



WAFER SYSTEMS

Wafer Systems Limited

威發系統有限公司*

(Incorporated in the Cayman Islands with limited liability)

(Stock Code: 8198)

**FIRST QUARTERLY REPORT
FOR THE 3 MONTHS ENDED 31 MARCH 2007**

CHARACTERISTICS OF THE GROWTH ENTERPRISE MARKET (“GEM”) OF THE STOCK EXCHANGE OF HONG KONG LIMITED (THE “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 of the Exchange 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 Exchange. GEM-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 at www.hkgem.com in order to obtain up-to-date information on GEM-listed issuers.

The 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.

As at the date of this report, the Board consists of one executive director, Mr. Chan Sek Keung, Ringo, one non-executive director, Mr. Kwan Kit Tong and three independent non-executive directors, namely Mr. Pang Hing Chung, Alfred, Mr. David Tsoi and Mr. Chan Tze Ngan.

This report, for which the directors (the “directors”) of Wafer Systems Limited (the “Company”) collectively and individually accept full responsibility, includes particulars given in compliance with the Rules Governing the Listing of Securities on GEM (the “GEM Listing Rules”) for the purpose of giving information with regard to the Company. The directors, having made all reasonable enquiries, confirm that, to the best of their knowledge and belief: (i) the information contained in this report is accurate and complete in all material respects and not misleading; (ii) there are no other matters the omission of which would make any statement in this report misleading; and (iii) 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.

* For identification purpose only

TO OUR SHAREHOLDERS

The board of Directors (the “Board”) hereby report the unaudited consolidated results of the Company and its subsidiaries (collectively, the “Group”) for the three months ended 31 March 2007 (the “Review Period”) together with the comparative unaudited figures for the corresponding period in 2006.

BUSINESS REVIEW AND PROSPECTS

The Group continued its business principally in the provision of network infrastructure solutions, including the sales of network equipment and software, provision of related network professional services and sales of its proprietary network software.

First quarter of the year is a traditionally slow season for our business. During the Review Period, the Group recorded a turnover of approximately HK\$50.6 million (2006: approximately HK\$46.4 million), an increase of approximately 9% from that recorded in the corresponding period in 2006. Loss attributable to equity holders of the Company for the Review Period was reduced to HK\$958,000 (2006: approximately loss HK\$3,890,000). The better results compared with the year before have largely been due to the better performance in the businesses of professional services and proprietary network software during the Review Period.

Geographically, mainland China remained predominantly the biggest business generating area for the Group. During the Review Period, the Group continued to invest in building up its capability in next generation network (“NGN”) software and solutions and management software. Sales of such software during the Review Period have continued its upward trend.

Continual technology up-grading, congenial partnership with technology leaders and high customer satisfaction will continue to be the priorities of the Group to maintain being a leading NGN solution and service provider.

INTERIM DIVIDEND

The Board does not recommend the payment of an interim dividend for the Review Period (2006: Nil).

FINANCIAL INFORMATION

Unaudited Consolidated Financial Results

		For the three months ended 31 March	
		2007	2006
	Note	HK\$'000	HK\$'000
Turnover	2	50,552	46,358
Other income		31	483
Charges in materials and equipment		(36,059)	(38,555)
Employee expenses		(5,566)	(4,962)
Depreciation and amortisation		(1,077)	(1,210)
Other expenses		(7,637)	(5,255)
Finance costs		(1,202)	(749)
		<u> </u>	<u> </u>
Loss before taxation	3	(958)	(3,890)
Taxation	4	–	–
		<u> </u>	<u> </u>
Loss for the period		<u>(958)</u>	<u>(3,890)</u>
Attributable to:			
Equity holders of the Company		<u>(958)</u>	<u>(3,890)</u>
Loss per share			
– Basic (cents)	5	<u>(0.33)</u>	<u>(1.34)</u>

NOTES TO THE UNAUDITED CONSOLIDATED FINANCIAL RESULTS

(1) Basis of presentation

The unaudited consolidated financial results have been prepared in accordance with Hong Kong Financial Reporting Standards issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA") and the applicable disclosure requirements of the GEM Listing Rules.

