



2003-2004

First Quarterly 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 future 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 at www.hkgem.com in order to obtain up-to-date information on GEM-listed issuers.

The Stock Exchange takes no responsibility for the contents of this report, makes no representation as to its accuracy or completeness and expressly disclaims any liability whatsoever for any loss howsoever arising from or in reliance upon the whole or any part of the contents of this report.

This report, for which the directors of Arcotech Corporation collectively and individually accept responsibility, includes particulars given in compliance with the Rules Governing the Listing of Securities on the Growth Enterprise Market of the Stock Exchange for the purpose of giving information with regard to Arcotech Corporation. The directors, having made all reasonable enquiries, confirm that, to the best of their knowledge and belief:- (1) the information contained in this report is accurate and complete in all material respects and not misleading; (2) there are no other matters the omission of which would make any statement in this report misleading; and (3) all opinions expressed in this report have been arrived at after due and careful consideration and are founded on bases and assumptions that are fair and reasonable.

FIRST QUARTER RESULTS (UNAUDITED)

The Board of Directors (the “Board”) of Arcontech Corporation (the “Company”) is pleased to announce the unaudited condensed consolidated results of the Company and its subsidiaries (collectively the “Group”) for the three months ended 30 June 2003, together with the comparative unaudited figures for the corresponding period in 2002 (the “Relevant Periods”) as follows:

	<i>Note</i>	Three months ended	
		30 June	
		2003	2002
		<i>HK\$'000</i>	<i>HK\$'000</i>
Turnover	2	58,207	119,145
Cost of sales		<u>(52,694)</u>	<u>(86,105)</u>
Gross profit		5,513	33,040
Other revenues	2	57	229
Selling and distribution expenses		(248)	(1,990)
General and administrative expenses		(12,573)	(11,580)
Depreciation		(7,483)	(5,166)
Loss on deemed disposal of Subsidiary		<u>(20)</u>	<u>—</u>
Operating (loss)/profit		(14,754)	14,533
Finance costs	3	<u>(2,472)</u>	<u>(1,461)</u>
(Loss)/profit before taxation		(17,226)	13,072
Taxation	4	<u>—</u>	<u>(2,220)</u>
(Loss)/profit after taxation		(17,226)	10,852
Minority interests		<u>1,567</u>	<u>(847)</u>
(Loss)/profit attributable to shareholders		<u>(15,659)</u>	<u>10,005</u>
Interim dividend per share		<u>nil</u>	<u>0.35 cent</u>
(Loss)/earnings per share - basic	5	<u>(1.91) cents</u>	<u>1.27 cents</u>

Notes to condensed accounts:

1. Basis of presentation and accounting policies

These unaudited consolidated condensed accounts are prepared in accordance with Hong Kong Statement of Standard Accounting Practice ("SSAP") 25, Interim Financial Reporting, issued by the Hong Kong Society of Accountants ("HKSA").

In the current period, the Group has adopted, for the first time, the new and revised Statement of Standard Accounting Practice ("SSAP") 12 "Income Taxes" issued by the HKSA which is effective for accounting periods commencing on or after 1 January 2003. The adoption of the above new and revised SSAP has no material impact on the accounts of the company for the current and prior accounting periods. Accordingly, no prior period adjustment is required.

2. Turnover and revenue

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

	Three months ended	
	30 June	
	2003	2002
	<i>HK\$'000</i>	<i>HK\$'000</i>
Turnover		
Sales of goods at invoiced value, net of returns and discounts	58,207	112,140
Royalty income	—	7,005
	<hr/>	<hr/>
	58,207	119,145
	<hr/>	<hr/>
Other revenues		
Interest income	2	177
Rental income	44	—
Sundry income	11	—
Software and internet service income	—	52
	<hr/>	<hr/>
	57	229
	<hr/>	<hr/>
Total revenues	<u>58,264</u>	<u>119,374</u>

