



2006/2007

Kantone Holdings Limited (Stock Code: 1059)

www.kantone.com

INTERIM REPORT

Kantone Holdings Limited (www.kantone.com) (stock code 1059) is a leading IT solutions provider, with expertise in high security, high reliability and high integrity communications networks established over 50 years of proven track record, resulting in trusted relationships with clients in the government and enterprise sectors. It commands a dominant position in the command and control communications solutions in the mission critical services sector, including emergency and rescue operations, and has a global presence in over 50 markets.

Kantone's latest addition to the backbone of high security, high reliability, and high integrity IT solutions is the business of e-Gaming, e-Lottery, Leisure and Entertainment, where Kantone is a market leader in China in the provision of software and technology infrastructure for one-stop electronic betting solutions. Kantone builds on its long history of online telephone call data handling systems and call centre software applications to develop integrated platforms with secure e-commerce solutions for global gaming and entertainment activities.

Kantone is listed on The Stock Exchange of Hong Kong Limited and is a subsidiary of Champion Technology Holdings Limited, a communications software group.



KANTONE HOLDINGS LIMITED

(Incorporated in the Cayman Islands with limited liability)

INTERIM REPORT

For the six months ended 31 December 2006

FINANCIAL HIGHLIGHTS

- Group turnover was HK\$702 million, up 6.7%
- Profit attributable to equity holders was HK\$188 million, up 18.9%
- EBITDA rose 22.8% to HK\$263 million
- Earnings per share was HK6.44 cents, up 2.7%
(Excluding impairment loss of HK\$25.8 million, earnings per share increased to HK7.33 cents.)
- Increased interim dividend of HK1.3 cents per share

The directors of Kantone Holdings Limited (the “Company” or “Kantone”) are pleased to announce the unaudited condensed consolidated financial statements of the Company and its subsidiaries (together the “Group”) for the six months ended 31 December 2006 together with the comparative unaudited figures for the corresponding period last year as follows:

CONDENSED CONSOLIDATED INCOME STATEMENT

For the six months ended 31 December 2006

		Six months ended 31 December	
		2006	2005
	Notes	HK\$'000 (Unaudited)	HK\$'000 (Unaudited)
Turnover	2	702,189	658,020
Cost of sales		(420,113)	(403,444)
Gross profit		282,076	254,576
Other income		12,612	6,596
Distribution costs		(21,511)	(25,925)
General and administrative expenses		(56,351)	(49,771)
Impairment loss recognised for available-for-sale investments/investments		(25,767)	–
Loss on fair value change of convertible bonds		–	(25,901)
Finance costs		(4,547)	(2,604)
Profit before taxation		186,512	156,971
Taxation	4	(41)	(268)
Profit for the period		<u>186,471</u>	<u>156,703</u>
Attributable to:			
Equity holders of the Company		187,623	157,742
Minority interests		(1,152)	(1,039)
		<u>186,471</u>	<u>156,703</u>
Dividends	5	<u>37,859</u>	<u>29,780</u>
Earnings per share	6		
– Basic		<u>HK6.44 cents</u>	<u>HK6.27 cents</u>
– Diluted		<u>HK6.25 cents</u>	N/A

CONDENSED CONSOLIDATED BALANCE SHEET

At 31 December 2006

		As at 31 December 2006 HK\$'000 (Unaudited)	As at 30 June 2006 HK\$'000 (Audited)
Non-current assets			
Property, plant and equipment	7	44,188	43,080
Development costs for systems and networks		702,933	549,656
Goodwill		36,795	36,795
Intangible assets		8,850	10,030
Available-for-sale investments		253,373	193,222
Deposits		562,571	465,071
		1,608,710	1,297,854
Current assets			
Inventories		29,053	26,772
Trade and other receivables	8	365,198	346,495
Taxation recoverable		80	79
Deposits, bank balances and cash		198,905	251,947
		593,236	625,293
Current liabilities			
Trade and other payables	9	56,905	69,999
Warranty provision		1,871	1,683
Amount due to ultimate holding company		45	103
Taxation payable		140	13
Bank borrowings – amount due within one year		99,651	54,019
Other borrowings – amount due within one year		2,360	2,650
Convertible bonds	10	77,830	18,219
		238,802	146,686
Net current assets		354,434	478,607
Total assets less current liabilities		1,963,144	1,776,461