The accounting policies adopted in preparing the unaudited consolidated financial report were in consistent with those applied for the annual financial report for the year ended 31 December 2006.

The unaudited consolidated results have been reviewed by the audit committee of the Company (the "Audit Committee").

(2) Turnover

An analysis of the Group's turnover recognised for the three months ended 31 March 2007 together with the comparative figures for the corresponding period in 2006 are as follows:

	(Unaudited)	
	For the three months	
	ended 31 March	
	2007	2006
	HK\$'000	HK\$'000
Network infrastructure	38,293	39,454
Professional services	10,328	6,215
Network software	1,931	689
Total	50,552	46,358

(3) Loss before taxation

Loss before taxation has been arrived at after charging:

	For the three months	
	ended 31 March	
	2007	2006
	HK\$'000	HK\$'000
Amortisation of software product development costs	650	656
Depreciation of property, plant and equipment	427	554
Employee expenses (including directors' remuneration)	5,566	4,962
and after crediting:		
Interest income	31	15

(4) Taxation

No provision for Hong Kong profits tax has been made, as the Group had no assessable profit for the three months ended 31 March 2007 and its corresponding period in 2006.

PRC income tax has not been provided for the Review Period and its corresponding period in 2006 as the Company's PRC subsidiaries had either no assessable profit or were within their tax exemption period.

Pursuant to the relevant laws and regulations in the PRC, the Company's PRC subsidiaries are entitled to exemption from PRC income tax for two years commencing from their first profit-making year of operation and thereafter entitled to a 50% relief from PRC income tax for the immediate following three years. During the Review Period, one of the Company's PRC subsidiaries was still within its 50% tax relief period; while one of the Company's PRC subsidiaries was still within its tax exemption period as its first profit-making year of operation has not started yet.

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

(5) Loss per share

The calculation of basic (loss) earnings per share for the three months ended 31 March 2007 is based on the unaudited loss attributable to equity shareholders of the Company of approximately HK\$958,000 (2006: loss of approximately HK\$3,890,000) and on the weighted average number of approximately 289,945,000 ordinary shares (2006: approximately 289,945,000) in issue during the period.

Diluted loss per share has not been presented for the three months ended 31 March 2007 since the effect is anti-dilutive.

(6) Reserves

Movements of reserves during the Review Period have been:--

	Share capital HK\$'000	Share premium HK\$'000	Share-based payments reserve HK\$'000	Statutory surplus reserve fund HK\$'000	Enterprise expansion fund HK\$'000	Staff welfare fund HK\$'000	Exchange reserve HK\$'000	Retained earnings/ Accumulated losses HK\$'000	Total HK\$'000
As at 1 January 2006	2,900	55,824	587	1,003	502	502	566	(2,458)	59,426
Recognition of equity settled share-based payments	-	-	24	-	-	-	-	-	24
Exchange difference on translation of foreign operations	-	-	-	-	-	-	338	-	338
Loss for the three months ended 31 March 2006	-	-	-	-	-	-	-	(3,890)	(3,890)
As at 31 March 2006	<u>2,900</u>	<u>55,824</u>	<u>611</u>	<u>1,003</u>	<u>502</u>	<u>502</u>	<u>904</u>	<u>(6,348)</u>	<u>55,898</u>
As at 1 January 2007	2,900	55,824	643	1,505	502	-	1,196	2,643	65,213
Recognition of equity settled share-based payments	-	-	28	-	-	-	-	-	28
Exchange difference on translation of foreign operations	-	-	-	-	-	-	834	-	834
Loss for the three months ended 31 March 2007	-	-	-	-	-	-	-	(958)	(958)
As at 31 March 2007	<u>2,900</u>	<u>55,824</u>	<u>671</u>	<u>1,505</u>	<u>502</u>	-	<u>2,030</u>	<u>1,685</u>	<u>65,117</u>

PURCHASE, REDEMPTION OR SALE OF LISTED SECURITIES OF THE COMPANY

During the Review Period, neither the Company nor any of its subsidiaries purchased, sold or redeemed any of the Company's listed securities.

