arcontech
The Innovators

2003
Annual Report

Characteristics of The Growth Enterprise Market (the "GEM") of The Stock Exchange of Hong Kong Limited (the "Stock Exchange"):

GEM has been established as a market designed to accommodate companies to which a high investment risk may be attached. In particular, companies may list on GEM with neither a track record of profitability nor any obligation to forecast further profitability. Furthermore, there may be risks arising out of the emerging nature of companies listed on GEM and the business sectors or countries in which the companies operate. Prospective investors should be aware of the potential risks of investing in such companies and should make the decision to invest only after due and careful consideration. The greater risk profile and other characteristics of GEM mean that it is a market more suited to professional and other sophisticated investors.

Given the emerging nature of companies listed on GEM, there is a risk that securities traded on GEM may be more susceptible to high market volatility than securities traded on the Main Board of the Stock Exchange and no assurance is given that there will be a liquid market in the securities traded on GEM.

The principal means of information dissemination on GEM is publication on the Internet website operated by the Stock Exchange. Listed companies are not generally required to issue paid announcements in gazetted newspapers. Accordingly, prospective investors should note that they need to have access to the GEM website in order to obtain up-to-date information on GEM-listed issuers.

arcontech
The Innovators

Contents

Corporate Information

Executive Directors
TSOI Siu Ching, Leo
YIP Ho Bun, Edwin
HO Ping

Independent Non-executive Directors
LO Chi Ko
HO Yung San

Company Secretary
YIP Ho Bun, Edwin, *FHKSA*

Qualified Accountant
YIP Ho Bun, Edwin, *FHKSA*

Compliance Officer
YIP Ho Bun, Edwin, *FHKSA*

Principal Bankers
The Hongkong and Shanghai Banking Corporation Limited
Hang Seng Bank Limited

Auditors
Graham H. Y. Chan & Co.
Certified Public Accountants

Audit Committee
LO Chi Ko
HO Yung San
YIP Ho Bun, Edwin

Authorised Representatives
TSOI Siu Ching, Leo
YIP Ho Bun, Edwin

Share Registrar and Transfer Office
Computershare Hong Kong Investor Services Limited
Shops 1712-1716, 17th Floor
Hopewell Centre
183 Queen's Road East
Hong Kong

Registered Office
Ugland House
P.O. Box 309
George Town
Grand Cayman
Cayman Islands
British West Indies

Head Office and Principal Place of Business
Unit 5, 11/F.,
Goodluck Industrial Centre
808 Lai Chi Kok Road
Kowloon
Hong Kong

Financial Highlights

		Year ended 31 Mach	
	2003	2002	Change
	HK$'000	HK$'000	%
Revenue			
Turnover	**540,367**	472,395	14
Profitability			
Gross profit	**114,545**	150,596	(24)
Operating (loss)/profit	**(431,939)**	84,946	(608)
(Loss)/profit before taxation	**(439,181)**	81,032	(642)
(Loss)/profit attributable to shareholders	**(421,107)**	67,612	(723)
Net woth			
Shareholders' fund	**18,596**	337,476	(94)
Per share			
(Loss)/earnings per share	**(51.84) cents**	9.39 cents	(652)
Net assets per share	**2.27 cents**	46.87 cents	(95)
Dividend per share	**1.05 cents**	3.00 cents	(65)
Turnover period			
Inventory turnover period	**78 days**	15 days	N/A
Trade receivable turnover period	**73 days**	252 days	N/A

Chairman's Statement

On behalf of the Board of Directors (the "Board"), I am pleased to present to shareholders the annual report of Arcontech Corporation (the "Company") and its subsidiaries (collectively the "Group"), for the year ended 31 March 2003.

Financial Results

For the year ended 31 March 2003, the Group continued to operate under difficult market conditions, in particular, the unexpected US-Iraq War and the attack of SARS in the first half of 2003 further increased such difficulties. The Group also faced a weak US consumer market for audio/visual products. This market trend has forced customers from the US to adopt a new procurement practice, under which the lead time for orders placed by those customers were generally much shorter than in previous periods. As a result, the Group was forced to increase its inventory level so as to meet such short lead time for the orders of the customers. The Group therefore, in line with market demand, adopted an aggressive policy towards turning over its inventory level.

In order to increase inventory turnover, and in response to the pressure on prices from customers, the Group generally lowered prices on its products and the turnover of the Group for the year was increased to HK$540.4 million compared to HK$472.4 million for the previous year.

The inventory turnover policy adopted by the Group as well as the relatively lower profit margin for audio/visual product solutions sold during the year led to lower gross profit margin of 21% compared to 32% for the previous year.

A large number of products sold during the year was returned to the Group by customers which were in financial difficulty and some of which were facing debt recovery proceedings commenced by one of the bank creditors of the Group. Some of the inventory sold during the year were embedded by these customers in products such as CD-ROM which were moving towards the mature stage of its product life cycle and were particularly exposed to bad market conditions and competition from replacement products such as DVD. Inventory in the amount of HK$104.7 million was therefore written off, written down or provided for as appropriate in the accounts.

The returned inventory could only be effectively re-used or sold if they are reprogrammed with different functions and features to be used with other products. However, the Group was unable to invest any resources into such required research and development.

One of the bank creditors of the Group commenced winding up proceedings against the Company and its principal subsidiary, Arcon Technology Limited ("ATL") on 16 July 2003. The winding up action coupled with the financial difficulty faced by the Group's customers due to the slow US market conditions caused many of the Group's customers to stop payment of debts to the Group. The effects of the winding up proceedings spiraled and a broad range of debtors refused to pay the Group and an amount of HK$349.2 million were provided for in the accounts for the year ended 31 March 2003 as bad and doubtful debts.

General and administrative expenses increased to HK$83.6 million after making a depreciation charge of HK$29.8 million.

Dividends

The Board does not recommend the payment of a final dividend for the year ended 31 March 2003 (2002: HK1 cent).

Total dividends for the year ended 31 March 2003 amounted to HK1.05 cents per share, consist of the interim dividend of HK0.35 cent per share for the three months ended 30 June 2002 paid to shareholders on 23 August 2002, the interim dividend of HK0.50 cent per share for the three months ended 30 September 2002 paid to shareholders on 27 November 2002 and the interim dividend of HK0.20 cent per share for the three months ended 31 December 2002 paid to shareholders on 12 March 2003. Before the declaration of such interim dividends, the directors had reviewed the operating results of the Group for the respective quarters and were of the view that it appeared to the Board to be justified by the profits of the Group for the declarations of these interim dividends.

Chairman's Statement

CLOSURE OF REGISTER OF MEMBERS

The Register of Members of the Company will be closed from Wednesday, 10 December 2003 to Saturday, 13 December 2003, both days inclusive, during which period no share transfers will be registered.

Business Review

The Group faced extreme challenges during the period under review due especially to weak global economies, the threat of war and terrorism, the US-led invasion of Iraq in March, the attack of SARS and a particularly poor consumer spending environment in the US markets. Business for the fourth quarter in the US in particular was weakened heavily in the lead up to the Iraq war and coincided with falling consumer confidence.

The operating landscape changed as the demand for high-end products continued to be weak. Competition amongst industry players have intensified and the resulting pressure on retail prices has affected all levels of industry. The aggressive inventory turnover policy adopted by the Group was a direct result of such market conditions and was driven by changes to operating models adopted by all levels of market participants to combat falling retail prices.

During the year, some of the solutions of the Group was embedded in products which were moving towards the mature stage of the product life cycle, and those customers were particularly exposed to market volatility. The solutions developed for the replacement products were not yet reflected in the financial performance of the Group for the year. The winding up petition filed against the Company and ATL by one of its bank creditors also severely affected the operations of the Group.

Combination of the above factors negatively impacted on the financial performance of the Group. During the year, the Group was focusing on a number of internal policies and restructure to combat the exposure to credit risk, given the changes in operating environment described above, including taking insurance policy on new sales, and measures were imposed on managing credit assessment. The Group was also in the process of implementing its new operational plan, focusing on streamlining its operations.

Prior to the difficulties faced by the Group with regards to the winding up proceedings against the Company and the failure of its customers to pay its debts, the Group was successful in adopting a revised operation policy to combat the difficult operating environment. The Group has moved towards focusing on developing solutions for fast moving consumer items such as audio visual products, Wi-Fi devices and simple digital devices which command a higher volume. The Group also focused on developing solutions for high end products which have a shorter time to market in order for the Group to benefit from the higher margin available during the early cycles of the product, and allow the Group to move its development focus to the next generation of products relatively quickly.

On the operation side, the management has during the year, extensively and substantially reshuffled executives' responsibilities in a major review of the Group organization. The management also realigned the organizational structure of the Group and adopted certain operational plans, which streamlined the operation and increased the operational efficiency in various areas of operating the Group's businesses.

On the senior management side, Mr. Edwin Yip was appointed as the Group's executive director and chief financial officer in August 2002, Mr. Ho Ping as an executive director and Mr. Zhang Xiaoming as an independent non-executive director in October 2002. Mr. Raymond Cheung, Mr. Lo Chi Ko and Mr. Ho Yung San were appointed as independent non-executive directors in May 2003 and August 2003 respectively. Mr. Tong Ka Ming, Patrick and Mr. Mak Kam Wah resigned as executive directors in October 2002 and August 2003 respectively. Mr. Wang Wei Hung, Mr. Chu Ho Hwa, Mr. Raymond Cheung and Mr. Zhang Xiaoming resigned as independent non-executive directors in April 2003, May 2003, July 2003 and August 2003 respectively. The Board would like to take this opportunity to welcome the new directors and to express its appreciation for the outgoing directors' contributions towards the Group during their terms of service.

Chairman's Statement

It is with deep regret and grief to inform you of the loss of our dear Chairman of the Technology Advisory Board and Chief Consultant of the Group, NEC Distinguished Professor Tien Chang Lin, who passed away in October 2002. Professor Tien's departure is a great loss to the Group. His leadership in the Group's Technology Advisory Board had guided us to become a leading solution provider in the 3C products industry and he will live in the memory of all the staff of the Group who have had the honor of working with him.

Financial Resources and Liquidity

As at 31 March 2003, the Group had total assets of approximately HK$351 million, which were financed by current liabilities of approximately HK$310 million, minority interests of approximately HK$22 million and shareholders' equity of approximately HK$19 million.

Current assets amounted to approximately HK$266 million, of which approximately HK$4 million were cash and bank deposits. The Group had a working capital ratio of approximately 0.86.

The Group raised approximately HK$119 million on 29 April 2002 by way of issuing 100,000,000 new shares through a top-up placement for the purpose of funding requirements under a supply agreement and for general working capital purposes.

Charges on Group Assets and Contingent Liabilities

The Group's banking facilities were secured by corporate guarantees given by the Company and there were approximately HK$186 million utilised banking facilities, mainly trade financing, as at 31 March 2003. Bank borrowing to equity ratio was 10.

Subsequent to the balance sheet date, one of the Group's bank creditors, the Hongkong and Shanghai Banking Corporation Limited, has filed a winding up petition against each of the Company and its principal subsidiary, Arcon Technology Limited. Some other major bank creditors have also demanded for immediate payments of the amounts due to them. In the absence of additional funding, the Group cannot meet the demands for immediate payments of its debts. The Company has engaged its legal adviser to advise on the petition and prepare its defence. It is expected that the Group will settle the matter in a satisfactory way and survive the crisis.

The Group is currently engaged in negotiations with its bank creditors, on a without prejudice basis, to achieve a debt restructuring agreement, but formal agreement has not been reached up to the date of this report.

In the absence of a formal standstill agreement to restructure the Group's bank loans and other debts, the directors consider that it is more appropriate to classify all borrowings of the Group as current liabilities in the accounts.

The directors believe that the Group's aggressive credit policy contributed significantly to its fast expansion in the market in the past years. Unfortunately, the unexpected US-Iraq War and the attack of SARS in the first half of 2003 had ruined this aggressive business mode. Demand dropped sharply and most of its customers are in financial difficulties. The Group's liquidity is thus affected and its funds are held up by inventory and doubtful debts. However, the Group's core business remains profitable.

Chairman's Statement

Foreign Exchange Exposure

The revenues of the Group are denominated mostly in Hong Kong Dollars and U.S. Dollars. The Group has minimal exposure to foreign exchange fluctuations and seldom needs to make use of financial instruments for hedging purposes.