	As at 31 December 2006 HK\$'000 (Unaudited)	As at 30 June 2006 HK\$'000 (Audited)
Non-current liabilities		
Bank borrowings – amount due after one year	765	1,061
Other borrowings – amount due after one year	700	2,349
Retirement benefits obligations	94,479	88,014
Deferred taxation	214	206
	<u>96,158</u>	<u>91,630</u>
Net assets	<u>1,866,986</u>	<u>1,684,831</u>
Capital and reserves		
Share capital	291,225	291,225
Reserves	1,560,437	1,377,325
Equity attributable to equity holders of the Company	1,851,662	1,668,550
Minority interests	15,324	16,281
	<u>1,866,986</u>	<u>1,684,831</u>

CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY (UNAUDITED)

For the six months ended 31 December 2006

	Attributable to equity holders of the Company							Minority interests	Total equity
	Share capital	Share premium	Dividend reserve	Subscription right reserve	Translation reserve	Retained profits	Total		
	HKS'000	HKS'000	HKS'000	HKS'000	HKS'000	HKS'000	HKS'000	HKS'000	HKS'000
At 1 July 2005	239,312	22,263	26,324	1,850	(8,507)	791,038	1,072,280	93	1,072,373
Exchange difference arising on translation of operations outside Hong Kong recognised directly in equity	-	-	-	-	4,583	-	4,583	(5)	4,578
Profit for the period	-	-	-	-	-	157,742	157,742	(1,039)	156,703
Total income and expense recognised for the period	-	-	-	-	4,583	157,742	162,325	(1,044)	161,281
On conversion of convertible bonds	7,416	21,545	-	-	-	-	28,961	-	28,961
On placement of shares	24,000	151,200	-	-	-	-	175,200	-	175,200
On acquisition of non-wholly owned subsidiaries	-	-	-	-	-	-	-	18,426	18,426
Expense incurred in connection with placement of shares	-	(5,452)	-	-	-	-	(5,452)	-	(5,452)
Dividends for the period	-	-	29,780	-	-	(29,780)	-	-	-
	31,416	167,293	29,780	-	-	(29,780)	198,709	18,426	217,135
At 31 December 2005 and 1 January 2006	270,728	189,556	56,104	1,850	(3,924)	919,000	1,433,314	17,475	1,450,789
Exchange difference arising on translation of operations outside Hong Kong recognised directly in equity	-	-	-	-	(4,122)	-	(4,122)	73	(4,049)
Profit for the period	-	-	-	-	-	174,958	174,958	(106)	174,852
Total income and expense recognised for the period	-	-	-	-	(4,122)	174,958	170,836	(33)	170,803

	Attributable to equity holders of the Company								
	Share capital <i>HKS'000</i>	Share premium <i>HKS'000</i>	Dividend reserve <i>HKS'000</i>	Subscription right reserve <i>HKS'000</i>	Translation reserve <i>HKS'000</i>	Retained profits <i>HKS'000</i>	Total <i>HKS'000</i>	Minority interests <i>HKS'000</i>	Total equity <i>HKS'000</i>
On acquisition of non-wholly owned subsidiaries	-	-	-	-	-	-	-	(1,161)	(1,161)
On conversion of convertible bonds	9,075	65,729	-	-	-	-	74,804	-	74,804
Dividend for the period	-	-	63,263	-	-	(63,263)	-	-	-
Dividend paid	-	-	(10,404)	-	-	-	(10,404)	-	(10,404)
Issue of shares as scrip dividend	11,422	39,296	(50,718)	-	-	-	-	-	-
	20,497	105,025	2,141	-	-	(63,263)	64,400	(1,161)	63,239
At 30 June 2006 and 1 July 2006	291,225	294,581	58,245	1,850	(8,046)	1,030,695	1,668,550	16,281	1,684,831
Exchange difference arising on translation of operations outside Hong Kong recognised directly in equity	-	-	-	-	(7,300)	-	(7,300)	195	(7,105)
Profit for the period	-	-	-	-	-	187,623	187,623	(1,152)	186,471
Total income and expense recognised for the period	-	-	-	-	(7,300)	187,623	180,323	(957)	179,366
Issue of convertible bonds	-	-	-	2,789	-	-	2,789	-	2,789
Proposed interim dividend	-	-	37,859	-	-	(37,859)	-	-	-
	-	-	37,859	2,789	-	(37,859)	2,789	-	2,789
At 31 December 2006	291,225	294,581	96,104	4,639	(15,346)	1,180,459	1,851,662	15,324	1,866,986

