



INTERIM REPORT 2006



SinoCom

SinoCom Software Group Limited
中訊軟件集團股份有限公司

(Incorporated in the Cayman Islands with limited liability)
(Stock Code: 0299)

Contents

Chairman's Statement	2
Condensed Consolidated Income Statement	3
Condensed Consolidated Balance Sheet	4
Condensed Consolidated Statement of Changes in Equity	5
Condensed Consolidated Cash Flow Statement	6
Notes to the Condensed Financial Statements	7
Management Discussion and Analysis	18

Chairman's Statement

On behalf of the board of directors (the "Board") of the Company, I am delighted to present the interim results of the company and its subsidiary companies (collectively as the "Group") for the six months ended 30 June 2006 (the "Period").

For the first half of the financial year, the Group continued to grow steadily in its business performance. Revenue achieved HK\$163 million as targeted. Although net income was roughly the same as the previous comparable period, recovery rate of the Group was at a significantly high level of about 80%. This encouraging performance was attributed to the software outsourcing industry's continual growth and the thriving economy in the PRC. The expansion of existing customers as well as the contribution from new clients was the key driving force for this sustained business growth. On the other hand, our cost was put under good control. The Group has optimized its people structure to achieve cost efficiency so as to maintain our competitiveness. Thus, our average wages and administration costs have stayed in line with the continuing business development of the Group.

It is no doubt that the fluctuation of Japanese Yen will impact the Group's profit results, as its revenue base was mostly denominated in Yen. To this end, the Group has implemented a policy to control related foreign exchange risk to reduce its inherent impact.

In the current financial year the Group will continue to grow and absorb the industry's professionals through acquisitions. However, this strategic direction will not restrict our acquisition targets to those operated in the PRC but also to those software outsourcing ventures in Japan. A survey shows that most of Japan's software outsourcing businesses was taken up by their local companies. As a result, by making this strategic move we not only can enter the huge Japanese software outsourcing market but also can source the low or medium-ended processes into China. And this will ultimately benefit our business in the PRC.

Due to the close economic relationship between China and Japan, as well as their linguistic and cultural similarities, the PRC has the definite competitive advantage in gaining the business from Japan. And Japan's recent economic recovery has fueled its demand for software outsourcing services. In the meantime, about 60% of the PRC's software outsourcing revenues comes from Japan. And it has been growing at an annual rate exceeding 30%. Hence, its potential growth looks promising. The Group will continue to focus in this high growth market – Japan. After taking into account these favourable factors, the Board is confident about our business prospect in the second half of the financial year.

Now I would like to extend my appreciation to the Board, our shareholders and business partners for their relentless support. And I would like to express my heartfelt gratitude to our strenuous staff force.

Wang Zhiqiang
Chairman and CEO

Hong Kong, 29 August 2006

Condensed Consolidated Income Statement

For The Six Months Ended 30 June 2006

	Notes	Six months ended 30 June	
		2006 HK\$ (unaudited)	2005 HK\$ (unaudited)
Turnover		163,355,949	123,076,051
Cost of services		(93,663,070)	(57,500,190)
Gross profit		69,692,879	65,575,861
Other income		5,402,248	1,108,472
Administrative expenses		(32,417,074)	(23,767,904)
Finance costs		(9,108)	–
Share of result of an associate		(65,446)	–
Profit before tax	4	42,603,499	42,916,429
Income tax expense	5	(7,258,505)	(6,746,582)
Profit for the period		35,344,994	36,169,847
Attributable to:			
Equity holders of the parent		35,700,686	35,696,248
Minority interests		(355,692)	473,599
		35,344,994	36,169,847
Earnings per share	7		
– Basic		3.30 HK cents	3.34 HK cents
– Diluted		3.20 HK cents	3.21 HK cents

Condensed Consolidated Balance Sheet

At 30 June 2006

	Notes	30 June 2006 HK\$ (unaudited)	31 December 2005 HK\$ (audited)
Non-current assets			
Property, plant and equipment	8	12,822,119	10,967,431
Interests in an associate	9	1,958,602	–
Deposits made for acquisition of subsidiaries	10	5,055,259	–
Goodwill		6,289,788	6,289,788
		26,125,768	17,257,219
Current assets			
Trade and other receivables	11	65,418,386	51,542,189
Amounts due from related parties	13	2,585	233,773
Cash and cash equivalents		287,290,202	283,944,864
		352,711,173	335,720,826
Current liabilities			
Trade and other payables	12	27,789,042	29,118,335
Amounts due to related parties	13	227,909	12,140
Bank loans	14	308,426	297,230
Current tax liabilities		6,641,262	3,727,100
		34,966,639	33,154,805
Net current assets			
		317,744,534	302,566,021
		343,870,302	319,823,240
Capital and reserves			
Share capital	15	27,383,978	27,016,778
Reserves		308,881,219	285,160,762
Equity attributable to equity holders of the parent		336,265,197	312,177,540
Minority interests		7,236,002	7,120,095
Total equity			
		343,501,199	319,297,635
Non-current liabilities			
Bank loans	14	369,103	525,605
		343,870,302	319,823,240