Employees

As at 31 March 2003, the Group had 153 full-time employees who were engaged in the following operations:

Engineering and R&D	117
Sales and marketing (including field application engineers)	11
Finance, accounting, operation and administration	25
Total headcount	153

The Group has successfully reduced the total headcounts from 216 to 153 as part of an internal reorganization and increased operational efficiency. The Group believes that the quality of its employees is the most important factor in sustaining the Group's growth and improving its profitability. Employees are remunerated according to their performance and work experience. In addition to basic salaries, staff benefits include medical scheme, share options and performance bonus.

Future Prospects

Business Outlook

The market sentiment has picked up significantly since the year under review and the Group's products are in demand by industry players. The Group has the know how to develop solutions which can replace expensive features often executed through hardware with a much cheaper alternative in software solutions.

The Group will look to adopting a streamlined operating structure and focus on its design strength in developing new products in order to command a higher margin instead of following industry standards during the year under review in driving for volume and turnover in order to move its inventory which has exposed the Group to credit risks and have affected the Group's financial performance during the year significantly.

Chairman's Statement

ADVANCES TO ENTITIES

In accordance with rules 17.15 to 17.17 of the GEM Listing Rules, the Company makes the following disclosures in relation to the details of advances to entities:

Name of entity	**Outstanding balance as at 31 March 2003 (before provision)** HK$'000
Shanghai Chuen Tian Electronic Co.	60,770
Golden Source Electronics Limited	33,877
He Mu Economy Development Co., Ltd.	70,810
HongPu International Development (Shanghai) Co., Ltd.	17,018
Huashen Electronic Ltd.	5,158
Li Guang Electronics Limited	17,238
Mighty Treasure Trading Limited	68,623
Silver City China Ltd.	11,094
Shenzhen He Si Rui Electrical Ltd.	7,181
Wealth-In Industrial Limited	6,252
Windsor Technology Limited	90,394
Funet Radio & Communications Corporation	31,200
Semi House Pte Ltd.	15,795

The above entities are independent third party customers of the Group and the above amounts represented trade receivable balances for sales made to the respective customers as at 31 March 2003. The amounts are unsecured, interest-free and repayable in accordance with the credit terms as agreed with respective customers. Except for the amount due from Semi House Pte Ltd. which had been fully settled subsequent to 31 March 2003, adequate provision for bad and doubtful debts have been made on all the above amounts in the accounts for the year ended 31 March 2003.

Acknowledgement

Finally, I would like to thank my fellow directors and staff for the enormous effort and commitment they made in overcoming many challenges to achieve the year's result, and thank our shareholders for their trust and support.

Tsoi Siu Ching Leo
Chairman

Hong Kong, 20 November 2003

Business Objectives Review

An analysis comparing of business objectives as stated in the Company's prospectus dated 8 August 2000 with the Group's actual business progress up to 31 March 2003 is set out below:

Business Objectives:	***Actual Business Progress:***
Revenue	
• achieve around 50%:50% balance of turnover from customer-driven embedded software solutions and self-initiated turnkey device solutions	• the sales from self-initiated turnkey device solutions have increased to more than 30% of the total turnover
Product launches, sales and marketing	
• launch embedded software solutions with pressure sensor and pattern recognition features	• the Group has launched turnkey device solutions for TFT-LCD controllers and home appliances with voice recognition during the year. It is expected to make contribution to the Group's sales in the coming year.
• launch new generation of GPS devices integrating auto-navigation system, fleet management system, geographical information system, electronic road pricing system, diagnostic rescue system and m-commerce features for both corporate and general public users	• the Group, through its subsidiary, Satellite Devices Corporation, has successfully launched the auto-navigation systems with full Hong Kong maps, RoadPilot in December 2002. Further versions with maps of major China cities are under development and will be launched in the coming year.
• launch new generation of digital healthcare products integrating medical testing and internet medical data uploading and downloading features	• the Group is finalizing its digital healthcare products with overseas requirements for overseas medical authorities, and are expected to be put into testing in the coming year
• launch Bluetooth devices for various 3C applications with advanced networking and data-downloading features	• the Group is studying the market potential for products with integration of Bluetooth technologies, voice recognition and environment control features for applications in intelligent home appliances and other consumer electronics
• launch walking PCs with speech-to-text features	• the Group is finalising its development plans for products utilising micro-pressure sensors and pattern recognition technologies, and has started the research on solutions for walking PCs speech-to-text features
Research and development ("R&D")	
• initiate R&D on new and innovative 3C products based on latest technology trends and standards, such as in the areas of wireless access, convergence and smart devices	• the R & D team will dedicate towards developing new and cost-effective solutions for producing a wide range of digital products including AV equipment, mobile handsets and DECT, etc.

Business Objectives Review

Human resources, operations and administration

- recruit additional staff as required for business growth
- the Group has successfully reduced the total headcount to 153 and achieved better performance and cost-savings and there were more than 110 engineers within the Group

Strategic acquisitions and alliances

- explore opportunities to acquire or form alliance with companies providing synergies and technological supports
- the Group is actively pursuing opportunities to establish or acquire technological alliance/ventures which are able to compliment the future business development of the Group. However, up to the end of the year, nothing concrete has been concluded

Use of Proceeds

The Group raised net proceeds of approximately HK$156 million upon listing of the Company's shares on GEM of the Stock Exchange. By 31 March 2003, the Group had used up all the proceeds from the listing to achieve the business objectives as stated above and in the manner as set out in the Company's prospectus. The proceeds have been applied as follows:

	According to the use of proceeds as stated in the prospectus dated 8 August 2000 HK$'million	Amount utilized up to 31 March 2003 HK$'million
Setting up SMS and City Band operating centre to facilitate sales of GPS and m-commerce applications	55	55
Setting up a shielded laboratory dedicated to the R&D of Bluetooth devices and purchase of related equipment	50	50
Upgrading the existing R&D facilities and equipment	15	15
On-going product development of GPS and m-commerce applications	10	10
On-going product development of digital healthcare devices	10	10
Enhancing sales and marketing efforts to further promote the Group's business	5	5
General working capital purposes	11	11
Total	156	156

Profiles of Directors and Senior Management

Executive Directors

Mr. TSOI Siu Ching, Leo, aged 43, is the founder, Chairman, Chief Technology Officer and Chief Executive Officer of the Group. He is primarily responsible for the overall management, supervision of the operating unit heads, the formulation of corporate strategy and oversees the direction of the Group. Mr. Tsoi graduated from the Hong Kong Polytechnic University in 1982 and is a member of the Institute of Electrical and Electronics Engineers. Mr. Tsoi has over 20 years of experience in the semi-conductor industry. He joined the Group in 1992.

Mr. YIP Ho Bun, Edwin, aged 57, is an executive director and the Chief Financial Officer of the Group. He is primarily responsible for the overall financial planning and corporate planning of the Group. He is a fellow member of the Association of Chartered Certified Accountants, a fellow member of the Hong Kong Society of Accountants, and an associate member of the Taxation Institute of Hong Kong. Mr. Yip has over 30 years of experience working in senior finance and accounting position in various companies. He joined the Group in 2002.

Mr. HO Ping, aged 46, is an executive director of the Group. He is responsible for the overall management, corporate development and investment activities of the Group. He was educated at Qinghua University, the PRC and has over 18 years of experience in the technology sector. He joined the Group in 2002.

Independent Non-executive Directors

Mr. LO Chi Ko, aged 33, is an independent non-executive director and the Chairman of the Audit Committee of the Group. He holds a bachelor degree from the Hong Kong Baptist University and a master degree in business administration from the University of Surrey, United Kingdom. He has over 9 years of experience in corporate finance and accounting sector, particularly in auditing and taxation areas. Mr. Lo is a member of the Hong Kong Society of Accountants and the Australian Society of Certified Public Accountants. He joined the Group in 2003.

Mr. HO Yung San, aged 41, is an independent non-executive director of the Group. He holds a higher diploma in production and industrial engineering from the Hong Kong Polytechnic University. He has more than 16 years of experience in project management and corporate administration in multinational companies in Hong Kong and in the PRC. He joined the Group in 2003.

Senior Management

Mr. TANG Ho Cheung, Gary, aged 29, is the Vice President of Engineering of the Group. He is responsible for development of software solutions for the Group. He graduated from the Hong Kong Polytechnic University in 1997 and has over 5 years of experience in the information technology and electronics industry. He joined the Group in 1997.

Ms. CHING Fung Ki, Wendy, aged 39, is the Vice President of Administration. She is responsible for the overall administration and resource management of the Group. She has over 17 years of experience in business administration and corporate management and is the wife of Mr. Tsoi Siu Ching, Leo. She joined the Group in 1996.

Mr. SAM Luen Lai, Paul, aged 36, is the Accounting Manager of the Group. He is responsible for the overall treasury and direction of accounting of the Group. He has over 8 years of experience in the field of accounting and financial management. He joined the Group in 2003.

Report of the Directors

The directors have pleasure in submitting their annual report together with the audited accounts for the year ended 31 March 2003.

Principal activities and geographical analysis of operations

The principal activity of the Company is investment holding. The principal activities of the Group are design, development of software and engineering solutions, including the sales of semiconductors and other electronic components, and the location-based technology devices and applications ("GPS"). All of the Group's turnover was derived from Hong Kong.

Results and appropriations

The results of the Group for the year are set out in the consolidated profit and loss account on page 21.

The details of dividends declared and paid during the year are set out in note 8 to the accounts. The Board does not recommend the payment of final dividend for the year ended 31 March 2003.

Reserves

Details of the movements in the reserves of the Group and the Company during the year are set out in note 22 to the accounts.

Fixed assets

Details of the movements in fixed assets of the Group during the year are set out in note 12 to the accounts.

Donations

The Group made a charitable donation of HK$22,700 during the year.

Share capital and share options

Details of the movements in share capital and share options of the Company during the year, together with reasons therefore, and details of the Company's share option scheme are set out in note 20 and note 21 to the accounts.

Subsidiaries

Particulars of the principal subsidiaries of the Company as at 31 March 2003 are set out in note 13 to the accounts.

Distributable reserves

Under section 34 of the Companies Law (2003 Revision) of the Cayman Islands, the share premium is available for distribution to shareholders subject to the provisions of the Articles of Association of the Company and no distribution may be paid to shareholders out of the share premium unless, immediately following the date on which the distribution of dividend is proposed to be paid, the Company shall be able to pay its debts as they fall due in the ordinary course of business. As at 31 March 2003, the Company had no reserve available for distribution.

Segmental information

An analysis of the Group's turnover and contribution to profit before taxation by principal activity for the year ended 31 March 2003 are set out in note 3 to the accounts.

No geographical segmental analysis is presented as the Group's operations are principally located in Hong Kong.

Report of the Directors

Bank loans and other borrowings

Particulars of bank loans and other borrowings of the Group as at 31 March 2003 are set out in note 23 to the accounts.

Financial summary

The summary of the published results and of the assets and liabilities of the Group for the last five financial years is set out on page 60.

Purchase, sale or redemption of shares

The Company has not redeemed any of its shares during the year. Neither the Company nor any of its subsidiaries has purchased or sold any of the Company's shares during the year.

Directors

The directors during the year were:

Mr. TSOI Siu Ching, Leo
Mr. YIP Ho Bun, Edwin (appointed on 23 August 2002)
Mr. HO Ping (appointed on 11 October 2002)
Mr. TONG Ka Ming, Patrick (resigned on 11 October 2002)
Mr. MAK Kam Wah (resigned on 13 August 2003)
Mr. WANG Wei Hung* (resigned on 30 April 2003)
Mr. CHU Ho Hwa, Howard* (resigned on 15 May 2003)
Mr. ZHANG, Xiaoming* (appointed on 11 October 2002 and resigned on 13 August 2003)
Mr. CHEUNG Kwok Ming, Raymond*(appointed on 15 May 2003 and resigned on 22 July 2003)
Mr. LO Chi Ko* (appointed on 13 August 2003)
Mr. HO Yung San* (appointed on 13 August 2003)

* *Independent non-executive directors*

Mr. Yip Ho Bun, Edwin will retire by rotation, at the forthcoming annual general meeting in accordance with Article 116 of the Company's Articles of Association and, being eligible, offers himself for re-election.

Biographical details of directors and senior management

Brief biographical details of directors and senior management are set out on page 11.

Report of the Directors

Directors' service contracts

Mr Tsoi Siu Ching, Leo, an Executive Director, had entered into a service contract with the Company for a term of two years from 19 July 2000. The two years terms expired on 19 July 2002 and, thereafter, the contracts may be terminated by either party thereto giving to the other not less than six calendar months prior notice in writing, or otherwise in accordance with its terms.

