Interim Report **2003**

STONE
ELECTRONIC
TECHNOLOGY
LIMITED

INTERIM RESULTS

The Board of Directors of Stone Electronic Technology Limited (the "Company") is pleased to announce the unaudited consolidated results of the Company and its subsidiaries (the "Group") for the six months ended 30 June, 2003 with comparative figures for the corresponding period in 2002 as follows:

		Unaudited	
		Six months ended 30 June,	
	Note	**2003**	2002
			restated
		HK$'000	*HK$'000*
Turnover	*3*	**488,943**	470,333
Cost of sales		**(428,442)**	(408,577)
Gross profit		**60,501**	61,756
Other revenue		**3,035**	3,345
		63,536	65,101
Distribution costs		**(29,904)**	(27,261)
Administrative expenses		**(32,222)**	(49,344)
Other operating expenses		**(15,569)**	(8,335)
Loss from operations		**(14,159)**	(19,839)
Non-operating income/(expenses)	*4*	**871,439**	(3,597)
Finance costs		**(975)**	(1,030)
Share of profits less losses of associates		**(12,300)**	650
Profit/(loss) from ordinary activities before taxation	*5*	**844,005**	(23,816)
Taxation	*6*	**(1,670)**	198
Profit/(loss) from ordinary activities after taxation		**842,335**	(23,618)
Minority interests		**(455,684)**	7,590
Profit/(loss) for the period attributable to shareholders		**386,651**	(16,028)
Earnings/(loss) per share	*7*		
— Basic		**32.26 cents**	(1.34) cents

The notes on pages 5 to 19 form part of this interim financial report.

Unaudited consolidated balance sheet at 30 June, 2003

	Note	At 30 June, 2003 HK$'000	At 30 June, 2003 HK$'000	At 31 December, 2002 restated HK$'000	At 31 December, 2002 restated HK$'000
Non-current assets					
Fixed assets					
— Investment properties			**61,537**		61,537
— Property, plant and equipment			**63,719**		64,944
			125,256		126,481
Goodwill			**7,974**		18,650
Interest in associates	8		**166,784**		179,651
Other financial assets	9		**49,468**		66,448
Deferred tax assets			**3,934**		3,937
			353,416		395,167
Current assets					
Investments	10	**1,376,453**		481,798	
Inventories	11	**141,793**		164,392	
Trade and other receivables	12	**186,978**		250,943	
Pledged deposits		**1,472**		3,357	
Cash and cash equivalents		**263,119**		213,692	
		1,969,815		1,114,182	
Current liabilities					
Bank loans		**41,408**		34,671	
Trade and other payables	13	**177,798**		205,250	
Taxation		**15,744**		15,776	
		234,950		255,697	
Net current assets			**1,734,865**		858,485
Total assets less current liabilities			**2,088,281**		1,253,652
Non-current liability					
Bank loans			**8,000**		12,000
Minority interests			**734,809**		305,328
NET ASSETS			**1,345,472**		936,324
CAPITAL AND RESERVES					
Share capital	14		**119,856**		119,856
Reserves	15		**1,225,616**		816,468
			1,345,472		936,324

The notes on pages 5 to 19 form part of this interim financial report.

Unaudited consolidated statement of changes in equity for the six months ended 30 June, 2003

	Note	Six months ended 30 June, 2003 HK$'000	2002 restated HK$'000
Total equity balance at 1 January as previously reported		**933,309**	867,294
— prior period adjustment in respect of deferred taxation	2	**3,015**	3,114
— as restated		**936,324**	870,408
(Deficit)/surplus on revaluation of investments in securities	15	**(12,900)**	430
Exchange differences on translation of the financial statements of foreign entities	15	**(567)**	3,944
Net (loss)/gain not recognised in the income statement		**(13,467)**	4,374
Net profit/(loss) for the period		**386,651**	(16,028)
Realisation of investment revaluation reserve to income statement	15	**36,980**	—
Realisation of capital reserve on disposal of a subsidiary	15	**(1,016)**	—
Realisation of goodwill on disposal of associates and subsidiaries		**—**	9
Total equity balance at 30 June		**1,345,472**	858,763

The notes on pages 5 to 19 form part of this interim financial report.

Unaudited condensed consolidated cash flow statement for the six months ended 30 June, 2003

	Six months ended 30 June,	
	2003	2002
	HK$'000	*HK$'000*
Net cash from operating activities	**35,316**	75,829
Net cash from/(used in) investment activities	**34,071**	(29,427)
Net cash used in financing activities	**(19,960)**	(30,057)
Net increase in cash and cash equivalents	**49,427**	16,345
Cash and cash equivalents at 1 January	**213,692**	284,979
Cash and cash equivalents at 30 June	**263,119**	301,324
Analysis of the balances of cash and cash equivalents		
Cash at bank and in hand	**263,119**	301,324

The notes on pages 5 to 19 form part of this interim financial report.

Notes on the unaudited interim financial report

1. Basis of preparation

This interim financial report is unaudited, but has been reviewed by KPMG in accordance with Statement of Auditing Standards 700 "Engagements to review interim financial reports", issued by the Hong Kong Society of Accountants (the "HKSA"). KPMG's independent review report to the board of directors is included on page 20.

The interim financial report has been prepared in accordance with the requirements of the Rules Governing the Listing of Securities ("Listing Rules") on The Stock Exchange of Hong Kong Limited, including compliance with Statement of Standard Accounting Practice 25 "Interim financial reporting" issued by the HKSA.