CONDENSED CONSOLIDATED CASH FLOW STATEMENT

For the six months ended 31 December 2006

	Six months ended	
	31 December	
	2006	2005
	<i>HK\$'000</i>	<i>HK\$'000</i>
	(Unaudited)	(Unaudited)
Net cash from operating activities	308,727	224,178
Net cash used in investing activities	(459,309)	(245,769)
Net cash from financing activities	55,343	161,421
Net (decrease) increase in cash and cash equivalents	(95,239)	139,830
Cash and cash equivalents at the beginning of the period	251,947	138,854
Effect of foreign exchange rate changes	473	(450)
Cash and cash equivalents at the end of the period	<u>157,181</u>	<u>278,234</u>
Represented by:		
Deposits, bank balances and cash	198,905	287,348
Bank overdrafts	(41,724)	(9,114)
	<u>157,181</u>	<u>278,234</u>

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

For the six months ended 31 December 2006

1. BASIS OF PREPARATION

The unaudited condensed consolidated financial statements have been prepared in accordance with the applicable disclosure requirements set out in Appendix 16 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited and with Hong Kong Accounting Standard (“HKAS”) 34 “Interim Financial Reporting” issued by the Hong Kong Institute of Certified Public Accountants (the “HKICPA”).

The condensed consolidated financial statements have been prepared on historical cost basis except for certain financial instruments, which are measured at fair values on initial recognition. The accounting policies adopted in the condensed consolidated financial statements are consistent with those followed in the preparation of the annual financial statements of the Company and its subsidiaries (the “Group”) for the year ended 30 June 2006.

The HKICPA has issued a number of new/revised HKFRSs that are first effective or available for early adoption for the current accounting period of the Group. The Group has adopted new/revised HKFRSs that are mandatory for the financial year ending 30 June 2007. The adoption of these new/revised HKFRSs has no significant impact on the Group’s results and financial position.

2. **TURNOVER AND SEGMENT INFORMATION**

For management purposes, the Group is currently organised into five main operating businesses – sales of general systems products, provision of services and software licensing, leasing of systems products, investments in e-commerce projects and holding strategic investments in advanced technology product development companies. These businesses are the basis on which the Group reports its primary segment information.

	Sales of general systems products <i>HKS '000</i>	Provision of services and software licensing <i>HKS '000</i>	Leasing of systems products <i>HKS '000</i>	Investments in e-commerce projects <i>HKS '000</i>	Strategic investments <i>HKS '000</i>	Consolidated <i>HKS '000</i>
Six months ended 31 December 2006						
TURNOVER						
External and total revenue	<u>445,110</u>	<u>242,034</u>	<u>5,384</u>	<u>2,700</u>	<u>6,961</u>	<u>702,189</u>
RESULTS						
Segment result	<u>72,679</u>	<u>132,368</u>	<u>714</u>	<u>2,555</u>	<u>(17,797)</u>	190,519
Interest income						5,554
Unallocated corporate expenses, net						(5,014)
Finance costs						(4,547)
Profit before taxation						<u>186,512</u>
Taxation						(41)
Profit for the period						<u>186,471</u>
Six months ended 31 December 2005						
TURNOVER						
External and total revenue	<u>430,351</u>	<u>209,261</u>	<u>8,294</u>	<u>3,641</u>	<u>6,473</u>	<u>658,020</u>
RESULTS						
Segment result	<u>71,859</u>	<u>97,128</u>	<u>5,641</u>	<u>3,496</u>	<u>6,217</u>	184,341
Interest income						5,052
Loss on fair value change of convertible bonds						(25,901)
Unallocated corporate expenses, net						(3,917)
Finance costs						(2,604)
Profit before taxation						<u>156,971</u>
Taxation						(268)
Profit for the period						<u>156,703</u>

3. DEPRECIATION AND AMORTISATION

	Six months ended	
	31 December	
	2006	2005
	<i>HK\$'000</i>	<i>HK\$'000</i>
Amortisation on:		
Development costs for systems and networks, included in cost of sales	65,952	48,838
Intangible assets, included in general and administrative expenses	1,180	–
Depreciation of property, plant and equipment, included in general and administrative expenses	5,223	6,173
	<u>72,355</u>	<u>55,011</u>
Total depreciation and amortisation	<u>72,355</u>	<u>55,011</u>

4. TAXATION

	Six months ended	
	31 December	
	2006	2005
	<i>HK\$'000</i>	<i>HK\$'000</i>
The charge comprises:		
Hong Kong Profits Tax		
– underprovision in prior years	–	12
Taxation in other jurisdictions	41	256
	<u>41</u>	<u>268</u>
	<u>41</u>	<u>268</u>

Hong Kong Profits Tax is calculated at 17.5% (2005: 17.5%) on the estimated assessable profits derived from Hong Kong. Taxation in other jurisdictions is calculated at the rates prevailing in the respective jurisdictions.