SHARE OPTION SCHEMES

The Company, at the general meeting held on 20 April 2002, adopted both a pre-IPO share option scheme (the "Pre-IPO Share Option Scheme") and a post-IPO share option scheme (the "Post-IPO Share Option Scheme").

Save as disclosed below, no options granted pursuant to either the Pre-IPO Share Option Scheme or the Post-IPO Share Option Scheme had been exercised during the Review Period.

(a) Pre-IPO Share Option Scheme

One single grant of 11,913,000 shares in aggregate was made to various participants on 30 April 2002 under this scheme. As at 31 March 2007, options comprising an aggregate of 8,310,000 shares were outstanding, as detailed below:

	Exercise price per share <i>HK\$</i>	Number of share options		
		Outstanding as at 1.1.2007	Lapsed during Review Period	Outstanding as at 31.3.2007
Types of participants:				
Directors	0.55	3,750,000	–	3,750,000
Advisor	0.55	750,000	–	750,000
Employees	0.55	3,810,000	–	3,810,000
		<u>8,310,000</u>	<u>–</u>	<u>8,310,000</u>

Pre-IPO share options are exercisable as to (i) a maximum of 25% of the total number of options granted six months after 17 May 2002 (the "Listing Date"); (ii) a maximum additional 6.25% of the total number of options granted after the expiry of each 3-month period twelve months after the Listing Date; and (iii) the remaining options granted on or after the third anniversary of the Listing Date until the end of the option period or lapse of an option.

The above outstanding options may be exercised, in accordance with the terms of the Pre-IPO Share Option Scheme, before 30 April 2012.

(b) Post-IPO Share Option Scheme

There have been a total of 6 lots of Post-IPO share options granted. The lots were 5,277,000 shares on 12 July 2002, 7,859,000 shares on 20 February 2003, 385,000 shares on 10 October 2003, 2,844,000 shares on 23 February 2004, 828,000 shares on 11 October 2004 and 6,980,000 shares on 12 January 2007.

A summary of the Post-IPO Share Option Scheme movements during the Review Period and as at 31 March 2007 is as follows:

Date of grant	Type of participants	Exercisable period	Exercise price per share <i>HK\$</i>	Number of share options			
				Outstanding as at 1.1.2007	Granted during Review Period	Lapsed during Review Period <i>(Note 1)</i>	Outstanding as at 31.3.2007
12.7.2002	Employees	12.7.2003 to 11.7.2012	0.384	2,025,000	-	-	2,025,000
20.2.2003	Directors	20.2.2004 to 19.2.2013	0.138	3,825,000	-	-	3,825,000 <i>(Note 2)</i>
	Advisors	20.2.2004 to 19.2.2013	0.138	300,000	-	-	300,000
	Employees	20.2.2004 to 19.2.2013	0.138	1,961,000	-	-	1,961,000
				6,086,000	-	-	6,086,000
10.10.2003	Employees	10.10.2004 to 9.10.2013	0.142	135,000	-	-	135,000
23.2.2004	Employees	23.2.2005 to 22.2.2014	0.165	1,458,000	-	-	1,458,000
11.10.2004	Employees	11.10.2005 to 10.10.2014	0.124	315,000	-	-	315,000
12.1.2007	Directors	12.1.2008 to 11.1.2017	0.088	-	750,000	-	750,000
	Employees	12.1.2008 to 11.1.2017	0.088	-	6,230,000	-	6,230,000
				-	6,980,000	-	6,980,000
		Total:		10,019,000	6,980,000	-	16,999,000

Notes: –

- (1) These options were lapsed according to the rules of this scheme due to the employees having left the Group.
- (2) Out of these 3,825,000 share options outstanding as at 31 March 2007, 375,000 shares were granted to each of Mr. Alasdair Gordon Nagle and Ms. Clara Ho, directors appointed to the Board to represent the interests of The Applied Research Council. Both Mr. Nagle and Ms. Ho exercised the options on 3 April 2007 and shares were allotted to them accordingly.

Post-IPO share options are exercisable starting from the first anniversary of the date of grant at stepped annual increments of 25% of the total options granted, for a period not later than 10 years from the date of grant.