The financial information relating to the financial year ended 31 December, 2002 included in the interim financial report does not constitute the Company's statutory accounts for that financial year but is derived from those accounts. Statutory accounts for the year ended 31 December, 2002 are available from the Company's registered office. The auditors have expressed an unqualified opinion on those accounts in their report dated 25 April, 2003.

The same accounting policies adopted in the Annual Report 2002 have been applied to the interim financial report except for the changes in accounting policy as explained in Note 2 below.

The notes on the interim financial report include an explanation of events and transactions that are significant to an understanding of the changes in financial position and performance of the Group since the Annual Report 2002.

2. Changes in accounting policy

In prior years, deferred tax liabilities were provided using the liability method in respect of the taxation effect arising from all material timing differences between the accounting and tax treatment of income and expenditure, which were expected with reasonable probability to crystallise in the foreseeable future. Future deferred tax assets were not recognised unless their realisation was assured beyond reasonable doubt. With effect from 1 January, 2003, in order to comply with SSAP 12 (revised) "Income Taxes" issued by the HKSA, the Group adopted a new policy for deferred tax as set out below.

Under SSAP 12 (revised), deferred tax assets and liabilities arise from deductible and taxable temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the tax bases respectively. Deferred tax assets also arise from unused tax losses and unused tax credits.

Apart from certain limited exceptions, all deferred tax liabilities, and all deferred tax assets to the extent that it is probable that future taxable profits will be available against which the asset can be utilised, are recognised. The limited exceptions are temporary differences arising from goodwill not deductible for tax purposes, negative goodwill treated as deferred income, the initial recognition of assets or liabilities that affect neither accounting nor taxable profit, and temporary differences relating to investments in subsidiaries to the extent that, in the case of taxable differences, the Group controls the timing of the reversal and it is probable that the differences will not reverse in the foreseeable future, or in the case of deductible differences, unless it is probable that they will reverse in the future.

The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of the assets and liabilities, using tax rates enacted or substantively enacted at the balance sheet date. Deferred tax assets and liabilities are not discounted.

2. **Changes in accounting policy** *(Cont'd)*

The carrying amount of a deferred tax asset is reviewed at each balance sheet date and is reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow the related tax benefit to be utilised. Any such reduction is reversed to the extent that it becomes probable that sufficient taxable profit will be available.

As a result of the adoption of this accounting policy, the Group's profit for the period has been increased by HK$48,000 (2002: loss decreased by HK$540,000) and the Group's net assets as at 30 June, 2003 has been increased by HK$3,063,000 (at 31 December, 2002: HK$3,015,000).

The new accounting policy has been adopted retrospectively, with the opening balance of retained profits and the comparative information adjusted for the amounts relating to prior periods as disclosed in the consolidated statement of changes in equity.

3. Segment information

The Group is principally engaged in the activities of manufacturing, distribution and sale of electronic and electrical products, office equipment, the provision of value-added technical services and media-related business.

An analysis of the Group's turnover and contribution from operations by business segment for the six months ended 30 June, 2003 is set out below:

	Group turnover		Contribution to (loss)/ profit from operations	
	Six months ended 30 June,		Six months ended 30 June,	
	2003	2002	**2003**	2002 restated
	HK$'000	*HK$'000*	***HK$'000***	*HK$'000*
Principal activities				
Manufacturing, distribution and sale of electronic and electrical products and office equipment	**465,561**	441,000	**(11,438)**	998
Value-added technical services	**23,382**	27,469	**7,090**	(3,025)
Media-related business	**—**	1,864	**(202)**	(10,404)
	488,943	470,333	**(4,550)**	(12,431)
Unallocated operating income and expenses			**(9,609)**	(7,408)
			(14,159)	(19,839)

No analysis of the Group's turnover and contribution from operations by geographical segment has been presented as almost all the Group's operating activities are carried out in the People's Republic of China (the "PRC") and less than 10 per cent of the Group's turnover and contribution from operations were derived from activities conducted outside the PRC.

4. Non-operating income/(expenses)

	Six months ended 30 June, 2003 HK$'000	2002 HK$'000
Net realised/unrealised gain on equity securities	**936,966**	—
Impairment loss on non-trading securities	**(36,980)**	—
Gain on disposal of interest in subsidiaries	**2,855**	—
Loss on disposal of interest in associates	**—**	(462)
Provision for diminution in value of a property held for sale	**(16,022)**	—
Impairment loss on goodwill	**(10,026)**	—
Provision for winding up of subsidiaries	**(595)**	(3,135)
Provision for loan receivable	**(4,080)**	—
Others	**(679)**	—
	871,439	(3,597)

5. Profit/(loss) from ordinary activities before taxation

Profit/(loss) from ordinary activities before taxation is arrived at after charging/(crediting):

	Six months ended 30 June, 2003 HK$'000	2002 restated HK$'000
Interest on borrowings	**700**	789
Amortisation of negative goodwill	**(65)**	(7,676)
Amortisation of positive goodwill	**2,324**	1,592
Depreciation	**4,085**	4,462
Cost of inventories	**428,442**	408,577
Provision for write down in value of obsolete inventories	**1,256**	1,103
Provision for bad and doubtful debts	**7,522**	2,308
Gain on disposal of property, plant and equipment	**(1)**	(19)
Management fees	**1,301**	1,301

6. Taxation

	Six months ended 30 June, 2003 HK$'000	2002 restated HK$'000
Hong Kong profits tax	—	—
Income tax outside Hong Kong in the PRC ("PRC income tax")	**1,666**	155
Deferred taxation	**3**	(491)
	1,669	(336)
Share of associate's PRC income tax	**1**	138
	1,670	(198)

No provision for Hong Kong profits tax has been made in the accounts for the period as the Hong Kong companies of the Group sustained losses for taxation purposes during the period. PRC income tax is calculated at the applicable rates on the estimated taxable income outside Hong Kong in the PRC.