The low effective tax rate is attributable to the fact that a substantial portion of the Group's profit neither arises in, nor is derived from, Hong Kong and is accordingly not subject to Hong Kong Profits Tax and such profit is either exempted or not subject to taxation in any other jurisdictions.

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5. DIVIDENDS

Dividends represents interim dividend of HK1.3 cents (2005: HK1.1 cents) per share, in scrip form with a cash option.

The interim dividend is calculated based on 2,912,252,703 shares in issue at 31 December 2006.

6. EARNINGS PER SHARE

The calculation of the basic and diluted earnings per share is based on the following data:

	Six months ended 31 December	
	2006	2005
	HK\$ '000	HK\$ '000
Earnings for the purpose of calculating basic earnings per share	187,623	<u>157,742</u>
Effect of dilutive potential ordinary shares:		
Interest of convertible bonds	224	
Issue costs of convertible bonds	<u>2,130</u>	
Earnings for the purpose of calculating diluted earnings per share	<u>189,977</u>	
	Number of shares	
	'000	'000
Weighted average number of shares for the purpose of calculating basic earnings per share	2,912,253	<u>2,516,528</u>
Effect of dilutive potential ordinary shares in respect of convertible bonds	<u>129,123</u>	
Weighted average number of shares for the purpose of calculating diluted earnings per share	<u>3,041,376</u>	

The conversion of the Company's outstanding convertible bonds did not have dilution effect on earnings per share for the period ended 31 December 2005 since the conversion would result in an increase in profit per share.

7. PROPERTY, PLANT AND EQUIPMENT

	<i>HK\$ '000</i>
Net book value at 1 July 2006	43,080
Currency realignment	2,661
Additions	3,764
Disposals	(94)
Depreciation	(5,223)
Net book value at 31 December 2006	<u>44,188</u>

At 31 December 2006, certain land and buildings of the Group with a net book value of HK\$12,688,000 (30 June 2006: HK\$11,865,000) were pledged to a bank as security for banking facilities granted to the Group. Loss on disposal of property, plant and equipment of the Group amounted to HK\$60,000 for the period.

8. TRADE AND OTHER RECEIVABLES

	31 December 2006 <i>HK\$'000</i>	30 June 2006 <i>HK\$'000</i>
Trade receivables	132,669	198,973
Guaranteed distribution receivables	36,843	32,163
Other receivables	195,686	115,359
	<u>365,198</u>	<u>346,495</u>

The Group maintains a well-defined credit policy regarding its trade customers dependent on their credit worthiness, nature of services and products, industry practice and condition of the market with credit period ranging from 30 to 180 days. The aged analysis of trade receivables at the reporting date is as follows:

	31 December 2006 <i>HK\$'000</i>	30 June 2006 <i>HK\$'000</i>
0-60 days	106,099	152,492
61-90 days	25,314	43,446
91-180 days	636	1,276
> 180 days	620	1,759
	<u>132,669</u>	<u>198,973</u>

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9. TRADE AND OTHER PAYABLES

As at 31 December 2006, the balance of trade and other payables included trade payables of HK\$12,706,000 (30 June 2006: HK\$11,143,000). The aged analysis of trade payables at the balance sheet date is as follows:

	31 December 2006 HK\$'000	30 June 2006 HK\$'000
0-60 days	7,861	7,487
61-90 days	491	630
91-180 days	–	267
> 180 days	4,354	2,759
	<u>12,706</u>	<u>11,143</u>

10. CONVERTIBLE BONDS

	31 December 2006 HK\$'000	30 June 2006 HK\$'000
1% convertible bonds – unlisted	<u>77,830</u>	<u>18,219</u>

On 23 August 2006, the Company issued additional tranche 1 convertible bonds of US\$8,000,000 due 2008 (the “Additional Tranche 1 Convertible Bonds”). The Additional Tranche 1 Convertible Bonds bear interest at the rate of 1% per annum and interest will be payable semi-annually in arrears in June and December each year. During the period, there was no conversion in convertible bonds. At 31 December 2006, principal value of US\$8,100,000 of the convertible bonds remained outstanding.