The above outstanding options may be exercised within such exercise period in accordance with the terms of the Post-IPO Share Option Scheme.

DIRECTORS' AND CHIEF EXECUTIVE'S INTERESTS OR SHORT POSITION IN SHARES AND UNDERLYING SHARES OF THE COMPANY

As at 31 March 2007, the interests and short positions of the directors, the chief executive of the Company and their respective associates (as defined in the GEM Listing Rules) 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 by the Company pursuant to Section 352 of the SFO or as otherwise notified to the Company and the Exchange pursuant to the required standard of dealings by directors as referred to in Rule 5.46 of the GEM Listing Rules, were as follows:

(a) Long positions in shares in the Company

Name of director	Number of shares held						Total interest in shares	Approximate percentage of the Company's issued share capital
	Personal interest	Capacity	Family interest	Corporate interest	Capacity	Other interest		
Mr. Chan Sek Keung, Ringo	8,852,000	Beneficial owner	–	56,400,000 (Note)	Interest through a controlled corporation	–	65,252,000	22.50%

Note: Such shares in the Company are held by Woodstock Management Limited ("Woodstock"), a company wholly owned by Mr. Chan Sek Keung, Ringo, who is deemed, by virtue of the SFO, to have an interest in these shares.

(b) Long positions in underlying shares in the Company (Directors' rights to acquire shares)

Name of Director	Date of grant	Number of	Number of	Number of	Number of	Aggregate	Approximate
		unlisted pre-IPO share option outstanding as at 1.1.2007	unlisted pre-IPO share option outstanding as at 31.3.2007	unlisted post-IPO share option outstanding as at 1.1.2007	unlisted post-IPO share option outstanding as at 31.3.2007		
Mr. Chan Sek Keung, Ringo	30.4.2002	3,000,000	3,000,000	-	-		
	20.2.2003	-	-	1,200,000	1,200,000	4,200,000	1.45%
Mr. Pang Hing Chung, Alfred	30.4.2002	750,000	750,000	-	-		
	20.2.2003	-	-	750,000	750,000	1,500,000	0.52%
Mr. David Tsoi	20.2.2003	-	-	750,000	750,000		
	12.1.2007	-	-	-	750,000	1,500,000	0.52%
Mr. Alasdair Gordon Nagle (Note 3)	20.2.2003	-	-	375,000	375,000	375,000	0.13%
Ms. Clara Ho (Note 3)	20.2.2003	-	-	375,000	375,000	375,000	0.13%
Mr. Kwan Kit Tong, Kevin	20.2.2003	-	-	375,000	375,000	375,000	0.13%

Notes:-

- (1) Each of the above directors is the personal beneficial owner of the share options granted to him or her.
- (2) Each of the directors' interests represent his or her respective long positions in the underlying shares in the Company by virtue of options granted to the directors pursuant to the Pre-IPO Share Option Scheme and the Post-IPO Share Option Scheme both adopted by the Company on 20 April 2002 (further details are set out under the section headed "Share Option Schemes").
- (3) Both Mr. Nagle and Ms. Ho exercised their respective option rights on 3 April 2007. They subsequently resigned from directorship in the Company with effect from 13 April 2007 after The Applied Research Council, whose interests Mr. Nagle and Ms. Ho were on the Board to represent, ceased to be a substantial shareholder of the Company after 12 April 2007.

- (4) Options granted on 30 April 2002 were exercisable during the period from 17 November 2002 to 29 April 2012 at the exercise price of \$0.55 per share.
- (5) Options granted on 20 February 2003 were exercisable during the period from 20 February 2004 to 19 February 2013 at the exercise price of \$0.138 per share.
- (6) Options granted on 12 January 2007 were exercisable during the period from 12 January 2008 to 11 January 2017 at the exercise price of \$0.088 per share.

Other than as disclosed above, none of the directors, the chief executive of the Company and their respective associates (as defined in the GEM Listing Rules), had any interests or short positions in any shares, underlying shares or debentures of the Company or any of its associated corporations as at 31 March 2007.