Segment information

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

	Sales of software and engineering solutions	Sales of software and engineering solutions	Sales of GPS For the three months ended 30 June 2003 HK\$'000	Sales of GPS For the three months ended 30 June 2002 HK\$'000	Group For the three months ended 30 June 2003 HK\$'000	Group For the three months ended 30 June 2002 HK\$'000
Turnover	44,459	97,051	13,748	22,094	58,207	119,145
Segment results	(10,151)	11,439	(4,603)	3,094	(14,754)	14,533
Finance costs					(2,472)	(1,461)
(Loss)/profit before taxation					(17,226)	13,072
Taxation					—	(2,220)
(Loss)/profit after taxation					(17,226)	10,852
Minority interests					1,567	(847)
(Loss)/profit attributable to shareholders					(15,659)	10,005

3. Finance costs

	Three months ended 30 June	
	2003 HK\$'000	2002 HK\$'000
Interest on bank loans and overdrafts	2,453	1,442
Interest element of finance leases	19	19
	<u>2,472</u>	<u>1,461</u>

4. **Taxation**

No provision for Hong Kong profits tax has been made as the Group has no assessable profits for the period ended 30 June 2003 (2002: 16%).

Taxation on profits of subsidiaries in the Mainland China has been calculated on the estimated assessable profits for the periods at the rates of taxation prevailing in the Mainland China.

5. **(Loss)/earnings per share**

The calculation of basic (loss)/earnings per share for the three months ended 30 June 2003 is based on the Group's loss attributable to shareholders of approximately HK\$15,659,000 (2002: profit of HK\$10,005,000) and weighted average number of 820,000,000 ordinary shares (2002: 789,230,769 ordinary shares) in issue during the period.

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

6. **Movement of reserves**

	Share premium <i>HK\$'000</i>	Merger reserve <i>HK\$'000</i>	Exchange reserve <i>HK\$'000</i>	Retained earnings <i>HK\$'000</i>	Total <i>HK\$'000</i>
At 1 April 2002	74,242	20,943	(122)	170,413	265,476
Issue of shares					
pursuant to placing	113,000	—	—	—	113,000
Share issuing expenses	(3,855)	—	—	—	(3,855)
Profit attributable to shareholders	—	—	—	10,005	10,005
Exchange differences	—	—	(28)	—	(28)
	<u> </u>	<u> </u>	<u> </u>	<u> </u>	<u> </u>
At 30 June 2002	<u>183,387</u>	<u>20,943</u>	<u>(150)</u>	<u>180,418</u>	<u>384,598</u>
At 1 April 2003	183,387	20,943	(230)	(267,504)	(63,404)
Loss attributable to shareholders	—	—	—	(15,659)	(15,659)
Exchange differences	—	—	(2)	—	(2)
	<u> </u>	<u> </u>	<u> </u>	<u> </u>	<u> </u>
At 30 June 2003	<u>183,387</u>	<u>20,943</u>	<u>(232)</u>	<u>(283,163)</u>	<u>(79,065)</u>

INTERIM DIVIDENDS

The Board does not recommend the payment of interim dividend for the three months ended 30 June 2003 (2002: HK0.35 cent).

MANAGEMENT DISCUSSION AND ANALYSIS

Financial Performance

For the three-month period ended 30 June 2003, the Group continued to operate under increasingly difficult market conditions and in particular the attack of SARS severely affected the confidence of overseas customers on the ability of suppliers in Asia such as the Group to meet orders on a timely basis. During the period under review, the Group's unaudited consolidated turnover and loss attributable to shareholders are HK\$58.2 million (2002: HK\$119.1 million) and HK\$15.7 million and (2002: profit of HK\$10.0 million) respectively. There is a 51.1 % decrease in turnover with a 256.5 % decline in profit attributable to shareholders over the corresponding period last year.