In the opinion of the directors of the Company, the fair value change of the convertible bonds during the period was immaterial and accordingly, no adjustment had been made to the financial statements.

11. CAPITAL COMMITMENTS

	31 December 2006 HK\$'000	30 June 2006 HK\$'000
Capital expenditure in respect of property, plant and equipment, and development costs for systems and networks authorised but not contracted for	<u>143,375</u>	<u>179,025</u>

12. OPERATING LEASE ARRANGEMENTS**The Group as lessee**

At the balance sheet date, the Group had future minimum lease payments payable under non-cancellable operating leases in respect of rented premises and machinery and equipment which fall due as follows:

	31 December 2006		30 June 2006	
	Land and buildings HK\$'000	Machinery and equipment HK\$'000	Land and buildings HK\$'000	Machinery and equipment HK\$'000
Within one year	142	3,058	280	2,517
In the second to fourth year inclusive	2,499	3,014	2,335	3,558
	<u>2,641</u>	<u>6,072</u>	<u>2,615</u>	<u>6,075</u>

Leases are negotiated for an average term of one to four years and rentals are fixed for an average term of one to four years.

The Group as lessor

At the balance sheet date, the Group contracted with tenants in respect of plant and machinery and telecommunications networks which fall due as follows:

	31 December 2006 HK\$'000	30 June 2006 HK\$'000
Within one year	18,922	10,874
In the second to fifth year inclusive	21,156	20,756
Over five years	1,195	1,803
	<u>41,273</u>	<u>33,433</u>

INTERIM DIVIDEND AND SCRIP DIVIDEND SCHEME

The directors have resolved to pay an interim dividend of HK1.3 cents per share for the six months ended 31 December 2006 (2005: HK1.1 cents per share) to shareholders whose names appear on the register of members of the Company on 20 April 2007. Total interim dividend payment amounts to HK\$37.9 million, an increase of 27 percent as compared with HK\$29.8 million of last corresponding period.

The interim dividend will be satisfied by allotment of new shares of the Company, credited as fully paid, by way of scrip dividend, with an alternative to the shareholders to elect to receive such dividend (or part thereof) in cash in lieu of such allotment (the “Scrip Dividend Scheme”).

The Scrip Dividend Scheme is subject to the granting by the Listing Committee of The Stock Exchange of Hong Kong Limited of a listing of and permission to deal in the shares to be issued pursuant thereto. A circular setting out the details of the Scrip Dividend Scheme together with the form of election will be sent to the shareholders of the Company as soon as practicable.

It is expected that certificates for shares to be issued under the Scrip Dividend Scheme and dividend warrants will be dispatched to those entitled thereto on or before 15 June 2007.

CLOSURE OF REGISTER OF MEMBERS

The register of members of the Company will be closed from 16 April 2007 to 20 April 2007, both days inclusive, during which period no transfer of shares of the Company will be effected. In order to qualify for the above interim dividend and the Scrip Dividend Scheme, all transfers of shares accompanied by the relevant share certificates must be lodged with the Company’s Branch Share Registrars in Hong Kong, Secretaries Limited, at 26th Floor, Tesbury Centre, 28 Queen’s Road East, Wanchai, Hong Kong no later than 4:00 p.m. on 13 April 2007.

MANAGEMENT DISCUSSION AND ANALYSIS

The Group maintained growth in turnover and profit for its core business. Worldwide demand for customised solutions, spurred by China's economic growth, continued. With a track record in delivering high security, high reliability and high integrity communications networks, the Group maintained its leadership position in the niche market of narrowband wireless communications, serving a broad range of customers from hospitals, hotels, aerospace, manufacturing, retail, government departments, to fire and rescue services. The Group's profitability was partially offset by impairment provisions in relation to some of the Group's investments.