SUBSTANTIAL SHAREHOLDERS AND OTHER SHAREHOLDERS WHOSE INTERESTS ARE RECORDED UNDER SECTION 336 OF THE SFO

As at 31 March 2007, the following persons or corporations, in addition to the directors, stated under the section headed "Directors' and chief executive's interests or short position in shares and underlying shares of the Company", were interested in shares or underlying shares representing 5% or more in the issued share capital of the Company as recorded in the register of interests required to be kept by the Company pursuant to Section 336 of the SFO.

Long positions in shares in the Company

<u>Name of shareholder</u>	<u>Capacity</u>	<u>Type of interests</u>	<u>Number of shares</u>	<u>Approximate percentage of the Company's issued share capital</u>
The Applied Research Council ("ARC") (Note 1,3)	Beneficial owner	Corporate	48,460,000	16.71%
HSBC Private Equity Technology (Asia) Limited (Note 2,3)	Investment manager	Corporate	48,460,000	16.71%
HSBC Private Equity (Asia) Limited (Note 2,3)	Interest through a controlled corporation	Corporate	48,460,000	16.71%
North 22 Nominees Limited (Note 4)	Beneficial owner	Corporate	36,900,000	12.73%
Mr. Ng Lai Yick (Note 4)	Beneficial owner	Personal	3,134,744	1.08%
	Interest through a controlled corporation	Corporate	36,900,000	12.73%
QPL International Holdings Limited ("QPL") (Note 5)	Beneficial owner	Corporate	35,456,745	12.23%
Mr. Li Tung Lok (Note 5)	Interest through a controlled corporation	Corporate	35,456,745	12.23%
Madam Su Ching Wah (Note 5)	Interest of spouse	Family	35,456,745	12.23%

Notes:-

- (1) ARC is the beneficial owner of these shares.
- (2) HSBC Private Equity Technology (Asia) Limited is deemed, by virtue of the SFO, to have an interest in these shares as it is the investment manager of ARC.

HSBC Private Equity (Asia) Limited is deemed, by virtue of the SFO, to have an interest in these shares as HSBC Private Equity Technology (Asia) Limited is its wholly-owned subsidiary.

- (3) By notice to the Company, ARC informed that it had disposed of 44,824,000 shares in the Company between 11 April 2007 and 12 April 2007. ARC, therefore, ceased to be a substantial shareholder of the Company after 12 April 2007.
- (4) Mr. Ng Lai Yick is deemed, by virtue of the SFO, to have an interest in the 36,900,000 shares held by North 22 Nominees Limited as the company is wholly-owned by him.
- (5) Mr. Li Tung Lok is the controlling shareholder of QPL and is deemed, by virtue of the SFO, to have an interest in the 35,456,745 shares held by QPL.

Madam Su Ching Wah is the spouse of Mr. Li Tung Lok and is deemed, by virtue of the SFO, to have an interest in the 35,456,745 shares held by QPL.

Save as disclosed above, the Company had not been notified of any other relevant interests or short positions in the shares or underlying shares in the Company as at 31 March 2007.

COMPETITION AND CONFLICT OF INTERESTS

Each of the directors and the management shareholders of the Company and their respective associates (as defined in the GEM Listing Rules) has confirmed that none of them had any business or interest in companies that competed or might compete with the business of the Group or any other conflict of interests with the interests of the Group.

AUDIT COMMITTEE

The Company established the Audit Committee on 29 October 2001 with written terms of reference in compliance with Rules 5.28 to 5.29 of the GEM Listing Rules and with reference to the guidelines published by the Hong Kong Institute of Certified Public Accountants.

The present Audit Committee consists of three independent non-executive directors, namely, Mr. David Tsoi, Chairman, Mr. Pang Hing Chung, Alfred and Mr. Chan Tze Ngon. Mr. Chan Tze Ngon has joined the Board and the Audit Committee since 1 May 2007.

The Audit Committee has reviewed the draft of this report and has provided advice and comments thereon.

By Order of the Board
WAFER SYSTEMS LIMITED
CHAN Sek Keung, Ringo
Chairman and Chief Executive Officer

Hong Kong, 15 May 2007