANCE

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

AUDIT COMMITTEE

- (i) The Company's audit committee was formed on 15 March 2000 with written terms of reference in compliance with the GEM Listing Rules.
- (ii) The audit committee has three members comprising the independent non-executive directors, namely, Messrs. Ronny Chow Fan Chim, Kenneth Tseung Yuk Hei and Matthew P. Johnston. All committee members possess appropriate industry and financial experience to advise on the Company's strategy and other matters.
- (iii) The composition of the audit committee meets the requirements of Rule 5.28 of the GEM Listing Rules.
- (iv) The primary duties of the audit committee are to review the financial information of the Group and supervise the financial reporting process and internal control procedures of the Group.
- (v) The audit committee has reviewed the draft of this report and has provided advice and comments thereon.

COMPLIANCE WITH THE CODE ON CORPORATE GOVERNANCE PRACTICES

The Board has reviewed the Company's corporate governance practices and is satisfied that the Company has full compliance with the Code on Corporate Governance Practices as set out in Appendix 15 of the GEM Listing Rules for the nine-month period ended 31 December 2005.

By order of the Board

Leroy Kung Lin Yuen

Chairman

Hong Kong, 10 February 2006

The Directors of the Company as at the date of this report are as follows:

Executive Directors:

Mr. Leroy Kung Lin Yuen

Ms. Lena Foo

Independent Non-executive Directors:

Mr. Ronny Chow Fan Chim

Mr. Kenneth Tseung Yuk Hei

Mr. Matthew P. Johnston