Financial Results

The Group achieved a turnover of HK\$702 million for the six months ended 31 December 2006 (the "Period"), an increase of 6.7 percent as compared with HK\$658 million for the six months ended 31 December 2005 (the "Previous Period"). Gross profit increased by 11 percent to HK\$282.1 million, and gross margin remained steady at 40 percent. Such results were attributable to the Group's continued investment in product development and systems advancement, thereby enhancing the value-added features of its products and solutions. The slower growth in turnover reflected the Group's continuing effort to reduce reliance on general systems products where margins continued to come under pressure, and a corresponding increase in focus on services and software solutions with the associated higher margins.

Profit attributable to equity holders was HK\$188 million, an increase of 18.9 percent compared with HK\$158 million for the Previous Period. Earnings per share for the Period was HK6.44 cents, an increase of 2.7 percent. EBITDA (earnings before interest, taxation, depreciation and amortisation) rose by 22.8 percent to HK\$263 million.

Included in the profit before taxation of HK\$186.5 million was an impairment loss of HK\$25.8 million in relation to the Group's various investments. As a general principle of prudence in anticipation of the increasing volatilities in the global financial markets and operating environments, the Group decided to provide for impairment where the income producing assets may be affected in the coming years. This is in accordance with the latest accounting standards requiring annual review of the carrying value of relevant corporate assets as compared with the present value of estimated future cashflows.

Excluding the non-cash item of impairment loss of HK\$25.8 million, the Group's earnings per share increased to HK7.33 cents.

Total operating expenses went up largely in line with the increase in turnover and as a result of a general increase in staff costs on the back of a strengthening economy. General and administrative expenses were HK\$56.4 million, up 13 percent (2005: HK\$49.8 million); of which depreciation and amortisation expenses were HK\$72.4 million, up 32 percent (2005: HK\$55 million), attributable to the roll-out of several new projects. Distribution costs came down to HK\$21.5 million (2005: HK\$25.9 million) after continued efforts in expanding clientele in previous years.

Finance costs for the period increased to HK\$4.5 million (2005: HK\$2.6 million), attributable to higher utilisation of bank borrowings for working capital and increase in investments.

Review of Operations

The Group continued to benefit from China's economic growth, where sales maintained its momentum. The success of China's aerospace projects, the forthcoming award of 3G telecom licences, as well as upcoming international events to be held in China such as the 2008 Olympics and the 2010 World Expo were also drivers to the growth in investment in the telecoms and related sectors. For the six-month period, China sales accounted for HK\$439 million of the Group's turnover (2005: HK\$408 million).

In Europe, where healthcare and fire services continued to be core sectors for the Group's messaging solutions, business remained stable. A suite of new products and integrated wireless solutions was being developed to leverage the Group's existing customer base in key vertical sectors such as healthcare, hospitality, and retail. Within the UK, the reduced spending by the NHS (National Health Service) due to budget rebalancing was compensated by strong demand in the emergency services sector, where Kantone remained well-positioned to secure new long-term contracts, especially in the arena of Fire Services and Marine Coast Guard Security. Turnover attributable to the operations in Europe was HK\$196 million (2005: HK\$185 million).

In the US, Kantone's primary focus was on projects arising from the Government's spectrum migration programme for public sector networks.

e-Gaming and Online Entertainment

Building on its expertise in integrated IT solutions and telephone data management, Kantone continued to expand its portfolio of investments in betting software solutions and various gaming and entertainment websites. Its paperless lottery project in China progressed as planned, with new regions signed up and continued enhancement of integrated gaming technology solutions. Kantone commanded a leadership position in the e-lottery market in China, complete with its own IP (intellectual property) over a robust e-lottery platform with secure micropayment systems connected to banks. Such comprehensive platform facilitated one-stop-shop automated betting transactions for multiple lottery games. Betting turnover via Kantone's e-platform steadily increased, and the use of SMS on mobile phones and web-sites for paperless betting was gaining popularity among young people and the more well-off white-collar workers.

e-Lottery in China is still at its developing stage, but if it were to follow the trend of the high adoption rate of other technologies such as mobile phones and Internet usage, e-lottery will have a significant impact on China's overall lottery market, and in turn, will impact positively on the Group's results in the future.

Directors are fully aware that globally lottery and gaming is one of the fastest growth sectors, and it commands the level of risk commensurate with the higher return. The Group's endeavours in this area of business are expected to bear fruit after the initial period of investment.

OUTLOOK

Kantone will strive to strengthen its position in the niche markets of providing wireless integrated solutions tailored to customers' specialised requirements, as well as enhancing its value-added services to help customers achieve significant savings. In this regard, 2007 will be a year of continued investment in order to bring long-term growth to the Group.