Condensed Consolidated Statement of Changes in Equity

For The Six Months Ended 30 June 2006

	Attributable to equity holders of the parent											Minority interests	Total equity
	Share capital	Share premium	Capital reserve	Other reserve	General reserve fund	Shareholder's contribution	Translation reserve	Share option reserve	Retained earnings	Total			
	HK\$	HK\$	HK\$	HK\$	HK\$	HK\$	HK\$	HK\$	HK\$	HK\$	HK\$		
At 1 January 2005	26,589,078	115,537,034	10,657,000	5,077,863	8,881,288	2,725,949	(502,755)	1,126,361	90,856,544	260,948,362	526,611	261,474,973	
Exchange differences arising on translation of overseas operations recognised directly in equity	-	-	-	-	-	-	440,605	-	-	440,605	(49,479)	391,126	
Profit for the period	-	-	-	-	-	-	-	-	35,696,248	35,696,248	473,599	36,169,847	
Total recognised income and expense for the period	-	-	-	-	-	-	440,605	-	35,696,248	36,136,853	424,120	36,560,973	
Exercise of share options	419,200	14,115,700	-	-	-	-	-	(4,054,900)	-	10,480,000	-	10,480,000	
Recognition of equity-settled share based payments	-	-	-	-	-	-	-	3,482,136	-	3,482,136	-	3,482,136	
Acquisition of a subsidiary	-	-	-	-	-	-	-	-	-	-	575,543	575,543	
Dividend paid	-	-	-	-	-	-	-	-	(26,589,078)	(26,589,078)	-	(26,589,078)	
At 30 June 2005	27,008,278	129,652,734	10,657,000	5,077,863	8,881,288	2,725,949	(62,150)	553,597	99,963,714	284,458,273	1,526,274	285,984,547	
At 1 January 2006	27,016,778	130,987,815	10,657,000	5,077,863	16,232,460	2,725,949	2,532,981	2,002,709	114,943,985	312,177,540	7,120,095	319,297,635	
Exchange differences arising on translation of overseas operations recognised directly in equity	-	-	-	-	-	-	2,334,885	-	-	2,334,885	471,599	2,806,484	
Profit for the period	-	-	-	-	-	-	-	-	35,700,686	35,700,686	(355,692)	35,344,994	
Total recognised income and expense for the period	-	-	-	-	-	-	2,334,885	-	35,700,686	38,035,571	115,907	38,151,478	
Exercise of share options	367,200	13,391,139	-	-	-	-	-	(4,578,339)	-	9,180,000	-	9,180,000	
Recognition of equity-settled share based payments	-	-	-	-	-	-	-	6,590,542	-	6,590,542	-	6,590,542	
Dividend paid	-	-	-	-	-	-	-	-	(29,718,456)	(29,718,456)	-	(29,718,456)	
At 30 June 2006	27,383,978	144,378,954	10,657,000	5,077,863	16,232,460	2,725,949	4,867,866	4,014,912	120,926,215	336,265,197	7,236,002	343,501,199	

Condensed Consolidated Cash Flow Statement

For The Six Months Ended 30 June 2006

	Six months ended 30 June	
	2006	2005
	HK\$	HK\$
	(unaudited)	(unaudited)
Net cash from operating activities	29,348,814	20,775,815
Net cash used in investing activities:		
Deposits made for acquisition of subsidiaries	(5,055,259)	–
Purchase of property, plant and equipment	(4,377,254)	(2,133,186)
Investment in an associate	(2,024,048)	–
Interest received	4,221,767	947,991
Acquisition of a new subsidiary	–	261,438
Other investing cash flows	–	14,176
	(7,234,794)	(909,581)
Net cash used in financing activities:		
Dividend paid	(29,718,456)	(26,589,078)
Repayment of bank loans	(145,306)	–
Proceeds on issue of shares	9,180,000	10,480,000
	(20,683,762)	(16,109,078)
Net increase in cash and cash equivalents	1,430,258	3,757,156
Cash and cash equivalents at beginning of the period	283,944,864	247,305,655
Effects of foreign exchange rate change	1,915,080	390,014
Cash and cash equivalents at end of the period	287,290,202	251,452,825

Notes to the Condensed Financial Statements

For The Six Months Ended 30 June 2006

1. BASIS OF PREPARATION

The condensed financial statements have been prepared in accordance with the applicable disclosure requirements of Appendix 16 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited and with Hong Kong Accounting Standard 34 “Interim Financial Reporting”.