7. Earnings/(loss) per share

(a) Basic earnings/(loss) per share

The calculation of basic earnings/(loss) per share is based on the profit for the period attributable to shareholders of HK$386,651,000 (2002 (restated): loss of HK$16,028,000) and on the weighted average number of 1,198,564,406 ordinary shares (2002: 1,198,564,406 shares) in issue during the period.

(b) Diluted earnings/(loss) per share

Diluted earnings/(loss) per share is not presented because there were no dilutive potential ordinary shares in existence during the period or the prior period.

8. Interest in associates

	At 30 June, 2003 HK$'000	At 31 December, 2002 HK$'000
Share of net assets of unlisted associates	**124,152**	135,831
Goodwill	**42,632**	43,820
	166,784	179,651

9. Other financial assets

	At 30 June, 2003 HK$'000	At 31 December, 2002 HK$'000
Non-trading securities — equity securities		
— Listed in Hong Kong	**14,620**	27,520
— Unlisted	**27,198**	27,198
	41,818	54,718
Loan receivable	**15,300**	15,300
Less: Provision	**(7,650)**	(3,570)
	7,650	11,730
	49,468	66,448
Market value of listed securities	**14,620**	27,520

9. Other financial assets *(Cont'd)*

(a) Included in unlisted equity securities is a 9.51% equity interest in China Cable Information Network Company Limited ("China Cable") with a carrying value of HK$22,785,000 (at 31 December, 2002: HK$22,785,000). This investment is held in trust on behalf of the Group by Stone Group Corporation, a minority shareholder of the Group.

(b) Loan receivable is the amount advanced to the founders of an associate, East.net Technology Investment Ltd. ("East.net"), which is secured by the 51% equity interest in East.net owned by these founders. Loan receivable is interest bearing at the prevailing lending rate of The Hongkong and Shanghai Banking Corporation Limited and is not expected to be settled within the next twelve months.

10. Investments

	At 30 June, 2003	At 31 December, 2002
	HK$'000	*HK$'000*
Listed equity securities, at market value		
— in Hong Kong	**1,610**	1,400
— outside Hong Kong	**1,374,843**	480,398
	1,376,453	481,798

11. Inventories

Included in inventories are raw materials, work in progress and finished goods carried at net realisable value of HK$24,265,000 (at 31 December, 2002: HK$33,661,000).

12. Trade and other receivables

	At 30 June, 2003 HK$'000	At 31 December, 2002 HK$'000
Debtors, prepayments and other receivables	**133,108**	188,594
Gross amount due from customers for contract work	**11,157**	16,175
Amounts due from associates	**15,638**	10,916
Amounts due from related companies	**27,075**	35,258
	186,978	250,943

Included in the Group's debtors, prepayments and other receivables are trade debtors (net of specific provisions for bad and doubtful debts) with the following ageing analysis:

	At 30 June, 2003 HK$'000	At 31 December, 2002 HK$'000
Current	**48,130**	105,047
Due over 6 months but within 12 months	**32,299**	9,956
Due over 12 months but within 24 months	**4,921**	1,089
	85,350	116,092

All of the trade and other receivables are expected to be recovered within one year.

A credit period of 60 days to 90 days is normally granted to trade customers. Debtors with balances that are more than 6 months overdue are requested to settle all outstanding balances before any further credit is granted.

13. Trade and other payables

	At 30 June, 2003	At 31 December, 2002
	HK$'000	*HK$'000*
Creditors, accruals and other payables	**164,297**	196,099
Amounts due to associates	**2,246**	94
Amounts due to related companies	**11,255**	9,057
	177,798	205,250

Included in the Group's creditors, accruals and other payables are trade creditors with the following ageing analysis:

	At 30 June, 2003	At 31 December, 2002
	HK$'000	*HK$'000*
Due within 6 months or on demand	**39,770**	97,243
Due after 6 months but within 12 months	**32,041**	2,704
Due after 12 months but within 24 months	**2,982**	3,280
Due after 24 months but within 36 months	**4,864**	5,570
	79,657	108,797

14. Share capital

	2003	
	Number of shares	Amount
	'000	*HK$'000*
Authorised:		
Ordinary shares of HK$0.1 each	**2,000,000**	**200,000**
Issued and fully paid:		
At 1 January and 30 June	**1,198,565**	**119,856**

At 30 June, 2003, the outstanding options were as follows:

Date of options granted	Period during which options exercisable	Exercise price	Number of options outstanding
		HK$	
29 February, 2000	29 August, 2000 to 22 July, 2003	2.796	11,500,000
15 August, 2001	15 February, 2002 to 22 July, 2003	0.7264	14,151,000
22 May, 2002	22 May, 2002 to 21 May, 2012	0.792	17,356,000
22 May, 2002	22 August, 2002 to 21 May, 2012	0.792	19,575,000
22 May, 2002	22 August, 2003 to 21 May, 2012	0.792	19,575,000
22 May, 2002	22 August, 2004 to 21 May, 2012	0.792	19,575,000
22 May, 2002	22 August, 2005 to 21 May, 2012	0.792	19,575,000
31 December, 2002	31 December, 2002 to 30 December, 2012	0.476	113,856,000
			235,163,000