As a global player, we are constantly on guard of the different developments in the various markets where we operate. In the more mature markets such as Europe, sales of telecom equipment has shown signs of slowing growth, whereas Internet, IT services and software solutions remain the key drivers to stable growth. In emerging markets such as China, customers are getting more sophisticated and there is growing need to introduce more high value-added services and enriched innovative solutions to sustain margins and maintain growth. Across the board, it is encouraging to see continuing robust growth in the Internet and related services sector, where new technologies continue to open up new business opportunities. In particular, China increased its spending by 50% last year on Internet services such as online games, e-commerce, and instant messaging services, making it the world's second largest Internet market behind the United States.

In line with market trends, the Group's business strategy going forward will be driven by a focus on high margin and high growth sectors to pursue margin improvement. Such strategy naturally entails continued innovations and bigger investments, especially in China which continues to present enormous opportunities, in order to expand our portfolio of compelling solutions and offerings.

Against this challenging and more complex environment, the directors will continue to exercise prudence in managing investment risks while capturing market opportunities that produce what is in the best interest for the Group and its shareholders in the long term.

LIQUIDITY AND FINANCIAL RESOURCES

Financial Position and Gearing

As at 31 December 2006, the Group had HK\$199 million (30 June 2006: HK\$252 million) liquid assets made up of deposits, bank balances and cash. Current assets were approximately HK\$593 million (30 June 2006: HK\$625 million) and current liabilities amounted to approximately HK\$239 million (30 June 2006: HK\$147 million). With net current assets of HK\$354 million, the Group maintained a comfortable level of liquidity. The gearing ratio of the Group at the period-end, defined as the Group's total borrowings to equity attributable to equity holders of the Company, was 0.10 (30 June 2006: 0.05) mainly attributable to the issue of convertible bonds during the Period and increase in bank borrowings as at 31 December 2006.

Total borrowings comprised bank borrowings of HK\$100.4 million (30 June 2006: HK\$55.1 million); other borrowings, which represented block discounting loans, of HK\$3.1 million (30 June 2006: HK\$5 million); and convertible bonds of HK\$77.8 million (30 June 2006: HK\$18.2 million). Finance costs for the Period amounted to HK\$4.5 million (Previous Period: HK\$2.6 million).

Included in the bank borrowings of HK\$100.4 million were bank loans and overdrafts of HK\$5 million (30 June 2006: HK\$1.8 million) being secured by the Group's land and buildings with a net book value of HK\$12.7 million (30 June 2006: HK\$11.9 million). These borrowings comprised debts of HK\$4.2 million repayable within one year, HK\$0.8 million repayable in the second year and the remaining balance of less than HK\$0.1 million repayable in the third year. The unsecured bank borrowings of HK\$95.4 million were repayable on demand.

The other borrowings of HK\$3.1 million were unsecured, with HK\$2.4 million repayable within one year, HK\$0.5 million repayable in the second year and the remaining balance of HK\$0.2 million repayable in the third year.

As at 31 December 2006, the Company had outstanding convertible bonds with face value of USD8.1 million which will mature on 1 April 2008.

Treasury Policy

The Group is committed to financial prudence and continued to maintain a strong financial position with low gearing and a net cash position. The Group financed its operation and business development with a combination of internally generated resources, capital markets instruments, and banking facilities provided by its principal bankers.

Except for the USD convertible bonds, all other borrowings were used by the subsidiaries of the Group, bearing interest at floating rates. As all the borrowings were denominated either in local currencies or in USD, the currency risk exposure associated with the Group's borrowings was insignificant.

The Group does not engage in interest rate or foreign exchange speculative activities. It is the Group's policy to manage foreign exchange risk through matching foreign exchange income with expense, and where exposure to foreign exchange is anticipated, appropriate hedging instruments will be used.

Capital Commitments

As at 31 December 2006, the Group's capital commitments authorised but not contracted for was HK\$143 million (30 June 2006: HK\$179 million). The Group had set aside sufficient internally generated funds for the acquisition of property, plant and equipment, and development of systems and networks.

HUMAN RESOURCES

As at 31 December 2006, the Group employed over 800 staff around the globe. Competitive remuneration packages that take into account business performance, market practices and competitive market conditions are offered to employees in compensation for their contribution. In addition, share options and discretionary bonuses are also granted based on the performance of the Group and that of the individual.