Mr Yip Ho Bun, Edwin, an Executive Director, had entered into a service contract with the Company for a term of two years from 23 August 2002. The contract may be terminated by either party thereto giving to the other not less than six calendar months prior notice in writing, or otherwise in accordance with its terms.

Save as disclosed herein, none of the directors who has proposed for re-election at the forthcoming annual general meeting has a service contract with the Company which is not determinable within one year without payment of compensation, other than statutory compensation.

Directors' interests in contracts

No contracts of significance in relation to the Group's business to which the Company, its fellow subsidiaries, its subsidiaries or its holding company was a party and in which a director of the Company had a material interest, whether directly or indirectly, subsisted at the end of the year or at any time during the year.

Directors' benefits from rights to acquire shares or debentures

The Company has adopted a Pre-IPO Share Option Plan (the "Plan") and a Share Option Scheme (the "Scheme") on 19 July 2000. Under the terms of the Plan and the Scheme, the Board may, at their discretion, invite any employees or executive directors of the Company and/or any of its subsidiaries to subscribe for ordinary shares of HK$0.10 each in the Company. The maximum number of shares in respect of which options may be granted under the Plan and the Scheme may not exceed 30% of the issued share capital of the Company.

For the Scheme, the subscription price will be determined by the Board, save for the following: (1) in respect of any option granted prior to the listing of the shares of the Company on GEM, such price will be the issue price of the listing; and (2) for all other option granted upon listing of the shares of the Company on GEM, such price will not be less than the highest of (i) the nominal value of the shares, (ii) the closing price of the shares on the date of grant of the options, and (iii) the average of the closing prices of the shares on the five business days immediately preceding the date of grant of the options. With effect from 1 October 2001 with the amendments to the Rules Governing the Listing of Securities on the GEM of the Stock Exchange (the "GEM Listing Rules') in share option scheme, the total number of shares issued and to be issued upon exercise of the options granted to each grantee (including both exercised and outstanding options) in any 12-month period up to the date of grant shall not exceed 1% of the shares in issue at the date of grant.

The Scheme is valid and effective for a period of 10 years from the 19 July 2000. Any options granted under the Scheme may be exercised at any time during a period to be notified by the Board to each grantee, such period of time shall not be less than 3 years from the date on which the option is granted in accordance with the terms of the Scheme and not more than the date falling on the expiry of 10 years from the date of grant of the option or the date falling on the expiry of the Scheme, whichever date is later. Upon acceptance of the option, the grantee shall pay HK$1.00 to the Company by way of consideration for the grant.

For the Plan, the principal terms are the same as the terms of the Scheme except that: (a) the subscription price for the shares granted under the Plan is the issue price of the listing; (b) the total number of shares subject to the Plan is 28,800,000; (c) the grantee can be Non-executive Directors and employees of the Company and its subsidiaries who are not in full time employment of the Group and consultants and advisers to the Group; and (d) the Plan was terminated on 4 August 2000, being the day immediate prior to the day when bulk printing of the Company's prospectus took place.

Report of the Directors

On 20 July 2000, options to subscribe for an aggregate of 64,800,000 shares at an exercise price HK$1.18 have conditionally been granted by the Company under the Plan and the Scheme, of which 57,600,000 share options were outstanding as at 31 March 2003. The options granted under the Scheme are exercisable at any time within 3 years from 16 August 2000 while the options granted under the Plan are exercisable at any time within 3 years after the expiry of 6 months from 16 August 2000. Each of these shall lapse in accordance with the Plan and the Scheme if the relevant grantee ceases to be employed by the Group. As at 31 March 2003, no other options has been granted under the Scheme and none of the options has been exercised. However, options to subscribe for 7,200,000 shares lapsed during the year as certain grantees have ceased to be employees of the Group. All options under the Plan and the Scheme have been granted to each grantee in consideration for the payment of HK$1.00. Particulars of the outstanding options granted to the Directors of the Company as at 31 March 2003 are set out below:

	Pre-IPO Share Option Plan	**Share Option Scheme**
Name	**Number of underlying shares**	
Ex-directors:		
Mr. Mak Kam Wah	—	3,600,000
Mr. Chu Ho Hwa, Howard	3,600,000	—
Mr. Wang Wei Hung	3,600,000	—

No options were waived or exercised up to the date of this report.

Subsequent to 31 March 2003, the above directors had resigned and their options lapsed after three months of their resignation.

Save as disclosed above, none of the Directors or their spouses or children under 18 years of age had any right to subscribe for the shares of the Company, or had exercised any right during the year and up to the date of this report.

Save as disclosed above, at no time during the year was the Company or any of its subsidiaries a party to any arrangements to enable the Directors of the Company to acquire benefits by means of acquisition of shares in, or debentures of, the Company or any other body corporate.

Report of the Directors

Directors' interest in equity

As at 31 March 2003, the interests of the Directors and their associates in the share capital of the Company and its associated corporations (as defined in the Securities (Disclosure of Interests) Ordinance ("SDI Ordinance")), as required to be recorded in the register maintained under Section 29 of the SDI Ordinance of the Company or which required, pursuant to rules 5.40 to 5.49 of the GEM Listing Rules, to be notified to the Company and the Stock Exchange are as follows:

The Directors' interest in the Company:

Name	Type of inteest	Number of shares	Percentage of issued share capital
Mr. Tsoi Siu Ching, Leo	Corporate *(Note 1)*	472,384,000	57.61%
Mr. Mak Kam Wah	Personal	3,814,000	0.47%

The Director's interest in Arcon Technology Limited, a subsidiary of the Group:

Name	Personal Interests	Corporate Interests	Total Interests
Mr. Tsoi Siu Ching, Leo	10,250,000 Deferred Shares *(Note 3)*	5,000,000 Deferred Shares *(Notes 2 and 3)*	15,250,000 Deferred Shares *(Note 3)*

The Director's interest in Satellite Devices Corporation, a subsidiary of the Group:

Name	Corporate Interests	Total Interests
Mr. Tsoi Siu Ching, Leo	387,888,000 Ordinary Shares *(Note 4)*	387,888,000 Ordinary Shares

Note 1: Mr. Tsoi Siu Ching, Leo held these shares through Upgrade Technology Limited, a company in which Mr. Tsoi Siu Ching, Leo holds 100% of its issued share capital.

Note 2: These deferred shares are held by Winland Nominees Limited as nominee of Mr. Tsoi Siu Ching, Leo.

Note 3: These deferred shares carry rights with regards to distribution of capital and voting as summarized in paragraph (j) under the subsection headed "Corporate reorganisation" in the Company's prospectus dated 8 August 2000.

Note 4: Mr. Tsoi Siu Ching, Leo held 57.61% of the issued share capital of the Company through Upgrade Technology Limited, a company which is wholly and beneficially owned by Mr. Tsoi Siu Ching, Leo. The Company is interested in 387,888,000 shares of Satellite Devices Corporation held by its wholly owned subsidiary, Arcon Solutions (BVI) Limited.

Save as disclosed above, as at 31 March 2003, none of the Directors or their associates had any interests in the share capital of the Company and its associated corporations as defined in the SDI Ordinance.

Report of the Directors

Substantial shareholders

As at 31 March 2003, according to the register of substantial shareholders maintained under section 16(1) of the SDI Ordinance, the following persons are interested in 10% or more of the Company's issued share capital:

Name	Number of shares	Percentage of issued share capital
Upgrade Technology Limited *(Note 1)*	472,384,000	57.61%
Oaktree Capital Management LLC	92,020,000	11.22%

Note 1: Mr. Tsoi Siu Ching, Leo held these shares through Upgrade Technology Limited, a company in which Mr. Tsoi Siu Ching, Leo holds 100% of its issued share capital.

Other than as disclosed above, the Company has not been notified of any other interests representing 10% or more of the Company's issued share capital as at 31 March 2003.

Competing Interests

None of the Directors, initial management shareholders and their respective associates of the Company has an interest in a business which competes or may compete with the business of the Group.

Management contracts

No contracts concerning the management and administration of the whole or any substantial part of the business of the Company were entered into or existed during the year.

Major customers and suppliers

The percentages of sales and purchases for the year attributable to the Group's major customers and suppliers are as follows:

Sales	
- the largest customer	19%
- five largest customers combined	61%
Purchases	
- the largest supplier	11%
- five largest suppliers combined	47%

None of the Directors, their associates or any shareholder (which to the knowledge of the Directors owns more than 5% of the Company's share capital) had an interest in the major customers or suppliers noted above.

Audit committee

The Company established an audit committee with written terms of reference in compliance with Rules 5.23 to 5.25 of the GEM Listing Rules. The audit committee has three members comprising Messrs. Lo Chi Ko, Ho Yung San and Yip Ho Bun, Edwin. The primary duties of the audit committee are to review and supervise the financial reporting process and internal control of the Group. During the year the audit committee has met 4 times with the management to discuss and review the Group's various issues with a view to further improve the Group's corporate governance.

Report of the Directors

Board practices and procedures

The Group has complied with Board Practices and Procedures as set out in rules 5.28 to 5.39 of the GEM Listing Rules throughout the year.

Pre-emptive rights

There are no provisions for pre-emptive rights under the Company's Articles of Association, although there are no restrictions against such rights under the laws in the Cayman Islands.

Sponsor's interest

As updated and notified by the Company's sponsor, ICEA Capital Limited (the "Sponsor"), as at 31 March 2003, neither the Sponsor nor its directors or employees or associates (as referred to in Note 3 to Rule 6.35 of the GEM Listing Rules) had any interests in the securities of the Company or any company in the Group or any rights to subscribe for or to nominate persons to subscribe for the securities of the Company or any company in the Group.

Pursuant to the sponsorship agreement dated 7 August 2000 entered into between the Company and the Sponsor, the Sponsor would receive sponsorship fees for acting as the Company's retained sponsor until 31 March 2003. The sponsorship agreement terminated on 31 March 2003.

Retirement benefits scheme

Details of the retirement benefits scheme are set out in note 11 to the accounts.

Subsequent events

Details of the post balance sheet events which have been taken place subsequent to the balance sheet date are set out in note 28 to the accounts.

Auditors

PricewaterhouseCoopers resigned as joint auditors of the Company on 21 May 2003. Graham H.Y. Chan & Co. remained as the Company's auditors from that date.

The accounts have been audited by Graham H.Y. Chan & Co. who retire and, being eligible, offer themselves for re-appointment.

On behalf of the Board

Tsoi Siu Ching, Leo
Chairman

Hong Kong, 20 November 2003

Auditors' Report

GRAHAM H.Y. CHAN & CO.
CERTIFIED PUBLIC ACCOUNTANTS
HONG KONG

陳浩賢會計師事務所

AUDITORS' REPORT TO THE SHAREHOLDERS OF ARCONTECH CORPORATION
(incorporated in the Cayman Islands with limited liability)

We have audited the accounts on pages 21 to 59 which have been prepared in accordance with accounting principles generally accepted in Hong Kong.

Respective responsibilities of directors and auditors

The Company's directors are responsible for the preparation of accounts which give a true and fair view. In preparing accounts which give a true and fair view it is fundamental that appropriate accounting policies are selected and applied consistently.

It is our responsibility to form an independent opinion, based on our audit, on those accounts and to report our opinion to you.

Basis of opinion

We conducted our audit in accordance with Statements of Auditing Standards issued by the Hong Kong Society of Accountants. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the accounts. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the accounts, and of whether the accounting policies are appropriate to the circumstances of the Company and the Group, consistently applied and adequately disclosed.

We planned our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance as to whether the accounts are free from material misstatement. However, the evidence available to us was limited as follows:

1. Included in deposits, prepayments and other receivables in the consolidated balance sheet is a prepayment of masking, engineering and tooling charges totalling HK$42,640,000 made to a supplier for developing proprietary mobile phone chipsets. The prepaid masking charge is refundable in terms of rebate on purchases made by the Group in accordance with the agreement signed between Arcon Technology Limited ("ATL"), a wholly-owned subsidiary of the Company, and the supplier, details of which are disclosed in note 17 to the accounts. As at the date of this report, no purchases of the chipset has been made by ATL. In view of the financial difficulties suffered by the Group and the winding up petition as mentioned in the paragraph of "Fundamental uncertainty" below which had adversely affected the normal operations of the Group, it is uncertain whether purchases will be made and thus whether the prepaid masking charge will be refunded. There were no other satisfactory audit procedures we could adopt to ascertain that the prepayment was recoverable. Any adjustment to the amount of this asset would increase the loss of the Group for the year ended 31 March 2003 and reduce the Group's net assets at that date by that amount.