15. Reserves

	Capital redemption reserve	Share premium	Capital reserve	Exchange fluctuation reserve	Investment revaluation reserve	Retained profits/ (accumulated losses)	Total
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
At 1 January, 2003							
— as previously reported	151	1,022,607	15,274	(2,325)	(24,080)	(198,174)	813,453
— prior period adjustment in respect of deferred taxation *(note 2)*	—	—	—	—	—	3,015	3,015
— as restated	151	1,022,607	15,274	(2,325)	(24,080)	(195,159)	816,468
Unrealised loss on revaluation of investments in securities	—	—	—	—	(12,900)	—	(12,900)
Impairment loss transferred to income statement	—	—	—	—	36,980	—	36,980
Capital reserve released on disposal of a subsidiary	—	—	(1,016)	—	—	—	(1,016)
Exchange differences arising on consolidation	—	—	—	(567)	—	—	(567)
Profit for the period	—	—	—	—	—	386,651	386,651
At 30 June, 2003	**151**	**1,022,607**	**14,258**	**(2,892)**	**—**	**191,492**	**1,225,616**

16. **Material related party transactions**

(a) Transactions with and amounts paid to or received from Stone Group Corporation, a minority shareholder of the Group:

	Six months ended 30 June,	
	2003	2002
	HK$'000	*HK$'000*
Sale of traded products	**5,748**	10,529
Management fees (based on actual cost incurred) paid in relation to training, secretarial and general administrative services	**1,301**	1,301

(b) Purchase of traded products and component parts from a minority shareholder of a subsidiary	**19,445**	29,984

(c) Transactions with associates of the Group:

Sale of traded products	**22**	2,898
Purchase of lighting products	—	4,848

(d) Sale of GSM and GPS modules to an affiliated company of the Group	—	6,443

(e) The Group placed deposits totalling HK$7,098,000 (31 December, 2002: HK$7,841,000) as at 30 June, 2003 with Beijing Stone Finance Company, a subsidiary of Stone Group Corporation and a licensed financial company in the PRC.

16. Material related party transactions *(Cont'd)*

(f) One of the subsidiaries of Stone Group Corporation ("SGC Company") entered into an agreement with a wholly-owned subsidiary of the Group, whereby certain units of the investment property owned by this subsidiary are leased to SGC Company. SGC Company may sub-lease the units and will bear all the expenses of the investment property. The Group is entitled to share a portion of the net profit but not the loss, after deduction of expenses and relevant taxes, generated by SGC Company. No profit was shared by the Group in this arrangement as SGC Company incurred loss for the period.

(g) Stone Group Corporation holds in trust for Beijing Stone Electronic Technology Co., Ltd. ("Beijing Stone Electronic") the 9.51% investment in China Cable pursuant to an agreement entered into between the two parties in January, 2001. In April, 2003, another agreement was entered into between Beijing Stone Electronic and Stone Group Corporation pursuant to which Beijing Stone Electronic has the right to sell to Stone Group Corporation (which has the obligation to buy) its 9.51% equity interest in China Cable at a consideration equal to the fair value of the investment at the time of sale but to be capped at the original investment cost of HK$108,388,000. The effective period for exercising such right will end on 31 December, 2005.

17. Contingent liabilities

As at 30 June, 2003, the Group had contingent liabilities in respect of a counter guarantee for a bank loan of approximately HK$43.6 million (at 31 December, 2002: HK$52.9 million) granted to an associate.

18. Post balance sheet event

On 6 June, 2003, the Company and a placing agent entered into an agreement whereby (i) the placing agent agrees to procure subscribers to subscribe as principals for the convertible notes of a principal amount of at least HK$50 million, and (ii) the Company has granted to the placing agent the option (the "Option") to require the Company to issue additional convertible notes up to an additional principal amount of HK$350 million for subscription by the subscribers upon the terms and conditions of the placing agreement. On 14 July, 2003, convertible notes of HK$50 million were issued accordingly. The Option is exercisable by the placing agent on or before 13 January, 2005.

19. Comparative figures

Certain comparative figures have been adjusted as a result of changes in accounting policy for income taxes in order to comply with SSAP 12 (revised), details of which are set out in Note 2.

Independent Review Report to the Board of Directors of Stone Electronic Technology Limited

Introduction

We have been instructed by the Company to review the interim financial report set out on pages 1 to 19.

Respective responsibilities of directors and auditors

The Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited require the preparation of an interim financial report to be in compliance with the relevant provisions thereof and Statement of Standard Accounting Practice 25 "Interim financial reporting" issued by the Hong Kong Society of Accountants. The interim financial report is the responsibility of, and has been approved by, the directors.

It is our responsibility to form an independent conclusion, based on our review, on the interim financial report and to report our conclusion solely to you, as a body, in accordance with our agreed terms of engagement, and for no other purpose. We do not assume responsibility towards or accept liabilities to any other person for the contents of this report.