2. PRINCIPAL ACCOUNTING POLICIES

The condensed financial statements have been prepared on the historical cost basis.

The accounting policies used in the condensed financial statements are consistent with those followed in the preparation of the Group’s annual financial statements for the year ended 31 December 2005.

In the current interim period, the Group has applied, for the first time, a number of new standards, amendments and interpretations (“new HKFRSs”) issued by the Hong Kong Institute of Certified Public Accountants, which are either effective for accounting periods beginning on or after 1 December 2005 or 1 January 2006. The adoption of the new HKFRSs had no material effect on how the results for the current or prior accounting periods have been prepared and presented. Accordingly, no prior period adjustment has been required.

The Group has not early applied all the new standard, amendment or interpretations that have been issued but are not yet effective. The directors of the Company anticipate that the application of these standard, amendment or interpretations will have no material impact on the results and the financial position of the Group.

3. SEGMENT INFORMATION

For management purpose, the Group is currently engaged in the provision of services in two markets, the People’s Republic of China (“PRC”) and Japan. The Group’s primary format for reporting segment information is geographical segment.

The following table provides an analysis of the Group's turnover by location of markets, irrespective of the origin of the services:

Income statement for the six months ended 30 June 2006

	PRC HK\$	Japan HK\$	Consolidated HK\$
Turnover	18,503,813	144,852,136	163,355,949
Segment results	2,024,207	40,622,229	42,646,436
Other income			5,402,248
Finance costs			(9,108)
Share of results of an associate	(65,446)	-	(65,446)
Unallocated corporate expenses			(5,370,631)
Profit before tax			42,603,499

Income statement for the six months ended 30 June 2005

	PRC HK\$	Japan HK\$	Consolidated HK\$
Turnover	12,440,353	110,635,698	123,076,051
Segment results	2,345,625	41,748,456	44,094,081
Other income			1,108,472
Unallocated corporate expenses			(2,286,124)
Profit before tax			42,916,429

The Group is principally engaged in the provision of outsourcing software development services. For the six months ended 30 June 2006, 93.9% of turnover are generated from outsourcing software development services (for the six months ended 30 June 2005 is 93.6%) and accordingly, the directors of the Company consider the Group has a single reportable business segment only.

4. PROFIT BEFORE TAX

Profit before tax has been arrived at after charging (crediting) the following items:

	Six months ended 30 June	
	2006 HK\$	2005 HK\$
Depreciation of property, plant and equipment	2,104,166	1,374,207
Write off of property, plant and equipment	22,136	34,492
Operating lease rentals in respect of premises	10,100,043	5,977,334
Share option expense	6,590,542	3,482,136
Foreign exchange (gain) loss	(1,135,666)	6,189,622
Interest income	(4,221,767)	(947,991)

5. INCOME TAX EXPENSE

	Six months ended 30 June	
	2006 HK\$	2005 HK\$
PRC income tax	4,714,690	4,625,615
Japan income tax	2,543,815	2,120,967
	7,258,505	6,746,582

Zhongxun Computer System (Beijing) Company Limited ("SinoCom Beijing"), a subsidiary of the Company, is recognised as a technologically advanced enterprise by the relevant PRC government authorities since 26 September 1995. Pursuant to the Income Tax Laws, on 18 November, 1996, the External Branch of State Tax Authority in Beijing granted approval to SinoCom Beijing to enjoy the reduced state enterprise income tax rate of 15%. In addition, SinoCom Beijing is subject to a more favorable income tax rate of 10% pursuant to the relevant PRC regulations as the annual export revenue of its software development business is more than 70% of SinoCom Beijing's total annual income.

Other PRC subsidiaries of the Company do not have significant tax charges for the period.

Taxation arising in Japan is calculated at a progressive statutory rate of 22% on the portion of taxable income not exceeding YEN8,000,000 (equivalent to approximately HK\$537,000 and HK\$567,000 for the six months ended 30 June 2006 and 30 June 2005, respectively) and 30% on the portion of taxable income in excess of YEN8,000,000.

6. DIVIDEND

On 20 May 2005, a final dividend of HK10 cents per share was paid to the shareholders in respect of the financial year ended 31 December 2004.

On 19 May 2006, a final dividend of HK11 cents per share was paid to the shareholders in respect of the financial year ended 31 December 2005.

The directors do not recommend the payment of an interim dividend.