2. We did not receive a sufficient number of replies to confirmations requested from the Group's suppliers on the amounts of purchases for the year ended 31 March 2003 and of trade payables as at that date. Total sample amounts selected by us for such confirmation purpose amounted to approximately HK$426,463,000 and HK$105,929,000 respectively out of the population of total purchases for the year and the year-end trade payable balance of approximately HK$608,005,000 and HK$114,682,000 respectively. As at the date of this report, replies to confirmations not yet received by us amounted to approximately HK$105,748,000 for purchases and HK$19,134,000 for trade payable balances. There were no other satisfactory audit procedures we could adopt to confirm that all purchases for the year ended 31 March 2003 and all liabilities as at that date were properly recorded.

Auditors' Report

3. We did not receive a sufficient number of replies to confirmations requested from the Group's customers on amounts of sales for the year ended 31 March 2003 and of receivables as at that date. Total sample amounts selected by us for such confirmation purpose amounted to approximately HK$453,409,000 and HK$426,206,000 respectively out of the population of total sales for the year and the year-end trade receivable balance before provision for bad and doubtful debts of approximately HK$540,367,000 and HK$456,761,000 respectively. As at the date of this report, replies to confirmations not yet received by us amounted to approximately HK$59,926,000 for sales and HK$54,763,000 for trade receivable balances. There were no other satisfactory audit procedures we could adopt to confirm that all sales for the year ended 31 March 2003 and all assets as at that date were properly recorded.

In forming our opinion we also evaluated the overall adequacy of the presentation of information in the accounts. We believe that our audit provides a reasonable basis for our opinion.

Fundamental uncertainty relating to the going concern basis

In forming our opinion, we have considered the adequacy of the disclosures made in the accounts concerning the basis adopted in the preparation of the Group's accounts. The Group incurred a loss attributable to shareholders of HK$421,107,000 for the year ended 31 March 2003 and had net current liabilities of HK$43,794,000 as at 31 March 2003. Further, as explained in note 1 to the accounts, subsequent to the balance sheet date, one of the Group's bank creditors has filed a winding up petition against each of the Company and its principal subsidiary, Arcon Technology Limited. Some other major bank creditors have also demanded for immediate payments of the amounts due to them. The Company has engaged its legal adviser to advise on the petition and prepare its defence. Simultaneously, the Group is in negotiation with its bank creditors, on a without prejudice basis, to reach a debt restructuring agreement, the outcome of which is uncertain at this stage. Nevertheless, the directors have prepared the accounts on the going concern basis. In these circumstances we are unable to determine whether the use of the going concern basis in the preparation of these accounts is appropriate. We are unable to quantify the adjustments that would be required, if any, had these accounts been prepared on a break-up basis.

Disclaimer on view given by the accounts

Because of the significance of the effect on the accounts should the preparation of accounts on a going concern basis become not appropriate and the limitations in evidence available to us in respect of the matters as mentioned in the section of "Basis of opinion", we are unable to form an opinion as to whether the accounts give a true and fair view of the state of affairs of the Company and of the Group as at 31 March 2003 and of the Group's loss and cash flows for the year then ended and as to whether the accounts have been properly prepared in accordance with the disclosure requirements of the Hong Kong Companies Ordinance.

In respect alone of the limitations on our work as set out in the section "Basis of opinion":

(i) we have not obtained all the information and explanations that we considered necessary for the purposes of our audit; and

(ii) we were unable to determine whether proper books of account had been kept.

Graham H.Y Chan & Co.
Certified Public Accountants

Hong Kong, 20 November 2003

Consolidated Profit and Loss Account

For the year ended 31 March 2003

	Note	2003 HK$'000	2002 HK$'000
Turnover	3	**540,367**	472,395
Cost of sales		**(425,822)**	(321,799)
Gross profit		**114,545**	150,596
Other revenues	3	**3,270**	691
Selling and distribution expenses		**(9,819)**	(10,270)
General and administrative expenses		**(83,590)**	(63,313)
Gain on deemed disposal of interests in a subsidiary		**—**	7,242
Gain on disposal of subsidiaries		**398**	—
Loss on disposal of fixed assets		**(857)**	—
Write off and write down on value of inventories		**(18,897)**	—
Provision for inventories		**(85,765)**	—
Provision for bad and doubtful debts		**(349,224)**	—
Provision for other receivable		**(2,000)**	—
Operating (loss)/profit	3, 4	**(431,939)**	84,946
Finance costs	5	**(7,242)**	(3,914)
(Loss)/profit before taxation		**(439,181)**	81,032
Taxation credit/(charge)	6	**8,743**	(12,906)
(Loss)/profit after taxation		**(430,438)**	68,126
Minority interests		**9,331**	(514)
(Loss)/profit attributable to shareholders	7, 22	**(421,107)**	67,612
Dividends	8	**16,810**	35,695
Basic (loss)/earnings per share	9	**(51.84) cents**	9.39 cents

Consolidated Balance Sheet

As at 31 March 2003

	Note	2003 HK$'000	2002 HK$'000
Fixed assets	12	**84,500**	110,107
Investments in associated companies	14	**4**	4
Current assets			
Inventories	15	**90,831**	13,311
Trade receivables	16	**107,537**	325,925
Deposits, prepayments and other receivables	17	**57,386**	18,596
Tax recoverable		**6,728**	—
Cash and bank balances		**3,621**	76,036
		266,103	433,868
Current liabilities			
Trade payables	18	**114,682**	6,707
Other payables and accruals		**8,463**	6,920
Amount due to a director	19	**168**	2,182
Current portion of long-term liabilities	23	**21,814**	7,607
Trust receipt and factoring loans		**143,012**	91,219
Tax payable		**—**	16,680
Bank overdrafts		**21,758**	14,009
		309,897	145,324
Net current (liabilities)/assets		**(43,794)**	288,544
Total assets less current liabilities		**40,710**	398,655
Financed by:			
Share capital	20	**82,000**	72,000
Reserves	22(a)	**(63,404)**	265,476
Shareholders' funds		**18,596**	337,476
Minority interests		**22,114**	31,448
Long-term liabilities	23	**—**	20,988
Deferred taxation	24	**—**	8,743
		40,710	398,655

On behalf of the Board

Tsoi Siu Ching, Leo
Director

Yip Ho Bun, Edwin
Director

Balance Sheet

As at 31 March 2003

	Note	2003 HK$'000	2002 HK$'000
Investments in subsidiaries	13	**22,362**	153,751
Current assets			
Deposits and prepayments		**1,263**	49
Bank balance		**1**	65
		1,264	114
Current liabilities			
Other payables and accruals		**678**	558
Net current assets/(liabilities)		**586**	(444)
Total assets less current liabilities		**22,948**	153,307
Financed by:			
Share capital	20	**82,000**	72,000
Reserves	22(b)	**(59,052)**	81,307
Shareholders' funds		**22,948**	153,307

On behalf of the Board

Tsoi Siu Ching, Leo
Director

Yip Ho Bun, Edwin
Director

Consolidated Statement of Changes in Equity

For the year ended 31 March 2003

	2003 HK$'000	2002 HK$'000
Balance of total equity at beginning of year	**337,476**	305,582
Issue of new shares	**10,000**	—
Share premium arising on issue of new shares	**113,000**	—
Share issuing expenses	**(3,855)**	—
Dividends:		
Special interim dividend in specie of shares in a subsidiary	**—**	(10,495)
2001 Final dividend	**—**	(10,800)
2002 Interim dividend	**—**	(14,400)
2002 Final dividend	**(8,200)**	—
2003 Interim dividend	**(8,610)**	—
Exchange differences arising on translation of accounts of overseas subsidiaries	**(108)**	(23)
(Loss)/profit attributable to shareholders	**(421,107)**	67,612
Balance of total equity at end of year	**18,596**	337,476

Consolidated Cash Flow Statement

For the year ended 31 March 2003

	Note	2003 HK$'000	2002 HK$'000
Cash flows from operating activities			
Cash used in operations	25(a)	**(194,382)**	(33,617)
Interests on bank loans and overdrafts paid		**(7,174)**	(3,839)
Interest element of finance leases paid		**(68)**	(75)
Hong Kong profits tax paid		**(23,385)**	(1,790)
Overseas taxation paid		**(23)**	—
Net cash used in operating activities		**(225,032)**	(39,321)
Cash flows from investing activities			
Purchase of fixed assets		**(3,810)**	(61,558)
Proceeds from disposal of fixed assets		**47**	—
Investment in an associated company		**—**	(4)
Proceeds from disposal of subsidiaries	25(b)	**341**	—
Interest received		**1,054**	448
Net cash used in investing activities		**(2,368)**	(61,114)
Cash flows from financing activities			
New bank loans raised		**—**	27,300
Bank loans repaid		**(6,427)**	(401)
Increase in trust receipt and factoring loans		**51,793**	77,242
Repayment of capital element of finance leases		**(354)**	(381)
Net proceeds from issue of shares by the Company		**119,145**	—
Net proceeds from issue of shares by a subsidiary to the minority shareholders		**—**	22,089
Dividends paid		**(16,810)**	(25,200)
Net cash from financing activities		**147,347**	100,649
Net (decrease)/increase in cash and cash equivalents		**(80,053)**	214
Effect of foreign exchange rate changes		**(111)**	(23)
Cash and cash equivalents at beginning of year		**62,027**	61,836
Cash and cash equivalents at end of year		**(18,137)**	62,027
Analysis of balances of cash and cash equivalents:			
Cash and bank balances		**3,621**	76,036
Bank overdrafts		**(21,758)**	(14,009)
		(18,137)	62,027

Notes to the Accounts

For the year ended 31 March 2003

1 Basis of preparation

The accounts have been prepared on a going concern basis which assumes, among other things, the realisation of assets and satisfaction of liabilities in the normal course of business. The assumption is dependent upon the successful completion of the restructuring of the Group's debts, the withdrawal of the winding-up petition by the bank creditor, the continuing financial support of the Group's bankers and other external funds being available.

Subsequent to the balance sheet date, one of the Group's bank creditors, the Hongkong and Shanghai Banking Corporation Limited, has filed a winding up petition against each of the Company and its principal subsidiary, Arcon Technology Limited. Some other major bank creditors have also demanded for immediate payments of the amounts due to them. In the absence of additional funding, the Group cannot meet the demands for immediate payments of its debts. The Company has engaged its legal adviser to advise on the petition and prepare its defence.

The Group is currently engaged in negotiations with its bank creditors, on a without prejudice basis, to achieve a debt restructuring agreement, but formal agreement has not been reached up to the date of this report.

In the absence of a formal standstill agreement to restructure the Group's bank loans and other debts, the directors consider that it is more appropriate to classify all borrowings of the Group as current liabilities in the accounts.

The accounts have been prepared in accordance with accounting principles generally accepted in Hong Kong and comply with accounting standards issued by the Hong Kong Society of Accountants ("HKSA"). They have been prepared under the historical cost convention as modified by the revaluation of leasehold land and buildings and investment properties.

In current year, the Group has adopted, for the first time, the following new and revised Statements of Standard Accounting Practice ("SSAPs") issued by the HKSA which are effective for accounting periods commencing on or after 1 January 2002:

SSAP 1 (revised)	Presentation of financial statements
SSAP 15 (revised)	Cash flow statements
SSAP 34	Employee benefits

These SSAPs prescribe new accounting measurement and disclosure practices. The major effects on the Group's accounting policies on the amounts disclosed in the accounts of adopting these SSAPs are summarised as follows:

SSAP 1 (revised) prescribes the basis for the presentation of accounts and set out guidelines for their structure and minimum requirements for the content thereof. The principal impact of the revision to this SSAP is that a consolidated statement of changes in equity is now presented on page 24 in place of the consolidated statement of recognised gains and losses that was previously required.

Notes to the Accounts

For the year ended 31 March 2003

1 Basis of preparation (Continued)

SSAP 15 (revised) prescribes the format for the cash flow statement. The principal impact of the revision on this SSAP is that cash flows are now presented under three headings, that is, cash flows from operating, investing and financing activities, rather than the five headings previously required. The format of the consolidated cash flow statement set out on page 25 of the accounts and the notes thereto have been revised in accordance with the new requirements.

SSAP 34 prescribes the recognition and measurement criteria to apply to employee benefits, together with the required disclosures in respect thereof. The adoption of this SSAP has resulted in additional disclosures relating to the Company's share option scheme, as set out in note 21 of the accounts.