Review work performed

We conducted our review in accordance with Statement of Auditing Standards 700 "Engagements to review interim financial reports" issued by the Hong Kong Society of Accountants. A review consists principally of making enquiries of Group management and applying analytical procedures to the interim financial report and based thereon, assessing whether the accounting policies and presentation have been consistently applied unless otherwise disclosed. A review excludes audit procedures such as tests of controls and verification of assets, liabilities and transactions. It is substantially less in scope than an audit and therefore provides a lower level of assurance than an audit. Accordingly we do not express an audit opinion on the interim financial report.

Review conclusion

On the basis of our review which does not constitute an audit, we are not aware of any material modifications that should be made to the interim financial report for the six months ended 30 June, 2003.

KPMG

Certified Public Accountants

Hong Kong, 22 September, 2003

INTERIM DIVIDEND

The Directors resolved not to declare an interim dividend for the six months ended 30 June, 2003 (2002: Nil).

MANAGEMENT DISCUSSION AND ANALYSIS

Financial Performance

Despite the outbreak of SARS in the PRC region and other parts of the world which widely affected the economies and business activities in the PRC, the Group managed to keep up the pace of its business development. For the six months ended 30 June, 2003, the Group posted an increase of 4.0% to record an unaudited turnover of HK$488.9 million. Profit attributable to shareholders for the period was HK$386.7 million, representing a remarkable improvement as compared to a loss of HK$16.0 million recorded for the same period in 2002. This was mainly attributable to the significant appreciation of the Group's short-term investment in SINA Corporation ("SINA") .

Business Review

The Group is principally engaged in the manufacture and distribution of electronic and electrical products, which include industrial controllers and invoice printers. Turnover analysis by products and businesses for the period under review is as follows:

	Six months ended 30 June,		
	2003	2002	%
	HK$ million	*HK$ million*	+/(-)
Manufacture and distribution business (by major products)			
Industrial controllers	**219.8**	167.8	31.0
Stone-OKI printers	**81.7**	83.0	(1.6)
Gold Tax products	**23.4**	10.1	131.7
Uninterruptible power system ("UPS") equipment	**26.3**	53.1	(50.5)
Digital graphic products	**36.1**	19.7	83.2
Computers	**22.5**	52.9	(57.5)
Others	**55.7**	54.4	2.4
	465.5	441.0	
Fee income from value-added technical services	**23.4**	27.5	(14.9)
Media-related business	**—**	1.8	(100)
	488.9	470.3	

Manufacture and Distribution of Electronic Products

During the period under review, industrial controllers continued to be the Group's main revenue source, accounting for 44.9% of its total turnover. In the face of increasingly intense competition following China's accession to WTO, the Group, with the aim to enhance the competitiveness of the products it distributes, agreed with its suppliers to sell products at lower prices. Stimulated by these promotion efforts, turnover from industrial controllers increased by 31.0% to HK$219.8 million.

The Group distributes a range of industrial controllers for many internationally well-known brands, including Fuji, Siemens, Omron and Allen Bradley. During the first half of 2003, the Group continued to be the main PRC agent for these brands, ranking among the top three PRC agents in terms of sales volume, retaining its market leadership.

Another major product Stone-OKI printers accounted for 16.7% of the Group's total turnover. Loaded with Chinese software applications developed by the Group, the Stone-OKI printers are mainly used for the printing of Chinese invoices and bank passbooks. Major clients of this product include banks, post offices, securities companies, etc. Under the shadow of SARS outbreak in the second quarter of 2003, certain customers delayed the placement of purchasing orders. Turnover from the sales of Stone-OKI printers, as a result, saw a slight decline of 1.6% to HK$81.7 million for the first half of 2003.

The Group distributes technology products for two internationally renowned corporations, namely Invensys Inc and Roland DG Corporation. It distributes a range of UPS equipment from Invensys Plc, including Powerware UPS equipment, management software and systems. It is also the exclusive distributor of Roland DG Corporation's digital graphic products which include wide format inkjet printers, cutters, 3D scanners, etc. The distribution of these two types of technology products recorded a turnover of HK$26.3 million and HK$36.1 million respectively.

The Group made its way into the branded computer market in the PRC in 2002 through the establishment of a joint venture with a Singapore listed company, Achieva Investment Pte Ltd. for the manufacture and distribution of branded computer products in the PRC. During the period under review, turnover from the sales of computers under the brands of "Stone" and "Stone Collaborative" amounted to HK$6.3 million.

There are two major types of Gold Tax Products. One of them is the sales tax control cashiers ("STC Cashiers") stipulated by the State Tax Bureau ("STB") of China as a device for the collection of sales tax in the service industry. The Group was a pioneer in obtaining the rights to launch pilot sales of STC Cashiers in 20 designated cities in over 8 provinces in China in 2002. Furthermore, the Group secured sales rights in 5 additional regions including Shanghai and Beijing, laying solid foundations for the future development of this business. Another Gold Tax product is the anti-counterfeiting tax control machines ("ATC Machines"). Also stipulated by STB of China, ATC Machines are specially designed to counteract fake value-added tax invoices. Since the STB refused to accept hand-written invoices from 1 July, 2003, sales of ATC Machines increased to HK$20.8 million, a remarkable increase as compared to HK$6.2 million during the same period last year.

Other products distributed by the Group include semi-conductors, starters, fluorescence tubes and other electronic products. Turnover for these products for the six months ended 30 June, 2003 amounted to HK$55.7 million.