7. EARNINGS PER SHARE

The calculation of the basic and diluted earnings per share attributable to the ordinary equity holders of the parent is based on the following data:

	Six months ended 30 June 2006 HK\$	2005 HK\$
Earnings		
Earnings for the purpose of basic and diluted earnings per share (profit for the period attributable to equity holders of the parent)	35,700,686	35,696,248
Number of shares		
Weighted average number of ordinary shares for the purpose of basic earnings per share	1,083,169,981	1,068,287,812
Effect of dilutive potential ordinary shares: Share options	32,321,842	45,128,452
Weighted average number of ordinary shares for the purposes of diluted earnings per share	1,115,491,823	1,113,416,264

The weighted average number of ordinary shares for the purpose of basic earnings per share has been adjusted for the Company's share subdivision in May 2006, details of which are set out in note 15.

8. MOVEMENTS IN PROPERTY, PLANT AND EQUIPMENT

During the period, the Group spent HK\$4,377,254 (six months ended 30 June 2005: HK\$2,133,186) on additions to property, plant and equipment.

9. INTERESTS IN AN ASSOCIATE

The amount represents the Group's 30% equity interest in an associate, DIR System Technology (Beijing) Co. Ltd., a company incorporated in the PRC and principally engaged in development and marketing of computer software products in the PRC.

10. DEPOSITS MADE FOR ACQUISITION OF SUBSIDIARIES

In March 2006, the Group entered into sale and purchase agreements with certain independent third parties to acquire a total of 53% equity interest in a company, which is incorporated in the PRC and principally engaged in the development of software outsourced from Japan, for an aggregate cash consideration of RMB15,900,000 (equivalent to approximately HK\$15,288,000). As at 30 June 2006, the Group has paid a deposit of RMB1,800,000 (equivalent to approximately HK\$1,748,000) for the acquisition, the completion of which is conditional upon satisfaction of certain precedent conditions including approval by and registration with the relevant government authorities. The outstanding consideration as at 30 June 2006 for the acquisition is shown as the capital commitment set out in note 18.

In addition, the Group has paid a deposit of YEN49,000,000 (equivalent to approximately HK\$3,307,000) for the acquisition of a company, which is incorporated in Japan and principally engaged in the provision of software integration, integrated solutions and the distribution of software products. The relevant share transfer agreement relating to the acquisition was entered into in August 2006, details of which are set out in note 19.

11. TRADE AND OTHER RECEIVABLES

The Group normally allows credit period of 30 to 45 days to trade customers.

The following is an aged analysis of trade debtors at the balance sheet date:

	30 June 2006 HK\$	31 December 2005 HK\$
0-30 days	32,722,464	31,020,458
31-60 days	4,778,521	4,069,396
61-90 days	3,946,386	3,021,165
Over 90 days	4,654,069	970,258
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Trade debtors	46,101,440	39,081,277
Income tax receivable	6,434,207	4,131,585
Other debtors	9,794,217	3,369,778
Deposits	662,738	3,852,865
Prepayments	2,425,784	1,106,684
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	65,418,386	51,542,189

12. TRADE AND OTHER PAYABLES

The following is an aged analysis of trade creditors at the balance sheet date:

	30 June 2006 HK\$	31 December 2005 HK\$
0-60 days	957,786	625,345
61-90 days	1,630	7,690
Over 90 days	882	29,293
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Trade creditors	960,298	662,328
Accruals and other payables	26,828,744	28,456,007
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	27,789,042	29,118,335

13. AMOUNTS DUE FROM/TO RELATED PARTIES

	30 June 2006 HK\$	31 December 2005 HK\$
Amount due from a director	–	231,188
Amounts due from shareholders	2,585	2,585
	2,585	233,773
Amounts due to directors	215,769	–
Amount due to a shareholder	12,140	12,140
	227,909	12,140

The amounts are unsecured, non-interest bearing and have no fixed terms of repayments.

14. BANK LOANS

During the period, the Group repaid borrowings of HK\$145,306.