The adoption of these new and revised SSAPs has no material impact on the accounts of the Group for the current and prior accounting periods. Accordingly, no prior period adjustment is required.

2 Principal accounting policies

The principal accounting policies adopted in the preparation of these accounts are set out below:

(a) Group accounting

(i) Consolidation

The consolidated accounts include the accounts of the Company and its subsidiaries made up to 31 March. Subsidiaries are those entities in which the Group controls the composition of the board of directors, controls more than half the voting power or holds more than half of the issued share capital, or by way of having power to govern its financial and operating policies so that the Group obtains benefits from their activities.

The results of subsidiaries acquired or disposed of during the year are included in the consolidated profit and loss account from the effective date of acquisition or up to the effective date of disposal, except for some of the subsidiaries which were accounted for using merger accounting as a result of the group reorganisation took place in 2001.

All significant intercompany transactions and balances within the Group are eliminated on consolidation.

The gain or loss on the disposal of a subsidiary represents the difference between the proceeds of the sale and the Group's share of its net assets together with any unamortised goodwill or negative goodwill taken to reserves and which was not previously charged or recognised in the consolidated profit and loss account.

Minority interests represent the interests of outside shareholders in the operating results and net assets of subsidiaries.

In the Company's balance sheet the investments in subsidiaries are stated at cost less provision for impairment losses. The results of subsidiaries are accounted for by the Company on the basis of dividends received and receivable.

Notes to the Accounts

For the year ended 31 March 2003

2 Principal accounting policies (Continued)

(a) Group accounting (continued)

(ii) Associated companies

An associated company is a company, not being a subsidiary, in which an equity interest is held for the long-term and significant influence is exercised in its management.

The consolidated profit and loss account includes the Group's share of the results of associated companies for the year, and the consolidated balance sheet includes the Group's share of the net assets of the associated companies.

Equity accounting is discontinued when the carrying amount of the investment in an associated company reaches zero, unless the Group has incurred obligations or guaranteed obligations in respect of the associated company.

(b) Fixed assets

(i) Investment properties

Investment properties are interests in land and buildings in respect of which construction work and development have been completed, and which are held for their investment potential, any rental income being negotiated at arm's length. Investment properties are stated at valuation on an open market value basis, based on independent professional valuations at the balance sheet date. Any surplus or deficit arising on the revaluation of investment properties is credited or debited to the investment properties revaluation reserve unless the balance of this reserve is insufficient to cover a deficit on a portfolio basis, in which case the excess of the deficit over the balance on the investment properties revaluation reserve is charged to the profit and loss account. Where a deficit has previously been charged to the profit and loss account and a revaluation surplus subsequently arises, this surplus is credited to the profit and loss account to the extent of the deficit previously charged.

No depreciation is provided on investment properties except where the unexpired term of the relevant lease is 20 years or less, in which case depreciation is provided on the carrying amount over the remaining term of the lease.

Upon the disposal of an investment property, the balance of the investment properties revaluation reserve attributable to the properties disposed of is released from the investment properties revaluation reserve to the profit and loss account.

Notes to the Accounts

For the year ended 31 March 2003

2 Principal accounting policies (Continued)

(b) Fixed assets (continued)

(ii) Leasehold land and buildings

Leasehold land and buildings are stated at valuation, being the fair value at the date of revaluation, less subsequent accumulated depreciation or amortisation. Fair value is the amount for which an asset could be exchanged between knowledgeable, willing parties in an arm's length transaction and is determined on the basis of existing use. Increases in valuation are credited to the revaluation reserve. Decreases in valuation are first offset against increases on earlier valuations in respect of the same property and are thereafter charged to profit and loss account. Any subsequent revaluation surplus is credited to the profit and loss account to the extent of the deficit previously charged. During the year, the Group's leasehold land and buildings have been transferred to investment properties upon the change in use of the relevant properties from owner occupation to investment purpose.

(iii) Amortisation of leasehold land

Amortisation of leasehold land is calculated to write off its valuation over the unexpired period of the lease on a straight-line basis. The principal annual rate for this purpose is 2%.

(iv) Depreciation of leasehold buildings

Depreciation of leasehold buildings is calculated to write off their valuation over the expected useful lives to the Group on a straight-line basis. The principal annual rate used for this purpose is 4%.

(v) Other fixed assets

Other fixed assets are stated at cost less accumulated depreciation and accumulated impairment losses. Depreciation of other fixed assets is calculated to write off their cost on a straight-line basis over their expected useful lives to the Group. The principal annual rates are as follows:

Furniture, fixtures and office equipment, and computer equipment	20% - 33$^1/_3$%
Motor vehicles	25%

Major costs incurred in restoring fixed assets to their normal working condition are charged to the profit and loss account. Improvements are capitalised and depreciated over their expected useful lives to the Group.

The gain or loss on disposal of a fixed asset is the difference between the net sales proceeds and the carrying amount of the relevant asset, and is recognised in the profit and loss account.

Notes to the Accounts

For the year ended 31 March 2003

2 Principal accounting policies (Continued)

(c) Leases

(i) Finance leases

Leases that substantially transfer to the Group all the risks and rewards of ownership of assets are accounted for as finance leases. Finance leases are capitalised at the inception of the leases at the lower of the fair value of the leased assets or the present value of the minimum lease payments. Each lease payment is allocated between the capital element and finance charges so as to achieve a constant rate on the capital balances outstanding. The corresponding rental obligations, net of finance charges, are included in long-term liabilities. The finance charges are charged to the profit and loss account over the lease periods.

(ii) Operating leases

Leases where substantially all the risks and rewards of ownership of assets remain with the leasing company are accounted for as operating leases. Payments made under operating leases net of any incentives received from the leasing company are charged to the profit and loss account on a straight-line basis over the lease periods.

(d) Inventories

Inventories are stated at the lower of cost and net realisable value. Cost, calculated on the first-in, first-out basis, comprises all costs of purchase and other costs incurred in bringing the inventories to their present location and condition. Net realisable value is determined on the basis of anticipated sales proceeds less estimated selling expenses.

(e) Trade receivables

Provision is made against trade receivables to the extent they are considered to be doubtful. Trade receivables in the balance sheet are stated net of such provision, if any.

Notes to the Accounts

For the year ended 31 March 2003

2 Principal accounting policies (Continued)

(f) Impairment of assets

Assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of these assets may not be recoverable. Whenever the carrying amount of an asset exceeds its recoverable amount, an impairment loss representing the difference between the carrying amount and the recoverable amount of an asset, is recognised as an expense, unless the relevant asset is carried at a revalued amount, in which case the impairment loss is treated as a revaluation decrease. The recoverable amount is the higher of an asset's net selling price and value in use. The net selling price is the amount obtainable from the sale of an asset in an arm's length transaction less the costs of disposal, while value in use is the present value of estimated future cash flows expected to arise from the continuing use of an asset and from its disposal at the end of its useful life. Recoverable amounts are estimated for individual assets, or if it is not possible, for the cash-generating unit.

Reversal of an impairment loss of an asset recognised in prior years is recorded when there is an indication that the impairment loss recognised for the asset no longer exists or has decreased. Where an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset in prior years. A reversal of an impairment loss is recognised as income, unless the relevant asset is carried at a revalued amount, in which case the reversal of the impairment loss is treated as a revaluation increase.

(g) Cash and cash equivalents

Cash and cash equivalents are carried in the balance sheet at cost. For the purposes of the cash flow statement, cash and cash equivalents comprise cash on hand, deposits held at call with banks, cash investments with a maturity of three months or less from date of investment and bank overdrafts.

(h) Provisions

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation, and a reliable estimate of the amount can be made.

(i) Deferred taxation

Deferred taxation is accounted for at the current taxation rate in respect of timing differences between profit as computed for taxation purposes and profit as stated in the accounts to the extent that a liability or an asset is expected to be payable or recoverable in the foreseeable future.

Notes to the Accounts

For the year ended 31 March 2003

2 Principal accounting policies (Continued)

(j) Translation of foreign currencies

Foreign currency transactions are recorded at the applicable rates of exchange ruling at the transaction dates. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated at the applicable rates of exchange ruling at that date. Exchange differences arising in these cases are dealt with in the consolidated profit and loss account.

On consolidation, the accounts of overseas subsidiaries are translated into Hong Kong dollars using the net investment method. The profit and loss accounts of overseas subsidiaries are translated into Hong Kong dollars at the average rates for the year. The balance sheets of overseas subsidiaries are translated into Hong Kong dollars at the exchange rates ruling at the balance sheet date. The resulting translation differences are dealt with as a movement in the exchange reserve.

(k) Employee benefits

(i) Salaries, annual bonuses, paid annual leave, leave passage and the cost to the Group of non-monetary benefits are accrued in the year in which the associated services are rendered by employees of the Group. Where payment or settlement is deferred and the effect would be material, these amounts are stated at their present values.

(ii) Contributions to Mandatory Provident Fund as required under the Hong Kong Mandatory Provident Fund Schemes Ordinance, are recognised as an expense in the profit and loss account as incurred.

(iii) The financial impact of share options granted is not recorded in the Company's or the Group's balance sheet until such time as the options are exercised, and no charge is recognised in the profit and loss account in respect of the value of options granted during the year. Upon exercise of the share options, the resulting shares issued are recorded by the Company as additional share capital at the nominal value of the shares, and the excess of the exercise price per share over the nominal value of the shares is recorded by the Company in the share premium account. Options which are cancelled or which lapsed prior to their exercise date are deleted from the register of outstanding options and have no impact on the profit and loss account or balance sheet.

(l) Research and development costs

Costs incurred in the research and development of products of the Group are expensed as incurred unless the costs of development satisfy the criteria for the recognition of such costs as assets. During the year, all research and development costs have been expensed.

Notes to the Accounts

For the year ended 31 March 2003

2 Principal accounting policies (Continued)

(m) Revenue recognition

Revenue from the sale of goods is recognised on the transfer of risks and rewards of ownership, which generally coincides with the time when goods are delivered to customers and title has passed.

Royalty income and commission income on sales referral is recognised when the right to receive payment is established.

Software and internet service income is recognised when the services are rendered.

Rental income on operating leases is recognised on a straight-line basis over the period of the relevant leases.

Interest income is recognised on a time proportion basis, taking into account the principal amounts outstanding and the interest rates applicable.

(n) Borrowing costs

All borrowing costs are charged to the profit and loss account in the year in which they are incurred except for those borrowing costs that are directly attributable to the acquisition, construction or production of an asset that necessarily takes a substantial period of time to get ready for its intended use or sale, which are capitalised as part of the cost of that asset. During the year, all borrowing costs have been expensed.

(o) Segment reporting

A segment is a distinguishable component of the Group that is engaged either in providing products or services (business segment), or in providing products or services within a particular economic environment (geographical segment), which is subject to risks and rewards that are different from those of other segments.

In accordance with the Group's internal financial reporting the Group has determined that business segments be presented as the primary reporting format and geographical segment as the secondary reporting format.

Segment assets consist primarily of fixed assets, inventories, receivables and operating cash, and exclude investments in associated companies. Segment liabilities comprise operating liabilities. Capital expenditure comprises additions to fixed assets (note 12).