Value-added Technical Services

The Group started to place emphasis on the development of value-added technical services in 2002. In bundling the sale of hardware products with value-added technical services such as consultancy, technical support and customized software, the Group enhanced the value of its products and increased its competitiveness. Among these value-added technical services, the Group offered exclusive large-scale training programmes and installation services for the use of ATC Machines to customers in the western part of Beijing. For the six months ended 30 June, 2003, revenue from such training and installation services amounted to HK$13.7 million, representing an increase of HK$9.7 million as compared to the same period in 2002. However, since the projects newly contracted during the first half of the year are still in the initial stage of development, turnover for the value-added technical services recorded a slight decrease of 14.9% as compared to the corresponding period last year, amounting to HK$23.4 million.

Major Investments

The Group holds equity stakes in the NASDAQ-listed SINA through a 51% owned subsidiary. Since the share price of SINA saw a significant surge during the period under review, the Group disposed of part of its equity stakes, decreasing its shareholding from 9,476,524 shares (representing approximately 20.6%) to 8,706,524 shares (representing approximately 18.3%). The profit from the sale of SINA's shares amounted to HK$3.3 million. Based on the closing price of US$20.25 per SINA's share as at 30 June, 2003, after deducting minority interests, the unrealised profit from the investment in SINA held by the Group amounted to approximately HK$476.1 million.

Issue of Convertible Notes

The Group entered into a placing agreement with First Shanghai Securities Limited ("First Shanghai") for procuring the subscription of convertible notes for the principal amount of HK$50 million on a fully underwritten basis on 6 June, 2003. The said convertible notes were issued on 14 July, 2003. Assuming the full exercise of the HK$50 million convertible notes, a total of 96,153,846 new shares will be issued, representing approximately 8.0% of the existing issued share capital of the Company and approximately 7.4% of the enlarged issued share capital of the Company. Net proceeds from the issue of the convertible notes, after deducting expenses, were approximately HK$48.2 million. The Group intends to use the proceeds to acquire or invest in complementary businesses or to establish joint ventures which will complement its businesses.

Gross Profit

Gross profit decreased by HK$1.3 million or 2.0% to HK$60.5 million for the first half of 2003, as compared to the same period in 2002. The gross profit margin decreased to 12.4% for the first half of 2003 from 13.1% for the same period in 2002. This was principally attributed to the adjustment of selling price of industrial controllers to stimulate the sales as discussed above.

Distribution Costs, Administrative Expenses and Other Operating Expenses

Distribution costs increased by HK$2.6 million or 9.5% to HK$29.9 million for the first half of 2003, as compared to HK$27.3 million for the same period in 2002. This was resulted from the increase in marketing and promotion expenses as well as a larger salesforce to boost sales.

Administrative expenses decreased by HK$17.1 million or 34.7% to HK$32.2 million for the first half of 2003, as compared to HK$49.3 million for the same period in 2002. This was principally attributable to the drastic decrease in administrative expenses of Sun Stone. As a percentage of the total turnover, administrative expenses decreased to 6.6% for the first half of 2003, as compared to 10.5% for the same period in 2002.

Other operating expenses increased by HK$7.3 million or 88.0% to HK$15.6 million for the first half of 2003, as compared to HK$8.3 million for the same period in 2002. This was mainly due to an increase in provision for bad and doubtful debts which amounted to HK$5.2 million.

Liquidity and Capital Resources

The Group's primary liquidity needs are to fund daily operations and direct investments. At 30 June, 2003, the Group had working capital of HK$1,734.9 million, which included a cash balance of HK$264.6 million (including restricted cash of HK$1.5 million), as compared to working capital of HK$858.5 million, which included a cash balance of HK$217.0 million (including restricted cash of HK$3.4 million) at 31 December, 2002.

The current ratio was 8.4 times at 30 June, 2003, while at 31 December, 2002 it was 4.4 times. Cash and cash equivalents increased by HK$49.4 million due to partial disposal of equity stakes in SINA.

Inventories decreased by HK$22.6 million to HK$141.8 million at 30 June, 2003 when compared to 31 December, 2002, and the inventory turnover improved from 2.4 months at 31 December, 2002 to 2.2 months at 30 June, 2003. The improvement was mainly attributable to better inventories and procurement controls.

The Group had available banking facilities of HK$116.7 million at 30 June, 2003, which included letter of credit arrangements, overdrafts and other facilities commonly used by manufacturing and distribution companies. All these banking facilities bear interest at floating rates generally based on prime lending rates and are subject to periodic review. At 30 June, 2003, the Group had utilized approximately HK$49.4 million of its credit facilities. The Group believes that internal funds and the existing banking facilities will enable the Group to meet anticipated future cash flow requirements.

Use of Proceeds

The Group raised HK$234 million, net of expenses, under a private placement of 115,000,000 new shares in 1999. The proceeds have been used as follows:

— approximately HK$70 million for the acquisition of subsidiaries and other investments;

— approximately HK$62 million for the development of new businesses and for general working capital.

The remaining balance of approximately HK$102 million will be used for continuing investments in technology-related businesses and for general working capital.

Financial Position

As at 30 June, 2003, the Group had cash and cash equivalents of HK$263.1 million. Bank and other borrowings stood at HK$49.4 million. The gearing ratio was approximately 3.7% as compared to 5.0% at 31 December, 2002.

Details of Charges on Group Assets

As at 30 June, 2003, properties with carrying value of HK$14.0 million were pledged with banks as collateral against banking facilities and a term loan to subsidiaries of the Group. In addition, fixed deposits amounting to HK$1.5 million were pledged in respect of a bank guarantee issued to the customer of a subsidiary.