15. SHARE CAPITAL

	Number of shares	HK\$
Authorised:		
Ordinary shares of HK\$0.10 each, at 1 January 2005 and 31 December 2005	1,000,000,000	100,000,000
Subdivision of HK\$0.10 share each into HK\$0.025 share each (Note i)	3,000,000,000	–
Ordinary shares of HK\$0.025 at 30 June 2006	4,000,000,000	100,000,000
Issued and fully paid:		
At 1 January 2005	265,890,782	26,589,078
Exercise of share options	4,277,000	427,700
At 31 December 2005	270,167,782	27,016,778
Subdivision of HK\$0.10 share each into HK\$0.025 share each (Note i)	810,503,346	–
Exercise of share options (Note ii)	1,080,671,128	27,016,778
	14,688,000	367,200
At 30 June 2006	1,095,359,128	27,383,978

Notes:

- (i) At an extraordinary general meeting held on 10 May 2006, the shareholders of the Company has approved the subdivision of each of the existing issued and unissued shares of HK\$0.10 each in the share capital of the Company into four shares of HK\$0.025 each (the "Share Subdivision").
- (ii) Subsequent to the Share Subdivision, share options to subscribe for 14,688,000 ordinary shares of HK\$0.025 each were exercised during the period at HK\$0.625 per share (see note 16).

16. SHARE OPTIONS

The Company's share option scheme (the "Scheme") for eligible employees was adopted pursuant to a resolution passed on 2 April 2004. As at 1 January 2006, the number of shares in respect of which options had been granted under the Scheme was 13,128,000 and the subscription price of the options is HK\$2.50 per share. On 24 January 2006, the Company granted further options which entitle the holders to subscribe for 5,130,000 shares at a subscription price of HK\$5.55 per share. Details of movements of the share options during the period are as follows:

	Number of share options
Outstanding at beginning of the period	13,128,000
Granted during the period	5,130,000
Change upon Share Subdivision (Note)	54,774,000
Exercised during the period	(14,688,000)
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Outstanding at end of the period	58,344,000

Note: As a result of the Share Subdivision in May 2006, the terms of the then outstanding share options are adjusted according to rules of the share option scheme as follows:

- (a) Each option to subscribe for one share shall be adjusted to an option to subscribe for four shares;
- (b) The existing subscription price of HK\$2.50 payable for each share to be issued upon the exercise of the options outstanding as at 1 January 2006 shall be adjusted such that the subscription price payable for each share to be issued upon the exercise of an option would be HK\$0.625; and
- (c) The existing subscription price of HK\$5.55 payable for each share to be issued upon the exercise of the options granted in January 2006 shall be adjusted such that the subscription price payable for each share to be issued upon the exercise of an option would be HK\$1.3875.

The options granted in January 2006 may be exercisable during the period from the first anniversary of the date of grant, being 24 January 2007 to 23 January 2016 (both days inclusive), in the following manner:

- (a) no part of the options may be exercisable prior to the first anniversary of the date of grant;
- (b) 25% of the options will be exercisable at any time on or after the first anniversary of the date of grant up to and including 23 January 2016;
- (c) a further 25% of the options will be exercisable at any time on or after the second anniversary of the date of grant up to and including 23 January 2016;
- (d) another 25% of the options will be exercisable at any time on or after the third anniversary of the date of grant up to and including 23 January 2016; and
- (e) the remaining 25% of the options will be exercisable at any time on or after the fourth anniversary of the date of grant up to and including 23 January 2016.

The closing price of the Company's shares immediately before 24 January 2006, the date of grant, was HK\$5.55 per share.

The weighted average closing price of the Company's shares immediately before the dates on which the option were exercised, was HK\$2.17 per share.

The options granted on 24 January 2006 have a fair value of HK\$0.53 per option which was determined at the date of grant using the Black-Scholes pricing model and adjusted for the Share Subdivision.

The following assumptions were used to calculate the fair value of these share options:

Market price on date of grant	HK\$5.55
Exercise price (before adjustments for Share Subdivision)	HK\$5.55
Expected life	6.25 years
Expected volatility	44%
Expected dividend yield	2.5%
Risk free rate	4.09%

For the purposes of calculating the above fair value, the number of share options granted has been reduced to reflect historical experience of forfeiture of 2% of options granted.

The Black-Scholes option pricing model requires the input of highly subjective assumptions, including the volatility of share price. Changes in subjective input assumptions can materially affect the fair value estimate.

17. OPERATING LEASE COMMITMENTS

At the balance sheet date, the Group had commitments for future minimum lease payments in respect of rented premises which fall due as follows:

	30 June 2006 HK\$	31 December 2005 HK\$
Within one year	16,071,995	17,593,284
In the second to fifth year inclusive	23,731,919	24,990,019
	39,803,914	42,583,303

Operating lease payments represent rentals payable by the Group for its office premises. Leases are negotiated for an average term of two years.

18. CAPITAL COMMITMENT

As at 30 June 2006, the Group is committed to payments of approximately RMB14,100,000 (equivalent to approximately HK\$13,697,000) in respect of the acquisition of a subsidiary as disclosed in note 10.