Notes to the Accounts

For the year ended 31 March 2003

3 Turnover, revenues and segment information

The Group is principally engaged in the design, development of software and engineering solutions including the sales of semiconductors and other electronic components, and the location-based technology devices and applications ("GPS") in Hong Kong. Revenues recognised during the year are as follows:

	Group	
	2003	2002
	HK$'000	HK$'000
Turnover		
Sale of goods	**526,379**	445,656
Royalty income	**13,988**	26,739
	540,367	472,395
Other revenues		
Commission income	**—**	124
Software and internet service income	**256**	119
Operating lease rental income from investment property	**74**	—
Interest income	**1,054**	448
Sundry income	**1,886**	—
	3,270	691
Total revenues	**543,637**	473,086

Notes to the Accounts

For the year ended 31 March 2003

3 Turnover, revenues and segment information (Continued)

As the Group's operations are principally located in Hong Kong, no geographical segmental analysis is presented. An analysis of the Group's revenue, segment results and segment assets by principal business segment is as follows:

	Sales of software and engineering solutions excluding GPS 2003 HK$'000	**Sales of GPS 2003 HK$'000**	**Group 2003 HK$'000**	Sales of software and engineering solutions excluding GPS 2002 HK$'000	Sales of GPS 2002 HK$'000	Group 2002 HK$'000
Turnover	**482,917**	**57,450**	**540,367**	443,835	28,560	472,395
Segment results	**(402,970)**	**(29,367)**	**(432,337)**	82,967	(5,263)	77,704
Gain on deemed disposal of interests in a subsidiary			**—**			7,242
Gain on disposal of subsidiaries			**398**			—
Operating (loss)/profit			**(431,939)**			84,946
Finance costs			**(7,242)**			(3,914)
(Loss)/profit before taxation			**(439,181)**			81,032
Taxation credit/(charge)			**8,743**			(12,906)
(Loss)/profit after taxation			**(430,438)**			68,126
Minority interests			**9,331**			(514)
(Loss)/profit attributable to shareholders			**(421,107)**			67,612
Segment assets	**251,590**	**99,013**	**350,603**	450,706	93,269	543,975
Investments in associated companies			**4**			4
Total assets			**350,607**			543,979
Segment liabilities	**278,575**	**53,436**	**332,011**	170,325	36,178	206,503
Other information						
Capital expenditure	**1,705**	**3,805**	**5,510**	36,830	24,728	61,558
Depreciation	**18,113**	**11,723**	**29,836**	7,080	7,011	14,091
Loss on disposal of fixed assets	**413**	**444**	**857**	—	—	—
Write off and write down on value of inventories	**12,859**	**6,038**	**18,897**	—	—	—
Provision for inventories	**85,765**	**—**	**85,765**	—	—	—
Provision for bad and doubtful debts	**336,987**	**12,237**	**349,224**	—	—	—
Provision for other receivable	**2,000**	**—**	**2,000**	—	—	—

Notes to the Accounts

For the year ended 31 March 2003

4 Operating (loss)/profit

Operating (loss)/profit is stated after charging the following:

	Group	
	2003	2002
	HK$'000	HK$'000
Auditors' remuneration		
- current year provision	**650**	1,500
- underprovision in prior year	**172**	—
Depreciation of fixed assets		
- owned assets	**29,457**	13,712
- assets held under finance leases	**379**	379
Operating lease rentals in respect of land and buildings	**4,335**	2,110
Research and development costs *(note (a))*	**11,815**	11,296
Staff costs excluding directors' emoluments		
- salaries, bonus, allowances and benefits in kind	**23,604**	27,435
- retirement benefits scheme contributions *(note 11)*	**545**	635
Deficit arising from revaluation of property	**263**	73
Net exchange loss	**255**	139

(a) Included in the research and development costs were staff costs of HK$9,950,000 (2002: HK$10,757,000) which had also been included in staff costs disclosed above.

5 Finance costs

	Group	
	2003	2002
	HK$'000	HK$'000
Interest on bank loans and overdrafts	**7,174**	3,839
Interest element of finance leases	**68**	75
	7,242	3,914

Notes to the Accounts

For the year ended 31 March 2003

6 Taxation

The taxation (credit)/charge comprises:

	Group	
	2003	2002
	HK$'000	HK$'000
Hong Kong profits tax *(note (a))*	**—**	8,973
Overseas taxation *(note (b))*	**—**	37
(Over)/under provision in prior year	**—**	(160)
Deferred taxation *(note 24)*	**(8,743)**	4,056
	(8,743)	12,906

Notes:

a No Hong Kong profits tax has been provided as the Group had no estimated assessable profits for the year.

Hong Kong profits tax was provided at the rate of 16% for the year ended 31 March 2002 on the estimated assessable profits of the Group for that year.

b No overseas taxation has been provided as the Group's overseas subsidiaries did not have any taxable profits for the year.

Overseas taxation for the year ended 31 March 2002 represented tax charge on the estimated assessable profits of a PRC subsidiary for that year calculated at rates prevailing in the PRC.

7 (Loss)/profit attributable to shareholders

The loss attributable to shareholders is dealt with in the accounts of the Company to the extent of HK$232,694,000 for the year.

For the year ended 31March 2002, the profit attributable to shareholders was dealt with in the accounts of the Company to the extent of HK$31,819,000.

Notes to the Accounts

For the year ended 31 March 2003

8 Dividends

	2003 HK$'000	2002 HK$'000
Ordinary cash dividend		
Interim, paid, of HK1.05 cents in respect of 2003 (2002: HK 2 cents) per ordinary share	**8,610**	14,400
Final, paid, of HK1 cent in respect of 2002 (2001: HK1.5 cents) per ordinary share	**8,200**	10,800
	16,810	25,200
Distribution in specie		
Special interim dividend of SDC's shares	**—**	10,495
	16,810	35,695

The interim dividends in respect of 2003 were declared on 31 July 2002, 1 November 2002 and 12 February 2003 for the first three quarters of the year respectively. Before the declaration of such interim dividends, the directors had reviewed the operating results of the Group for the respective quarters and were of the view that it appeared to the Board to be justified by the profits of the Group for the declarations of these interim dividends.

9 (Loss)/earnings per share

The calculation of basic (loss)/earnings per share is based on the Group's loss attributable to shareholders of approximately HK$421,107,000 (2002: profit of HK$67,612,000) and the weighted average number of 812,328,767 ordinary shares (2002: 720,000,000 ordinary shares) in issue during the year.

Diluted (loss)/earnings per share is not presented because there were no dilutive potential ordinary shares outstanding during the two years ended 31 March 2003.

Notes to the Accounts

For the year ended 31 March 2003

10 Directors' and senior management's emoluments

(a) Directors' emoluments

The aggregate amounts of emoluments payable to the directors of the Company during the year are as follows:

	Group	
	2003	2002
	HK$'000	HK$'000
Independent non-executive directors		
Fees	**307**	307
Other emoluments of executive directors		
Basic salaries, allowances and other benefits in kind	**5,934**	4,414
Retirement benefits scheme contributions	**50**	36
	5,984	4,450
Total directors' emoluments	**6,291**	4,757

During the year, each of the executive directors of the Company received individual emoluments from the Group of HK$4,889,000 (2002: HK$3,368,000), HK$532,000 (2002: HK$541,000), HK$259,000 (2002: HK$541,000), HK$304,000 (2002: HK$nil) and HK$nil (2002: HK$nil) respectively.

No directors waived or agreed to waive any of their emoluments in respect of the years ended 31 March 2003 and 2002.

Certain directors of the Company have been granted options to acquire shares of the Company, details of which are set out in note 21 to the accounts. The emoluments of the directors disclosed above do not include the benefits derived or to be derived from the options granted under the Company's share option schemes.

Notes to the Accounts

For the year ended 31 March 2003

10 Directors' and senior management's emoluments (Continued)

(b) Five highest paid individuals

The five individuals whose emoluments were the highest in the Group for the year include one (2002: one) director whose emolument is reflected in the analysis presented above. The emoluments payable to the remaining four (2002: four) individuals during the year are as follows:

	Group	
	2003	2002
	HK$'000	HK$'000
Basic salaries, allowances and other benefits in kind	**3,405**	5,735
Retirement benefits scheme contributions	**44**	50
	3,449	5,785

The emoluments fell within the following bands:

	Number of individuals	
	2003	2002
Nil to HK$1,000,000	**3**	—
HK$1,000,001 - HK$1,500,000	**1**	2
HK$1,500,001 - HK$2,000,000	**—**	2

During the year, no emoluments have been paid by the Group to the directors or the five highest paid individuals as an inducement upon joining the Group, or as compensation for loss of office.

One of the above four highest paid individuals has been granted options to acquire shares of the Company, further details of which are included in the disclosures in note 21 to the accounts. The emoluments of the four highest paid individuals disclosed above do not include the benefits derived or to be derived from the options granted under the Company's share option schemes.

Notes to the Accounts

For the year ended 31 March 2003

11 Retirement benefits costs

The Group operates a mandatory provident fund scheme ("the MPF Scheme") under the Hong Kong Mandatory Provident Fund Schemes Ordinance for employees employed under the jurisdiction of the Hong Kong Employment Ordinance. Under the MPF Scheme, the employer and its employees are each required to make contributions to the scheme at 5% of the employees' relevant income, subject to a cap of monthly relevant income of HK$20,000. The Group's contributions to the MPF Scheme vest fully with the employees. The assets of the MPF Scheme are held separately from those of the Group in an independently administered fund.

Contributions totalling HK$45,000 (2002: HK$102,000) were payable to the MPF Scheme at the year end and are included in other payables and accruals in the consolidated balance sheet.

12 Fixed assets - Group

	Leasehold land and buildings HK$'000	Investment property HK$'000	Furniture, fixtures and office equipment HK$'000	Motor vehicles HK$'000	Computer equipment HK$'000	Total HK$'000
Cost or valuation						
At 1 April 2002	2,350	—	29,600	2,116	92,926	126,992
Additions	—	—	1,725	442	3,343	5,510
Disposals	—	—	(1,492)	(283)	(69)	(1,844)
Disposal of subsidiaries	—	—	(114)	—	—	(114)
Reclassification	(2,350)	2,350	—	—	—	—
Revaluation	—	(300)	—	—	—	(300)
At 31 March 2003	—	2,050	29,719	2,275	96,200	130,244
Accumulated depreciation						
At 1 April 2002	—	—	7,293	1,254	8,338	16,885
Charge for the year	37	—	6,128	446	23,225	29,836
Disposals	—	—	(671)	(236)	(33)	(940)
Reclassification	(37)	37	—	—	—	—
Revaluation	—	(37)	—	—	—	(37)
At 31 March 2003	—	—	12,750	1,464	31,530	45,744
Net book value						
At 31 March 2003	—	2,050	16,969	811	64,670	84,500
At 31 March 2002	2,350	—	22,307	862	84,588	110,107

Notes to the Accounts

For the year ended 31 March 2003

12 Fixed assets - Group (Continued)

The analysis of the cost or valuation of the above assets at 31 March 2003 is as follows:

	Investment property HK$'000	Furniture, fixtures and office equipment HK$'000	Motor vehicles HK$'000	Computer equipment HK$'000	Total HK$'000
At cost	—	29,719	2,275	96,200	128,194
At 2003 valuation *(note (b))*	2,050	—	—	—	2,050
	2,050	29,719	2,275	96,200	130,244

The analysis of the cost or valuation of the above assets at 31 March 2002 is as follows:

	Leasehold land and buildings HK$'000	Furniture, fixtures and office equipment HK$'000	Motor vehicles HK$'000	Computer equipment HK$'000	Total HK$'000
At cost	—	29,600	2,116	92,926	124,642
At 2002 valuation	2,350	—	—	—	2,350
	2,350	29,600	2,116	92,926	126,992

(a) The Group's investment property is situated in Hong Kong and is held under lease of between 10 to 50 years.

(b) The investment property was revalued on the basis of open market value in existing state as at 31 March 2003 by Midland Surveyors Limited, an independent firm of professional valuers.

(c) At 31 March 2003, the net book values of fixed assets held by the Group under finance leases included in the total amounts of furniture, fixtures and office equipment and motor vehicles amounted to HK$126,000 (2002: HK$174,000) and HK$330,000 (2002: HK$660,000) respectively.