Contingent Liabilities

As at 30 June, 2003, the Group had provided a counter guarantee of approximately HK$43.6 million for a bank loan granted to an associate.

Hedging

As the Group makes its purchases substantially from overseas, it is the Group's policy to enter into foreign exchange forward contract to hedge against foreign exchange fluctuation whenever necessary.

Employees

As at 30 June, 2003, the Group employed a total of 875 (31 December, 2002: 913) employees, of which 846 (31 December, 2002: 884) were employed in the PRC and 29 (31 December, 2002: 29) were in Hong Kong. Out of the 846 employees in the PRC, 24 were temporary employees. In addition to receiving salaries and bonuses, employees are also entitled to other benefits, with medical subsidies and employer's contributions to Mandatory Provident Fund for Hong Kong staff, and Central Pension Scheme and supplementary defined contribution retirement plans managed by independent insurance companies for PRC staff. Share options may also be granted to certain employees of the Group as incentives.

Outlook

Having experienced the intense market competition brought about by international enterprises and the severe challenges of the outbreak of SARS in the first half of the year, the Group believes that the pent-up market demand will gradually be released with the end of the epidemic. The Group expects improved sales performance in the second half of the year. It will continue to achieve its goal of enhancing values. Apart from consolidating its market position, it will also proactively capture the opportunities arising after the SARS outbreak.

In addition to actively developing its core businesses, the Group will pursue investments with attractive returns. Looking ahead, the Group will continue to adopt a prudent approach in its management and investment with a view to generating stable long-term revenues, rewarding shareholders' long-term support with outstanding results.

DIRECTORS' INTERESTS IN SHARES

The directors who held office at 30 June, 2003 had the following interests in the share capital of the Company and short position and its associated corporation (within the meaning of Part XV of the Securities and Futures Ordinance (the "SFO")) as recorded in the register kept by the Company pursuant to section 352 of the SFO:

	Ordinary Shares of HK$0.1 each of the Company				
	Personal interests	Family interests	Corporate interests	Other interests	% of the total issued shares
Mr. Duan Yongji	5,040,000	—	—	—	0.421

Note: Beijing Stone Investment Company Limited ("Stone Investment") together with its associates (as defined in the Listing Rules) holds a total of 407,110,053 shares in the Company. Stone Investment is owned as to 42.3% by Stone Jiu Guang New Technology Development (Holdings) Company Limited ("Stone Jiu Guang"), 6.7% by Stone Group Corporation and 51% by the Beijing Stone Investment Company Limited Employees' Shareholding Society ("Employees' Shareholding Society"). Stone Jiu Guang is owned as to 36% by Stone Group Corporation. In addition, Stone Group Corporation indirectly holds 92,374,413 shares in the Company. Messrs, Duan Yongji, Zhang Disheng, Shen Guojun, Li Wenjun (who resigned as a director of the Company on 22 May, 2003), Zhu Xiduo and Chen Xiaotao (collectively as "the said Directors") are also employees of Stone Group Corporation. So long as the said Directors remain as employees of Stone Group Corporation, each of them together with the other employees collectively own interests in the assets of Stone Group Corporation but none of them has any specific interest in Stone Group Corporation.

Save as disclosed above and interests of directors of the Company in the share options as disclosed in "Share Option Schemes", none of the directors or chief executive had any interests or short position in the share capital, underlying shares or debentures of the Company or any associated corporation as recorded in the register kept by the Company pursuant to section 352 of SFO.

SHARE OPTION SCHEMES

The Company has two share option schemes, namely old share option scheme adopted on 23 July, 1993 and terminated on 12 April, 2002 ("Old Scheme") and new share option scheme adopted on 12 April, 2002 ("New Scheme"). Each option gives the holder the right to subscribe for one ordinary share. Movement of the share options (including share options granted to the directors) were as follows.

	No. of options outstanding at the beginning of the period	No. of options lapsed during the period	No. of options outstanding at the period end	Date granted	Period during which options exercisable	Price per share on exercise of options	Market value per share at date of grant of options	% of the total issued shares
						HK$	*HK$*	
Old Scheme								
Mr. Duan Yongji	7,500,000	—	7,500,000	29-02-2000	29-08-2000 to 22-07-2003	2.796	3.575	0.626
	8,000,000	—	8,000,000	15-08-2001	15-02-2002 to 22-07-2003	0.7264	0.98	0.667
Mr. Li Wenjun	4,000,000	—	4,000,000	29-02-2000	29-08-2000 to 22-07-2003	2.796	3.575	0.334
	2,151,000	—	2,151,000	15-08-2001	15-02-2002 to 22-07-2003	0.7264	0.98	0.179
Mr. Shen Guojun	4,000,000	—	4,000,000	15-08-2001	15-02-2002 to 22-07-2003	0.7264	0.98	0.334

Note: Mr. Li Wenjun resigned as a director of the Company on 22 May, 2003. All the options granted to the directors under the Old Scheme as disclosed above were lapsed fully on 22 July, 2003.