19. POST BALANCE SHEET EVENTS

In August 2006, the Group entered into a share transfer agreement with an independent third party to acquire a 75% equity interest in a company, which is incorporated in Japan and principally engaged in the provision of software integration, integrated solutions and the distribution of software products, for an aggregate cash consideration of YEN120,000,000 (equivalent to approximately HK\$8,158,000). The acquisition was completed in August 2006, and management are in the process of determining the financial impact of this acquisition.

In addition, in August 2006, the Group entered into an agreement to acquire a total of 20% further equity interest in an existing non-wholly subsidiary, SinoCom-Artm Technology Co. Ltd., which is incorporated in the PRC and principally engaged in the provision of outsourcing software development and technical support services, from the minority owners of the subsidiary for a cash consideration of RMB2,400,000 (equivalent to approximately HK\$2,329,000). The completion of the acquisition is conditional upon satisfaction of certain precedent conditions including approval by and registration with the relevant government authorities.

20. RELATED PARTY TRANSACTION

Compensation of key management personnel

The remuneration of directors and other members of key management during the period was as follows:

	Six months ended 30 June	
	2006 HK\$	2005 HK\$
Short-term benefits	5,989,904	6,385,356
Share-based payments	472,282	1,015,762
	6,462,186	7,401,118

The remuneration of directors is determined by the salary review committee. The remuneration of the key executives is determined by the internal salary review committee having regard to the performance of individuals and market trends.

Management Discussion And Analysis

FINANCIAL REVIEW

Operating Results for the Period

Turnover

Turnover of the Group for the six months ended 30 June, 2006 (the "Period") amounted to approximately HK\$163 million, representing an increase of approximately HK\$40 million, or 33%, over the same period in 2005. Revenue was derived from outsourcing software development services and from technical support services, which accounted for approximately 94% and 6% of the total revenue respectively. Market segments were divided into Japan and PRC and each accounted for approximately 89% and 11% respectively. Increase in revenue was mainly due to business expansion with additional headcounts. There were also contributions from newly acquired subsidiaries, not significantly though.

Gross profit and cost of sales

Gross profit of the Group for the Period amounted to approximately HK\$69.7 million, representing an increase of approximately HK\$4.1 million over that for the same period in 2005. Gross profit margin was approximately 42.7% which was higher than the industry average but less than that of last year same period. Weaken Japanese Yen (average exchange rate against HK dollar during the Period depreciated by approximately 8.7% compared the average exchange rate same period last year), higher cost of sales, and thinner margin of newly acquired subsidiaries accounted for the decrease of gross profit margin.

Cost of sales increased to approximately HK\$93.7 million, representing an increase of approximately HK\$36.2 million or 62.9%. Among which HK\$14.7 millions were the cost of sales of Shensoft, a newly acquired subsidiary in November 2005. The remaining HK\$21.5 million were increases mainly in labour costs due to higher upward salary adjustment to employees in 2006 and new headcount salaries.

Other income

The Group recorded foreign exchange gain of approximately HK\$1.1 million and interest income of approximately HK\$4.2 million for the Period.

Operating expenses

Operating expenses during the Period increased to approximately HK\$32.5 million, representing an increase of approximately HK\$8.7 million or 36.7% over the same period in 2005. Major increases included an increase of HK\$4 million share option expenses charged when comparing the same period in 2005 and HK\$3.3 million of the operating expenses of Shensoft consolidated. The remaining increase was attributable to salary and headcount increments of management staff and other general costs inflation.

Liquidity and Financial Resources

Net assets

As at 30 June 2006, the Group recorded total assets of approximately HK\$378.8 million which were financed by liabilities of HK\$35.3 million, minority interest of HK\$7.2 million and equity of HK\$336.3 million. The Group's net assets value as at 30 June 2006 increased by 7.5% to approximately HK\$343.5 million as compared to approximately HK\$319.3 million as at 31 December 2005.

Liquidity

The Group had a total cash and bank balances of approximately HK\$287.3 million as at 30 June 2006 (As at 31 December 2005: approximately HK\$283.9 million). Bank borrowings of HK\$0.67 million was bank loans to Shensoft before its acquisition by the Group. Current ratio of 10 times remained the same as at both 30 June 2006 and 31 December 2005.

Foreign exchange exposure

The Group generates most of the revenue in Japanese Yen and incurs most of the costs in RMB. Any depreciation of Japanese Yen against RMB will result in decrease in the income of the Group, which will have an adverse impact to the Group's profitability. To minimize exposure on foreign exchange fluctuations, the Group reviews its foreign exchange position and adopts appropriate measures from time to time. As at 30 June 2006, cash and bank balances of the Group consisted of approximately 10% in US dollars, 68% in Japanese Yen, 3% in RMB and 18% in HKD. The Group will convert its foreign currencies into RMB whenever exchange rates are favourable as a buffer to meet its expenses in RMB.