Notes to the Accounts

For the year ended 31 March 2003

13 Investment in subsidiaries - Company

	2003 HK$'000	2002 HK$'000
Unlisted shares, at cost	**57**	57
Amounts due from subsidiaries *(note (b))*	**271,279**	160,282
Amounts due to subsidiaries *(note (b))*	**(4,466)**	(3,625)
	266,813	156,657
Less: Provision for impairment loss	**(244,508)**	(2,963)
	22,362	153,751

(a) The following is a list of the principal subsidiaries of the Company as at 31 March 2003:

Company	**Country/place and date of incorporation/ establishment**	**Issued and fully paid up share capital/ registered capital**	**Attributable equity interest %**	**Principal activities and place of operation**
Shares held directly:-				
Arcon Solutions (BVI) Limited	The British Virgin Islands 15 March 2000	US$3,250	100	Investment holding in Hong Kong
Shares held indirectly:-				
Arcon Technology Limited	Hong Kong 17 March 1992	Non-voting deferred shares HK$16,250,000 Ordinary HK$10	100	Sale of semiconductor products and DVD components and design, development of software and engineering solutions in Hong Kong
Satellite Devices Corporation	The Cayman Islands 11 June 2001 (listed on the GEM of the Stock Exchange in HK)	Ordinary HK$57,600,000	67.34	Investment holding in Hong Kong
Satellite Devices (BVI) Limited	The British Virgin Islands 15 March 2000	Ordinary US$3	67.34	Investment holding in Hong Kong

Notes to the Accounts

For the year ended 31 March 2003

13 Investment in subsidiaries - Company (Continued)

Company	Country/place and date of incorporation/ establishment	Issued and fully paid up share capital/ registered capital	Attributable equity interest %	Principal activities and place of operation
Satellite Devices Limited	Hong Kong 14 July 1999	Ordinary HK$5,000,000	67.34	Design, development and sales of location-based technology devices and applications in Hong Kong
衛科導航技術（深圳）有限公司 ("Satellite Devices Technology (Shenzhen) Company Limited")	The People's Republic of China excluding Hong Kong (the "PRC") 2 August 2002	Registered capital HK$3,000,000	67.34	Provision of technical support services in the PRC
恒星威資訊技術（深圳）有限公司 ("Heng Xing Wei Information Technologies (Shenzhen) Limited")	The People's Republic of China excluding Hong Kong (the "PRC") 23 March 2000	Registered capital HK$3,000,000	100	Provision of technical support services in the PRC
Arcon Management Services Limited	Hong Kong 24 March 2000	Ordinary HK$2	100	Provision of management services in Hong Kong
Arcon Smartdisplay Limited	Hong Kong 6 July 2001	Ordinary HK$2	100	Sales of display panels and audio products and provision of technical support services in Hong Kong

Heng Xing Wei Information Technologies (Shenzhen) Limited and Satellite Devices Technology (Shenzhen) Company Limited have adopted 31 December as their financial year end date in order to comply with the Accounting Regulations of the People's Republic of China for Enterprises with Foreign Investment.

The above includes the subsidiaries of the Company, which, in the opinion of the directors, principally affected the results of the year or formed a substantial portion of the net assets of the Group. To give details of other subsidiaries would, in the opinion of the Directors, result in particulars of excessive length.

(b) The amounts due from/to subsidiaries are unsecured, interest-free and have no fixed terms of repayment.

Notes to the Accounts

For the year ended 31 March 2003

14 Investment in associated companies

	Group	
	2003	2002
	HK$'000	HK$'000
Share of net assets	**1,474**	1,474
Amount due to an associated company *(note (b))*	**(1,470)**	(1,470)
	4	4

(a) The following is a list of the associated companies as at 31 March 2003:

Company	**Place and date of incorporation**	**Principal activities and place of operation**	**Issued share capital**	**Interest held indirectly**
Telematics Systems Limited	Hong Kong 22 June 2001	Sales of vehicle positioning systems and in-vehicle telematics units in Hong Kong	Ordinary shares of HK$10,000	26.94%
New Era Telematics Limited	Hong Kong 5 September 2001	Development and distribution of in-vehicle and ancillary products and provision for ancillary services in the PRC	Ordinary shares of HK$3,000,000	33%

Telematics Systems Limited and New Era Telematics Limited have adopted 31 December as their financial year end date.

Both associated companies were inactive during the year.

(b) The amount due to an associated company is unsecured, interest-free and has no fixed terms of repayment.

Notes to the Accounts

For the year ended 31 March 2003

15 Inventories

	Group	
	2003	2002
	HK$'000	HK$'000
Amount of inventories before provision	**176,596**	13,311
Less: Provision on Unsold Returned Goods *(note (b))*	**(85,765)**	—
	90,831	13,311

(a) As at 31 March 2003, the carrying amount of inventories that were carried at net realisable value amounted to approximately HK$11,650,000.

As at 31 March 2002, all inventories were carried at cost.

(b) Included in the amount of inventories before provision of HK$176,596,000 above, there was a total amount of approximately HK$107,826,000 representing the cost of the goods returned from customers on various dates subsequent to the year-end date ("Returned Goods"). The returns of goods are considered to be an adjusting event after the balance sheet date and have been recognised in the accounts. Certain amount of the Returned Goods were subsequently sold and were stated at their net realisable value. As at the date of this report, amount of approximately HK$85,765,000 of the Returned Goods remained unsold (the "Unsold Returned Goods") on which full provision has been made in the accounts. Included in the amount of the Unsold Returned Goods, there was a total amount of approximately HK$9,768,000 of which the sales were made under factoring arrangement with a bank creditor. According to the factoring agreement signed between Arcon Technology Limited and the bank creditor, the bank creditor has the right to take possession of such lot of returned goods and to sell those goods on such terms as it deems fit and the proceeds of sale, after deduction of all costs and expenses relating to such possession and sale, shall be treated by the bank creditor as a payment of or on account of the debt to which such goods relate.

16 Trade receivables

The Group normally grants credit period ranging from 30 days to 120 days to its trade debtors. As at 31 March 2003, the ageing analysis of trade receivable was as follows:

	Group	
	2003	2002
	HK$'000	HK$'000
0 - 30 days	**20,636**	62,904
31 - 60 days	**30,389**	20,166
61 - 90 days	**28,577**	30,256
Over 90 days	**377,159**	212,599
	456,761	325,925
Less: Provision for bad and doubtful debts	**(349,224)**	—
	107,537	325,925

Notes to the Accounts

For the year ended 31 March 2003

17 Deposits, prepayments and other receivables - Group

Included in deposits, prepayments and other receivables in the consolidated balance sheet is a prepayment of masking, engineering and tooling charges totalling HK$42,640,000 made to a supplier for developing proprietary mobile phone chipsets. According to the sales contract signed by Arcon Technology Limited ("ATL"), a wholly-owned subsidiary of the Company, and the supplier on 15 January 2003, the prepaid masking charge is refundable in the form of 10% rebate on chipset price awarded to ATL by the supplier on all purchases for three subsequent years but ended when purchase rebate reached US$5,000,000. As at the date of this report, no purchases of the chipset as referred to in the contract has been made by ATL. According to the directors, owing to the financial difficulties currently encountered by the Group and the winding up petition as mentioned in note 1 which has adversely affected the normal operations of the Group, no purchase orders can be made. In the opinion of the directors, after the successful completion of the restructuring of the Group's debts and the withdrawal of the winding up petition by the bank creditor, the Group's business will resume to normal and then the Group will be able to make purchases of the chipset and thus the prepaid masking charge will be refunded to the Group. Hence, no provision has been made for the prepaid amount.

18 Trade payables

At 31 March 2003, the ageing analysis of the trade payables was as follows:

	Group	
	2003	2002
	HK$'000	HK$'000
0 - 30 days	**69,465**	4,216
31 - 60 days	**2,987**	700
61 - 90 days	**11,136**	134
Over 90 days	**31,094**	1,657
	114,682	6,707

19 Amount due to a director - Group

The amount is unsecured, interest free and has no fixed term of repayment.

Notes to the Accounts

For the year ended 31 March 2003

20 Share capital

	Number of shares	Amount
		HK$'000
Ordinary shares of HK$0.1 each		
Authorised:		
As at 31 March 2003 and 31 March 2002	3,000,000,000	300,000
Issued and fully paid:		
At 1 April 2001 and 31 March 2002	720,000,000	72,000
At 1 April 2002	720,000,000	72,000
Shares issued pursuant to a placing agreement *(note (a))*	100,000,000	10,000
At 31 March 2003	820,000,000	82,000

(a) On 17 April 2002, the Company entered into a placing agreement and a subscription agreement (the "Agreements") with SBI E2-Capital Securities Limited ("SBI E2") and Upgrade Technology Limited ("Upgrade") pursuant to which SBI E2 will procure purchasers to purchase from Upgrade and Upgrade, in return, will subscribe from the Company for 100,000,000 shares of HK$0.1 each in the share capital of the Company at the price of HK$1.23 per share. On 29 April 2002, the Agreements were completed and the Company raised approximately HK$119 million by way of issuing 100,000,000 new shares through this top-up placement.

(b) At 31 March 2003, the Company had an aggregate of 57,600,000 share options outstanding granted under the Pre-IPO Share Option Plan (the "Plan") and the Share Option Scheme (the "Scheme"), details of which are set out in note 21 to the accounts.

Notes to the Accounts

For the year ended 31 March 2003

21 Share option scheme

The Company has adopted a Pre-IPO Share Option Plan (the "Plan") and a Share Option Scheme (the "Scheme") on 19 July 2000 for the purpose of providing incentives and rewards to eligible participants who contribute to the success of the Group's operations. Under the terms of the Plan and the Scheme, the Board of Directors of the Company (the "Board") may, at their discretion, invite any employees including executive directors of the Company and/or any of its subsidiaries to subscribe for ordinary shares of HK$0.1 each in the Company. The maximum number of shares in respect of which options may be granted under the Plan and the Scheme may not exceed 30% of the issued share capital of the Company.

For the Scheme, the subscription price will be determined by the Board, save for the following: (1) in respect of any option granted prior to the listing of the shares of the Company on GEM, such price will be the issue price of the listing; and (2) for all other option granted upon listing of the shares of the Company on GEM, such price will not be less than the highest of (i) the nominal value of the shares, (ii) the closing price of the shares on the date of grant of the options, and (iii) the average closing price of the shares for the five business days immediately preceding the date of grant of the options. With effect from 1 October 2001 with the amendments to the Rules Governing the Listing of Securities on the GEM of the Stock Exchange (the "GEM Listing Rules") in share option scheme, the total number of shares issued and to be issued upon exercise of the options granted to each grantee (including both exercised and outstanding options) in any 12-month period up to the date of grant shall not exceed 1% of the shares in issue at the date of grant.

The Scheme is valid and effective for a period of ten years from 19 July 2000. Any options granted under the Scheme may be exercised at any time during a period to be notified by the Board to each grantee, such period of time shall not be less than three years from the date on which the option is granted in accordance with the terms of the Scheme and not more than ten years from the date of grant of the option or the date falling on the expiry of the Scheme, whichever date is later. Upon acceptance of the option, the grantee shall pay HK$1.00 to the Company by way of consideration for the grant.

For the Plan, the principal terms are substantially the same as the terms of the Scheme as set out above except that: (a) the subscription price for the shares granted under the Plan is the issue price of the listing; (b) the total number of shares subject to the Plan is 28,800,000; (c) the grantee can be non-executive directors and employees of the Company and its subsidiaries who are not in full time employment of the Group and consultants and advisors of the Group; and (d) the Plan was terminated on 4 August 2000, being the day immediate prior to the day when bulk printing of the Company's prospectus took place.

On 20 July 2000, options to subscribe for an aggregate of 64,800,000 shares at an exercise price HK$1.18 have conditionally been granted by the Company under the Plan and the Scheme. The Options granted under the Scheme are exercisable at any time within 3 years from 16 August 2000 while options granted under the Plan are exercisable at any time within 3 years after the expiry of 6 months from 16 August 2000. Each of these shall lapse in accordance with the Plan and the Scheme if the relevant grantee ceases to be employed by the Group. All options under the Plan and the Scheme have been granted to each grantee in consideration for the payment of HK$1.00.

Notes to the Accounts

For the year ended 31 March 2003

21 Share option scheme (Continued)

Details of the share options outstanding as at 31 March 2003 which have been granted under the Scheme are as follows:

	Number of share options		
Name or category of participants	**Outstanding at 1 April 2002**	**Lapsed during the year**	**Outstanding at 31 March 2003**
Director:			
Mr. Mak Kam Wah (resigned on 13 August 2003)	3,600,000	—	3,600,000
Senior management *(note)*	32,400,000	(7,200,000)	25,200,000
Total	36,000,000	(7,200,000)	28,800,000

Note: Options to subscribe for 7,200,000 shares lapsed during the year as certain grantees have ceased to be employees of the Group.

Details of the share options outstanding as at 31 March 2003 which have been granted under the Plan are as follows:

Name and category of participants	**Number of share options outstanding at 1 April 2002 and 31 March 2003**
Directors:	
Mr. Chu Ho Hwa, Howard (resigned on 15 May 2003)	3,600,000
Mr. Wang Wei Hung (resigned on 30 April 2003)	3,600,000
	7,200,000
Consultants	21,600,000
Total	28,800,000

No options granted under the Plan have been exercised, cancelled, waived or lapsed since its adoption and up to 31 March 2003.