	No. of options outstanding at the beginning of the period	No. of options lapsed during the period	No. of options outstanding at the period end	Date granted	Period during which options exercisable	Price per share on exercise of options *HK$*	Market value per share at date of grant of options *HK$*	% of the total issued shares
New Scheme								
Mr. Duan Yongji *(Note a)*	3,900,000	—	3,900,000	22-05-2002	22-08-2002 to 21-05-2012	0.792	0.78	0.325
Mr. Shen Guojun *(Note a)*	4,000,000	—	4,000,000	22-05-2002	22-08-2002 to 21-05-2012	0.792	0.78	0.334
Mr. Li Wenjun *(Note a & f)*	3,000,000	—	3,000,000	22-05-2002	22-08-2002 to 21-05-2012	0.792	0.78	0.250
Mr. Zhu Xiduo *(Note a)*	3,000,000	—	3,000,000	22-05-2002	22-08-2002 to 21-05-2012	0.792	0.78	0.250
Mr. Chen Xiaotao *(Note b)*	8,000,000	—	8,000,000	22-05-2002	22-05-2002 to 21-05-2012	0.792	0.78	0.667
Mr. Zhang Disheng *(Note c & f)*	10,400,000	—	10,400,000	22-05-2002	22-05-2002 to 21-05-2012	0.792	0.78	0.868
Contracted employees *(Note d)*	87,556,000	24,200,000	63,356,000	22-05-2002	22-05-2002 to 21-05-2012	0.792	0.78	5.286
Contracted employees *(Note e)*	119,856,000	6,000,000	113,856,000	31-12-2002	31-12-2002 to 30-12-2012	0.476	0.47	9.499

Notes:

a. The options granted to these grantees shall be exercisable in the following four batches ("Vesting Period"):

   (i) Not more than 25% of options granted exercisable from 22-08-2002 to 21-08-2003;

   (ii) Not more than 50% of options granted exercisable from 22-08-2003 to 21-08-2004;

   (iii) Not more than 75% of options granted exercisable from 22-08-2004 to 21-08-2005; and

   (iv) Free to exercise from 22-08-2005 to 21-05-2012;

b. Free to exercise 4,000,000 options from 22-05-2002 to 21-05-2012 and the remaining 4,000,000 options are subject to the Vesting Period set out in Note (a).

c. Free to exercise 5,000,000 options from 22-05-2002 to 21-05-2012 and the remaining 5,400,000 options are subject to the Vesting Period set out in Note (a).

d. Free to exercise 8,356,000 options from 22-05-2002 to 21-05-2012 and the remaining 55,000,000 options are subject to the Vesting Period set out in Note (a).

e. Free to exercise 113,856,000 options from 31-12-2002 to 30-12-2012.

f. Mr. Li Wenjun resigned as a director of the Company on 22 May, 2003 and Mr. Zhang Disheng was appointed as a director of the Company on 22 May, 2003. The interests disclosed for Mr. Zhang Disheng represent the options granted to him prior to his appointment.

The consideration paid by each of the above directors and employees for the share options granted was HK$1.0.

During the period, except for options lapsed as mentioned above, no option was granted, exercised or cancelled pursuant to the Old Scheme or the New Scheme.

Save as disclosed above, at no time during the period was the Company or any of its subsidiaries a party to any arrangement to enable the directors or chief executive of the Company or their respective associate (as defined under the Listing Rules) to acquire benefits by means of acquisition of shares in , or debentures of, the Company or any other body corporate, or had exercised such rights.

SUBSTANTIAL INTERESTS IN THE SHARE CAPITAL OF THE COMPANY

As at 30 June, 2003 to the best knowledge of the directors, the following parties (other than a director or chief executive of the Company) were recorded in the register kept by the Company under section 336 of the SFO as being directly or indirectly interested in 5% or more of the issued share capital of the Company:

	Notes	**Number of Shares**	**% of the total issued Shares**
Stone Investment	*1*	407,110,053	33.97
Employees' Shareholding Society	2	407,110,053	33.97
Stone Jiu Guang	2	407,110,053	33.97
Stone Group Corporation	2	499,484,466	41.67

Notes:

1. The shareholding of 407,110,053 shares comprises the combined shareholdings of Stone Investment and its associates (as defined in the Listing Rules).

2. Stone Investment is owned as to 42.3% by Stone Jiu Guang, 6.7% by Stone Group Corporation and 51% by Employees' Shareholding Society which are accordingly deemed to be interested in the said 407,110,053 shares. In addition, Stone Group Corporation indirectly holds 92,374,413 shares of the Company.

Saved as disclosed above, the Company has not been notified of any other interest representing 5% or more of the issued share capital of the Company and recorded in the register of substantial shareholders maintained under Section 336 of the SFO as at 30 June, 2003.

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

Neither the Company nor any of its subsidiaries purchased, sold and redeemed any of the Company's listed securities during the six months ended 30 June, 2003.

AUDIT COMMITTEE

The Audit Committee has reviewed with the management the accounting principles and practices adopted by the Group and has discussed auditing, internal control and financial reporting matters including a general review of the unaudited financial statements for the six months ended 30 June, 2003. The interim financial report for the period ended 30 June, 2003 is unaudited, but has been reviewed, in accordance with the Statement of Auditing Standards 700 "Engagements to Review Interim Financial Reports" issued by the HKSA, by KPMG, whose review report is included in 2003 Interim Report to be despatched to the shareholders of the Company.

COMPLIANCE WITH THE CODE OF BEST PRACTICE

None of the Directors of the Company is aware of any information which would reasonably indicate that the Company is not, or was not in compliance with the Code of Best Practice, as set out in Appendix 14 of the Listing Rules, at any time during the six months ended 30 June, 2003.

By order of the Board
Duan Yongji
Chairman

Hong Kong, 22 September, 2003