Pledge of Asset

As at 30 June 2006, the Group did not pledge any of its assets to obtain banking facilities nor have any charge on its assets (As at 31 December 2005: Nil).

Contingent Liabilities

As at 30 June 2006, the Group did not have any material contingent liabilities (As at 31 December 2005: Nil).

Major Transaction

In March 2006, the Group signed a conditional agreement to acquire 53% equity interests of Beijing Jbridge Information Technology Co., Ltd., whose major business is in provision of software development outsourcing services to customers in Japan from which the Group was envisaged to be beneficial by their quality software development staff so as to further expand the business. Conditions to the agreement have not yet been fulfilled; therefore, the acquisition is still pending for completion.

In August 2006, the Group acquired 75% equity interests of MIS Co., Ltd (“MIS”), a company incorporated in Japan. Directors are of the view that business scopes of MIS are in line with the principal business of the Group. The Group also entered into a conditional agreement to acquire additional 20% to a total of 80% equity interest in SinoCom-ArtM Technology Co., Ltd (“Beijing Hanyang”). Approval has been granted by the PRC Ministry of Commerce. Completion is pending for the registration routine procedure which is expected to be completed soon.

Directors believed that all these acquisitions would help to enlarge the revenue base of and would provide a growth prospect to the Group. The presence of the Group in Japan would be strengthened by virtue of its bonding with clients and strategic setups in Japan.

The Group is committed to providing strong support to its clients by improving their services and business performance. It is dedicated to endeavouring for the sustained and steady growth of return to its shareholders as always.

OUTLOOK

Momentum of demand from Japan continues to be very strong. There would be business as long as there are resources available to handle the software development work. Human resources still remain growth bottle neck of the industry, in particular, those senior engineers returning to China from Japan. The Group will continue to expand at targeted organic growth rate of 30% per annum while another 10% to 15% by acquisition for the coming years. The organic growth rate is considered as a realistic rate under control by the experience of the management. Acquisition growth rate will be subject to uncertainties as to availability of suitable targets and the timing of completion. To this end, the Group engaged a financial advisor in Japan

helping to identify target companies in addition to its own connections. The Group will put more focus to acquire companies in Japan enabling it to equip with more senior engineering resources to handle high level work. Once the Group engages high level work in a project in Japan, it will naturally create more business opportunities of mid and low level work of the same project in PRC.

EMPLOYEE AND REMUNERATION POLICIES

As at 30 June 2006, the Group employed 2,148 employees in China and Japan. Employees are remunerated based on their performance, work experience and the prevailing market rates. Performance related bonuses are granted on a discretionary basis. Other employee benefits include pension fund, insurance and medical coverage, training programs and participation in the Group's share option scheme.

SHARE OPTION SCHEME

As at 30 June 2006, there were options for 58,344,000 ordinary shares of HK\$0.025 each in the share capital of the Company (the "Share(s)") granted by the Company pursuant to the option scheme, as adopted by the shareholders of the Company on 2 April 2004 (the "Option Scheme"), which were valid and outstanding. No options were lapsed during the six months ended 30 June 2006.

New share options were granted under the Option Scheme during the Period, which allowed and enabled 20,520,000 units of new shares to be issued during specific of time.

AUDIT COMMITTEE

The Audit Committee of the Company, which is chaired by an independent non-executive director, currently comprises three independent non-executive directors. It meets at least two times a year and meetings are attended by external auditors, the chief finance officer and the company secretary for the purpose of discussing the nature and scope of audit work, setting and monitoring the Company's internal audit program and assessing the Company's internal controls. It has reviewed this interim report, including the unaudited interim financial statements for the Period which were not required to be audited, and has recommended their adoption by the Board.

COMPLIANCE WITH THE CODE ON CORPORATE GOVERNANCE PRACTICES

The Company is committed to maintaining a high standard of corporate governance. During the accounting period ended 30 June 2006, the Company had met the code provisions set out in the Code on Corporate Governance Practices contained in Appendix 14 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (“the Listing Rules”) except A.2.1 that Mr Wang Zhiqiang had been both the Chairman and Chief Executive Officer of the Company. The roles of the Chairman of the Board and the Chief Executive Officer were not separated because, to our belief, the separation might not enhance the Group’s efficiency and business operation. The balance of power and authority is ensured by regular discussion and meetings of the Board and active participation of independent non-executive directors. The Board continues to review its practices from time to time with an aim to improve the Group’s corporate governance practices so as to meet international best practice.