Notes to the Accounts

For the year ended 31 March 2003

22 Reserves

(a) Group

	Share premium HK$'000	Merger reserve HK$'000	Exchange reserve HK$'000	Retained earnings/ (accumulated losses) HK$'000	Total HK$'000
At 1 April 2001	84,737	20,943	(99)	128,001	233,582
Profit attributable to shareholders	—	—	—	67,612	67,612
Dividends:					
Special interim dividend in specie of shares in a subsidiary	(10,495)	—	—	—	(10,495)
2001 Final dividend *(note 8)*	—	—	—	(10,800)	(10,800)
2002 Interim dividends *(note 8)*	—	—	—	(14,400)	(14,400)
Exchange differences arising on translation of accounts of overseas subsidiaries	—	—	(23)	—	(23)
At 31 March 2002	74,242	20,943	(122)	170,413	265,476
At 1 April 2002	74,242	20,943	(122)	170,413	265,476
Issue of new shares	113,000	—	—	—	113,000
Share issue expenses	(3,855)	—	—	—	(3,855)
Loss attributable to shareholders	—	—	—	(421,107)	(421,107)
Dividends:					
2002 Final dividend *(note 8)*	—	—	—	(8,200)	(8,200)
2003 Interim dividends *(note 8)*	—	—	—	(8,610)	(8,610)
Exchange differences arising on translation of accounts of overseas subsidiaries	—	—	(108)	—	(108)
At 31 March 2003	183,387	20,943	(230)	(267,504)	(63,404)

The merger reserve of the Group represents the difference between the nominal value of the shares of the subsidiaries acquired pursuant to the group reorganisation took place in 2001 and the nominal value of the Company's shares issued in exchange thereof.

Notes to the Accounts

For the year ended 31 March 2003

22 Reserves (Continued)

(b) Company

	Share premium (note (i)) HK$'000	Retained earnings/ (accumulated losses) HK$'000	Total HK$'000
At 1 April 2001	84,737	446	85,183
Profit for the year	—	31,819	31,819
Dividends:			
Special interim dividend in specie of shares in a subsidiary	(10,495)	—	(10,495)
2001 Final dividend *(note 8)*	—	(10,800)	(10,800)
2002 Interim dividends *(note 8)*	—	(14,400)	(14,400)
At 31 March 2002	74,242	7,065	81,307
At 1 April 2002	74,242	7,065	81,307
Issue of new shares	113,000	—	113,000
Share issuing expenses	(3,855)	—	(3,855)
Loss for the year	—	(232,694)	(232,694)
Dividends:			
2002 Final dividend *(note 8)*	—	(8,200)	(8,200)
2003 Interim dividends *(note 8)*	—	(8,610)	(8,610)
At 31 March 2003	183,387	(242,439)	(59,052)

(i) Under section 34 of the Companies Law (2003 Revision) of the Cayman Islands, the share premium is available for distribution to shareholders subject to the provisions of the Articles of Association of the Company and no distribution may be paid to shareholders out of the share premium unless, immediately following the date on which the distribution of dividend is proposed to be paid, the Company shall be able to pay its debts as they fall due in the ordinary course of business.

(ii) As at 31 March 2003, the Company had no reserve available for distribution.

Notes to the Accounts

For the year ended 31 March 2003

23 Long-term liabilities

	Group	
	2003	2002
	HK$'000	HK$'000
Bank loans	**21,505**	27,932
Obligations under finance leases	**309**	663
	21,814	28,595
Current portion of long-term liabilities	**(21,814)**	(7,607)
	—	20,988

At 31 March 2003, the Group's bank loans were repayable as follows:

	2003	2002
	HK$'000	HK$'000
Within one year	**21,505**	7,226
In the second year	**—**	13,881
In the third to fifth year	**—**	6,825
	21,505	27,932

At 31 March 2003, the Group's finance lease liabilities were repayable as follows:

	2003	2002
	HK$'000	HK$'000
Within one year	**362**	457
In the second year	**—**	277
In the third to fifth year	**—**	52
	362	786
Future finance charges on finance leases	**(53)**	(123)
Present value of finance lease liabilities	**309**	663

The present value of finance lease liabilities is as follows:

Within one year	**309**	381
In the second year	**—**	233
In the third to fifth year	**—**	49
	309	663

Notes to the Accounts

For the year ended 31 March 2003

24 Deferred taxation

	Group	
	2003	2002
	HK$'000	HK$'000
At beginning of year	**8,743**	4,687
Transfer (to)/from profit and loss account *(note 6)*	**(8,743)**	4,056
At end of year	**—**	8,743
Timing difference in respect of		
- Accelerated depreciation allowances	**11,961**	12,309
- Unutilised tax losses	**(11,961)**	(3,566)
	—	8,743

As at 31 March 2003, the Group had unrecognised deferred tax asset of HK$33,142,000 which represents the tax effect of timing differences arising as a result of tax losses available to set off against future assessable profits. This deferred tax asset has not been recognised in the accounts as it is not certain that the benefit will be realised in the foreseeable future. The Group had no material deferred tax asset as at 31 March 2002.

The Group had no material unprovided deferred tax liability as at 31 March 2003 and 2002.

Notes to the Accounts

For the year ended 31 March 2003

25 Notes to consolidated cash flow statement

(a) Reconciliation of (loss)/profit before taxation to cash used in operations

	Group	
	2003	2002
	HK$'000	HK$'000
(Loss)/profit before taxation	**(439,181)**	81,032
Adjustments for:		
Interest income	**(1,054)**	(448)
Interest on bank loans and overdrafts	**7,174**	3,839
Interest element of finance leases	**68**	75
Depreciation of owned fixed assets	**29,457**	13,712
Depreciation of fixed assets held under finance leases	**379**	379
Gain on deemed disposal of interests in a subsidiary	**—**	(7,242)
Share in a subsidiary issued to staff as part of the group reconstruction	**—**	5,592
Provision for bad and doubtful debts	**349,224**	—
Provision for other receivable	**2,000**	—
Write off and write down on value of inventories	**18,897**	—
Provision for inventories	**85,765**	—
Loss on disposal of fixed assets	**857**	—
Gain on disposal of subsidiaries	**(398)**	—
Deficit arising from revaluation of property	**263**	73
Operating profit before working capital changes	**53,451**	97,012
Increase in inventories	**(182,182)**	(9,580)
Increase in trade receivables, deposits, prepayments and other receivables	**(173,268)**	(118,092)
Increase/(decrease) in trade payables, other payables and accruals, including amount due to a director	**107,617**	(2,957)
Cash used in operations	**(194,382)**	(33,617)

Notes to the Accounts

For the year ended 31 March 2003

25 Notes to consolidated cash flow statement (Continued)

(b) Disposal of subsidiaries

	2003 HK$'000	2002 HK$'000
Net liabilities disposed of:		
Fixed assets	114	—
Deposits and prepayments	1,478	—
Other receivable	164	—
Cash and bank balances	37	—
Other payables and accruals	(1,813)	—
	(20)	—
Gain on disposal	398	—
Consideration	378	—
Satisfied by:		
Cash consideration received	378	—

The analysis of the net inflow of cash and cash equivalents in respect of the disposal of subsidiaries is as follows:

	2003 HK$'000	2002 HK$'000
Cash consideration received	378	—
Cash and bank balances disposed of	(37)	—
Net inflow of cash and cash equivalents	341	—

(c) Major non-cash transactions

	2003 HK$'000	2002 HK$'000
Special interim dividend in specie of shares in a subsidiary *(note 8)*	—	10,495
Shares in a subsidiary issued to staff as part of the group reconstruction	—	5,592

During the year, the Group was granted by the Chinese University of Hong Kong (the "University") an exclusive license to use the software with the right to grant sub-licenses to develop, manufacture, use and sell or supply projects developed by using the software for a term of 20 years at a consideration of HK$2,300,000. The acquisition of such exclusive license was included in the addition of fixed assets for the year. Among the consideration, HK$600,000 had been paid by cash and the balance of HK$1,700,000 (the "Balance") was included in other payables in the consolidated balance sheet as at 31 March 2003. Subsequent to the balance sheet date, the Balance was settled by the issue and allotment of 14,916,000 consideration shares of Satellite Devices Corporation, a company with 67.34% equity interest held by the Group, at HK$0.114 to the University.

Notes to the Accounts

For the year ended 31 March 2003

26 Operating lease commitments

(a) The Group as lessee

Rental payments paid by the Group under operating leases in respect of land and buildings during the year amounted to HK$4,335,000 (2002: HK$2,110,000).

As at 31 March 2003, the Group had future aggregate minimum lease payments under non-cancellable operating leases in respect of land and buildings falling due as follows:

	Group	
	2003	2002
	HK$'000	HK$'000
Within one year	**2,873**	1,884
In the second to fifth years inclusive	**2,001**	1,043
	4,874	2,927

The operating lease payments represent rentals payable by the Group for its office premises in Hong Kong and the Mainland China. Leases are negotiated and rentals are fixed for a period of one to three years.

(b) The Group as lessor

Rental income earned by the Group under an operating lease in respect of its investment property during the year amounted to HK$74,000 (2002: nil).

As at 31 March 2003, the Group had minimum lease receipts in respect of rentals receivable by the Group for its investment property under a non-cancellable operating lease which falls due as follows:

	Group	
	2003	2002
	HK$'000	HK$'000
Within one year	**177**	—
In the second to fifth years inclusive	**88**	—
	265	—

Notes to the Accounts

For the year ended 31 March 2003

27 Capital commitments

As at 31 March 2003, the Group had capital commitments in respect of acquisition of fixed assets:

	Group	
	2003	2002
	HK$'000	HK$'000
Contracted but not provided for	**540**	877
Authorised but not contracted for	**3,000**	28,106
	3,540	28,983

In addition, as at 31 March 2003, the Group had unprovided capital commitments amounting to HK$1,837,000 in respect of the investment in a subsidiary, Satellite Devices Technology (Shenzhen) Company Limited, being the balance of the required capital contribution to this subsidiary by the Group as at that date.

28 Subsequent events

(a) As mentioned in note 25(c), the balance of HK$1,700,000 for the purchase of the software license was subsequently settled by the issue and allotment of 14,916,000 consideration shares of Satellite Devices Corporation at HK$0.114 to the University on 17 April 2003.

(b) On 16 July 2003, one of the Group's bank creditors, The Hongkong and Shanghai Banking Corporation Limited ("HSBC"), filed a winding up petition against each of the Company and Arcon Technology Limited ("ATL"), a wholly-owned subsidiary of the Company, in respect of sums owing by ATL to HSBC under the banking facilities granted by HSBC to ATL. The Company has given corporate guarantee in favour of HSBC whereby the Company guaranteed all of ATL's indebtedness under the above banking facilities. The Company has engaged its legal advisor to advise on the petition and prepare its defence.

(c) On 2 May 2003, Arcon Solutions (BVI) Limited, a wholly-owned subsidiary of the Company, and Hang Seng Bank Limited ("Hang Seng Bank") entered into an agreement of charge over shares by which an aggregate number of 160,000,000 shares in Satellite Devices Corporation held by the Group were pledged to Hang Seng Bank as security for the repayment of the outstanding sums due by ATL to Hang Seng Bank. As at 22 June 2003, such outstanding sums amounted to approximately HK$39,636,000.

(d) Subsequent to the year end date, fixed assets of the Group with an aggregate carrying amount of approximately HK$2,059,000 have been disposed of and written off upon the removal of the Group's offices in Hong Kong and the Mainland China.

29 Contingent liabilities

The Company has issued corporate guarantees to banks in respect of banking facilities granted to a subsidiary. As at 31 March 2003, such facilities utilised by the subsidiary amounted to approximately HK$186,275,000.

30 Ultimate holding company

The directors regard Upgrade Technology Limited, a company incorporated in the British Virgin Islands, as being the ultimate holding company.

Notes to the Accounts

For the year ended 31 March 2003

31 Comparative figures

Due to the adoption of new/revised SSAPs during current year, the presentation of accounts and certain notes to accounts have been revised to comply with the new requirements. Accordingly, certain comparative figures have been reclassified to conform with current year's presentation.

32 Approval of accounts

The accounts were approved by the board of directors on 20 November 2003.

Financial Summary

	2003 HK$'000	2002 HK$'000	2001 HK$'000	2000 HK$'000	1999 HK$'000
Results					
(Loss)/profit attributable to shareholders	(421,107)	67,612	101,491	24,377	5,799
Assets and liabilities					
Total assets	350,607	543,979	359,764	135,562	72,331
Total liabilities	(309,897)	(175,055)	(54,182)	(80,852)	(55,997)
Minority interests	(22,114)	(31,448)	—	—	—
Shareholders' funds	18,596	337,476	305,582	54,710	16,334

Note:

The results, assets and liabilities of the Group for three years ended 31 March 2001 have been prepared on a combined basis as if the group structure, at the time when the Company's shares were listed on the GEM, had been in existence throughout the years concerned.