DIRECTORS' INTERESTS AND SHORT POSITIONS IN SECURITIES

As at 31 December 2006, the interests and short positions of the directors and chief executive of the Company in the shares, underlying shares or debentures of the Company or any of its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance (the "SFO")) which were recorded in the register required to be kept by the Company pursuant to section 352 of the SFO, or as otherwise notified to the Company and The Stock Exchange of Hong Kong Limited (the "Exchange") pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers were as follows:

Long positions:

Name of director	Capacity	Number of shares	Approximate percentage of the issued share capital	Number of warrants
<i>Securities of the Company</i>				
Mr. Paul Kan Man Lok	Corporate interest	<i>Note 1</i>	66.99%	–
<i>Securities of Champion Technology Holdings Limited ("Champion", the holding company of the Company)</i>				
Mr. Paul Kan Man Lok	Corporate interest	<i>Note 2</i>	28.21%	<i>Note 2</i>
<i>Securities of DIGITALHONGKONG.COM (a fellow subsidiary of the Company)</i>				
Mr. Paul Kan Man Lok	Corporate interest	<i>Note 3</i>	79.98%	–

Notes:

- 1,522,770,388 shares were held by Champion and 428,156,578 shares were held by Lawnside International Limited ("Lawnside"). Lawnside is beneficially wholly owned by Mr. Paul Kan Man Lok. As at 31 December 2006, Lawnside had interests in approximately 28.21% of the entire issued share capital of Champion. Mr. Paul Kan Man Lok was deemed to have corporate interest in the shares which were owned by Champion and Lawnside.
- 392,579,439 shares and 54,276,861 units of warrants were held by Lawnside. The warrants were issued by Champion pursuant to a bonus issue effected in February 2006, all of which expired on 26 February 2007.
- 117,300,000 shares were held by Champion and 2,669,171 shares were held by Lawnside.

Save as disclosed above, as at 31 December 2006, none of the directors or chief executive of the Company had any interest or short position in the shares, underlying shares or debentures of the Company or any of its associated corporations (within the meaning of Part XV of the SFO) which were recorded in the register required to be kept by the Company pursuant to section 352 of the SFO or as otherwise notified to the Company and the Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers.

SHARE OPTIONS AND DIRECTORS' RIGHTS TO ACQUIRE SHARES OR DEBENTURES

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

During the period under review, no option was granted, exercised, cancelled, lapsed or outstanding under the Company's share option scheme.

SUBSTANTIAL SHAREHOLDERS

As at 31 December 2006, the following persons (other than a director or chief executive of the Company disclosed under "Directors' Interests and Short Positions in Securities" section) had interests and short positions in the shares and underlying shares of the Company as recorded in the register required to be kept by the Company under section 336 of the SFO:

Name of shareholder	Long/short position	Capacity	Number of shares	Approximate percentage of the issued share capital
Champion	Long	Beneficial owner	1,522,770,388*	52.29%
Lawnside	Long	Beneficial owner	428,156,578*	14.70%

* See <Note 1> in the "Directors' Interests and Short Positions in Securities" section.

Save as disclosed herein and disclosed under "Directors' Interests and Short Positions in Securities" section, the Company had not been notified of any person, other than a director or chief executive of the Company, having interests or short positions in the shares or underlying shares of the Company, which was recorded in the register required to be kept under section 336 of the SFO as at 31 December 2006.

PURCHASE, SALE OR REDEMPTION OF LISTED SECURITIES

Neither the Company nor any of its subsidiaries purchased, sold or redeemed any of its listed securities during the period under review.

CODE ON CORPORATE GOVERNANCE PRACTICES

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 on Corporate Governance Practices, as set out in Appendix 14 of the Rules Governing the Listing of Securities on the Exchange (the “Listing Rules”) at any time during the six months ended 31 December 2006.

MODEL CODE FOR SECURITIES TRANSACTIONS BY DIRECTORS

The Company has adopted a code of conduct regarding directors’ securities transactions on terms as set out in Appendix 10 of the Listing Rules. The Company has made specific enquiry of all directors, result of which indicates that its directors have complied with such code of conduct throughout the period under review.

AUDIT COMMITTEE

The audit committee of the Company has reviewed with the management of the Group the accounting principles and practices adopted by the Group, its internal controls and financial reporting matters and this interim report.

By Order of the Board
Paul KAN Man Lok
Chairman

Hong Kong, 26 March 2007

