

CHAIRMAN'S STATEMENT

Business Review

Foreword

Culturecom Group has been heading in the direction of development R&D of Chinese Linux technologies, including (1) Chinese Character Generating Engine (CCGE), (2) Chinese Voice Engine (CVE) and Conceptual Judgment System Technology and (3) the related Linux software technologies, such as Midori Linux embedded operating system and Red Office. Our efforts in the R&D of these three spheres have achieved significant results, which have found favor in the eyes of and are adopted by certain technological companies, like IBM, IT companies of the V-Dragon Industry Alliance and others. Based on this core technology, we have developed various Chinese IT products and applications and have marketed them all in succession. Besides, we have adopted the marketing strategy of "eTown (Digital web-town)" that targets the market of first-time computer users of 1.2 billion population in China to establish an eTown community.

Technological Business Development

The V-Dragon 3210 Processor, based on the Group's CCGE and IBM's PowerPC Technology, has completed its related mother-board design and accessory software development and has been marketed for use in the embedded system products. Among them, the designing plan for mother-board of Tax Terminal/POS Machine has passed China's technological examination and verification. Presently, the Chinese Government is implementing the tax terminal project nationwide, which has entered its tender invitation stage. As our mother-board design has been agreed to adopt by a number of manufacturers, it is believed that substantial income and profits will be crystallized in the near future.

The overall operation mode of eTown has been formed after the activation of the first eTown in Yun'an county, Guangdong province of China in July 2004. The Municipal Government of Yunfu City, Guangdong province will be scheduled to convene a district-wide eTown mobilization meeting in January 2005, and the installation of eTown for 4 counties and cities and 55 towns within the district is scheduled to be completed by the first quarter of next year. At the "17th Meeting of Mayors of Huaihai Economic Zone, the PRC" held in November this year, it was also duly resolved to adopt the Group's eTown solution to build a unified information management and development platform for a population of 120,000,000 within the Zone's 20 cities, 133 counties and 463 towns. Thereafter, with the active support of the Municipal Government of Xuzhou City, the Group has set about the construction of Xuzhou eTown Platform, the first eTown platform in this Zone. In this regard, Xuzhou Government has instructed Xuzhou Telecom Bureau to sign with the Group the "Bundled-Sales Cooperative Agreement in relation to Xuzhou Telecom Broadband Business, eTown Computer and eTown Services", thereby Xuzhou Telecom Bureau will be able to provide local governments, schools, hospitals, enterprises and families with the Group's Chinese Linux Computer and eTown Services. Subsequent to the activation of eTown in Xuzhou, Huaihai Economic Zone, the Group will, acting in the spirit of the "summary of minutes of the 17th Meeting of Mayors of Huaihai Economic Zone, the PRC", continue to co-operate with the governments of all tiers within the Zone to complete zone-wide coverage of eTown services within the next two years.

CHAIRMAN'S STATEMENT (Continued)

Technological Business Development (Continued)

On the other hand, the Group has been negotiating with key agency of China's central government to initiate nation-wide construction work of eTown, and the next planned districts will be the Three Provinces in Northeast, the northwest areas, the Central China Economic District, the Economic Districts of Fujian, Zhejiang, Hunan and Jiangxi and the Economic Districts of Sichuan, Shaanxi, Gansu, Ningxia and etc. The Group believes that the advancement of the eTown marketing strategy will bring a considerable income and profits for the Group itself.

Red Office developed by the Group launched its latest version in June this year and was well received and purchased by the Beijing Municipal Government and other local governments following the purchase bid one after another, such as Shanxi Provincial Government and Hunan Provincial Government. As the Chinese Government tends to use software that possesses self-owned copyright of intellectual properties and open source solution, the Group believes that Red Office will account for a notable share in the future purchases from the Chinese Government.

The Group also made use of the Chinese Character DNA technology to successfully complete the R&D of CVE by the end of this year, and planned to develop jointly with IBM the world's first new-generation "Chinese Smart Computer Chip" that has voice processing capability. Such smart chip features the function of having a computer endowed with the capability to "hear, speak, comprehend and judge", and to enable the user interacting with the computer itself by means of natural language, spurring on a trend of application R&D of new-generation domestic intelligent home appliances. On the occasion, man and machine may communicate with each other through natural conversation, breaking through the restrictions associated with the use of key-board, hand-writing pad and other input methods, and enabling a 'serving the people' application status of the computer.

Comic Business

Comic business has undergone 21% growth after economic recovery of both Hong Kong and Asian markets. However, the future growth momentum will rely on development of new business and new market. By the first half of year 2004/2005, comic department of the Group has signed content distributionship agreement with over 10 major mobile phone service providers (SPs) in China with their total registered members amounted to more than 500 million.

Building up comic content based value added service platform on mobile phone, PC and TV channel is the focus of the year. For the licensing business of multi-media products, we licensed our comic title "Chinese Hero" to TV producers to produce two series of TV opera in 2004 and 2005 respectively. Shooting of the first episode already started by October. In addition, "Dragon Tiger Hero" is licensed to produce movie and is scheduled to be on screen by summer of 2005. Besides, more than 20 comic titles have been licensed to be published in China by 2005 and 2006.

CHAIRMAN'S STATEMENT (Continued)

Prospects

Cuturecom Group will carry through the above development strategy, utilizing developed technologies while collaborating unceasingly with friendly enterprises for further co-operation and promotion, in order to produce more fore-front products that fit in with the emerging need of eTown community. Meantime, the Group will, in addition to consolidating its success in Yun'an and Yunfu District and Huaihai Economic Zone that accounts for 10% of the total population of China, proactively expand the Group's eTown project into other areas of China. The Group will focus on the new first time computer users market of 1.2 billion to build eTown information infrastructure and eTown community. We are much confident that the Group has entered its harvest period and our R&D fruits will dominate the market in the short run.