COMPLIANCE WITH THE MODEL CODE SET OUT IN APPENDIX 10 TO THE LISTING RULES

The Company has adopted a code of conduct regarding securities transactions by directors (“Code of Conduct”) on terms no less exacting than the required standard set out in the Model Code set out in Appendix 10 to the Listing Rules (“the Code”) and the Company has made specific enquiry of all directors that they have complied with the required standard set out in the Code and the Code of Conduct.

PURCHASE, SALE OR REDEMPTION OF LISTED SECURITIES

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

DIRECTORS’ INTEREST IN SHARES

As at 30 June 2006, the interests and short positions of the Directors and chief executive of the Company in the shares of HK\$0.025 each, underlying shares and debentures of the Company and its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance “SFO”) which were required to be notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interest and short positions which they are taken or deemed to have under such provisions of the SFO) of which were required, pursuant to section 352 of the SFO, to be entered in the register referred to therein or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Companies (“Model Code”) were as follows:

(a) *Interests in the Company*

Name of Director	Capacity/ Nature of interest	No. of shares of the Company	Note	Approximate percentage of shareholding
Mr Wang Xubing	Interest of a controlled corporation	563,000,000 (L)		51.38%
Mr Wang Zhiqiang	Interest of a controlled corporation	563,000,000 (L)		51.38%
Dr Shi Chongming	Beneficial owner	4,043,200 (L)		0.37%
Mr Siu Kwok Leung	Beneficial owner	4,280,000 (L)		0.39%

Notes:

1. These Shares are beneficially owned by China Way International Limited ("China Way"). By virtue of his 51% shareholding interest in China Way, Mr Wang Xubing is deemed or taken to be interested in the 563,000,000 Shares of the Company owned by China Way for the purpose of the SFO.
2. These Shares are beneficially owned by China Way. By virtue of his 49% shareholding interest in China Way, Mr Wang Zhiqiang is deemed or taken to be interested in the 563,000,000 Shares of the Company owned by China Way for the purpose of the SFO.
3. The Letter "L" denotes a long position in Shares.

(b) *Interests in associated corporations of the Company*

Name of associated corporation	Name of director	Capacity/ Nature of interest	No. of ordinary shares of US\$1.00 each	Percentage of shareholding
China Way	Mr Wang Xubing	Beneficial owner	51 (L)	51%
China Way	Mr Wang Zhiqiang	Beneficial owner	49 (L)	49%

Note: The letter "L" denotes a long position in Shares.

Save as disclosed herein, as at 30 June 2006, none of the Directors or chief executive of the Company had any interests or short positions in the Shares, underlying shares and debentures of the Company or any of its associated corporations (within the meaning of Part XV of the SFO) which were required to be notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests and short positions which they were taken or deemed to have under such provisions of SFO) or which were required, pursuant to Section 352 of the SFO, to be entered in the register referred to therein or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code.

Other than as stated above, at no time during the Period was the Company or any of its subsidiaries a party to any arrangement to enable the directors of the Company (including their spouse and children under 18 years of age) to acquire benefits by means of the acquisition of Shares in or debentures of the Company or any other body corporate.

SUBSTANTIAL SHAREHOLDERS' AND OTHER PERSONS' INTERESTS AND SHORT POSITIONS IN SHARES AND UNDERLYING SHARES

As at 30 June 2006, details of substantial shareholders' and other persons' (who are required to disclose their interests pursuant to Part XV of the SFO) 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 are as follows:—

(a) Interests in Shares

Name of shareholder	Capacity / Nature of interest	No. of shares of the Company	Note	Approximate percentage of shareholding
China Way	Beneficial owner	563,000,000 (L)		51.38%
Wang Xubing	Interest of a controlled corporation	563,000,000 (L)		51.38%
Wang Zhiqiang	Interest of a controlled corporation	563,000,000 (L)		51.38%
Madam Zhang Yue	Interest of spouse	563,000,000 (L)	1	51.38%
Madam Yuan Yue Ling	Interest of spouse	563,000,000 (L)	2	51.38%

Notes:

1. Madam Zhang Yue is the wife of Mr Wang Xubing and is deemed to be interested in the 563,000,000 Shares in which Mr Wang Xubing is deemed or taken to be interested for the purposes of the SFO.
2. Madam Yuan Yue Ling is the wife of Mr Wang Zhiqiang and is deemed to be interested in the 563,000,000 Shares in which Mr Wang Zhiqiang is deemed or taken to be interested for the purposes of the SFO.
3. The letter "L" denotes a long position in Shares.

(b) Short Position in Shares and Underlying Shares

Save as disclosed in paragraph (a) above, no other interest required to be recorded in the register kept under Section 336 of the SFO has been notified to the Company.