The decrease in turnover and the loss attributable to shareholders was mainly attributable to the severe decline in orders due to the attack of SARS and the continuous shifting of the product mix of the solutions towards the fast-moving consumer electronics and audio/visual products.

Gross profit was 9.5 % for the three months period under review. The decline in gross profit is mainly caused by the keen competition in the global 3C products market and the relatively lower profit margin for our audio/visual product solutions shipped during the period under review.

General and administrative expenses decreased because of the adoption of the new operation plan, which streamlined the operations and efficiently allocated resources.

Business Review

During the period under review, the Group faced severe challenges. These challenges included weak global economies, continuous weakening consumer spending in high-end 3C products and in particular, increasingly fierce competition in the 3C products industry and the dominance of low-end and/or basic functionalities products, and most significantly, the effects of SARS.

Combinations of these factors negatively impacted the financial performance of the Group for the period under review. The effects of SARS caused unexpected severe limitations on the business of the Group and affected the Group on all its product lines in terms of decline in sales. During the period under review the Group adopted rigorous cost control policies in managing its operations.

The management also realigned the organizational structure of the Group and adopted a new operational plan, which streamlined the operation and increased the operational efficiency.

PROSPECTS

With the local production capacity recovering from the after effects of SARS and the more positive outlook towards the global economy, the Group's products are in demand by the industry.

The Group will continue to strengthen its marketing network and tighten its control on operating costs and plans to adopt product strategies to take advantage of the positive market sentiment.

DIRECTORS' INTEREST IN SHARES AND OPTIONS

As at 30 June 2003, the interests and short position of the directors of the Company in the shares, underlying shares and debentures of the Company or any of its associated corporation (within the meaning of Part XV of the Securities and Futures Ordinance (Cap. 571, Laws of Hong Kong) ("SFO")) which were required to be notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests or short positions which they were taken or deemed to have under such provisions of the SFO) or as recorded in the register required to be kept by the Company under Section 352 of the SFO or otherwise notified to the Company and the Stock Exchange pursuant to the minimum standards of dealings by directors as referred to in Rules 5.04 to 5.58 of the GEM Listing Rules were as follows:

A. Ordinary shares of HK\$0.10 each of the company

Name	Type of interest	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 were as follows:

Name	Personal Interests	Corporate Interests	Total Interests
Mr. Tsoi Siu Ching, Leo	10,250,000	5,000,000	15,250,000
	Deferred Shares (Note 3)	Deferred Shares (Note 2 and 3)	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	387,888,000
	Ordinary Shares (Note 4)	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 reorganization" in the prospectus of the Company 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, none of the Directors or their associates had any interests in the share capital of the Company or its associated corporations as defined in the SDI Ordinance.

B. Share options

The Company has adopted a Pre-IPO Share Option Plan (the “Plan”) and a Share Option Scheme (the “Scheme”) on 19 July 2000. Options to subscribe for an aggregate of 64,800,000 Shares at an exercise price of HK\$1.18 have conditionally been granted by the Company on 20 July 2000 under the Plan & Scheme. 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 & Scheme if the relevant grantee ceases to be employed by the Group.

As at 30 June 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 on 20 September 2002 and 2 December 2002 as certain grantees have ceased to be employees of the Group. All options under the Plan & 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, the senior managers and certain employees of the Group are set out below:

Name	Pre-IPO Share Option Plan Number of underlying shares	Share Option Scheme
<i>Director:</i>		
Mr. Mak Kam Wah	—	3,600,000
<i>Ex-directors:</i>		
Mr. Chu Ho Hwa, Howard	3,600,000	—
Mr. Wang Wei Hung	3,600,000	—
<i>Senior Management:</i>		
The estate of late Mr. Tien Chang Lin	14,400,000	—
Mr. Cheng Lee Lung	7,200,000	—
Ms. Ho Kwan Yin	—	14,400,000
Mr. Ching Man Leuk	—	3,600,000
Mr. Lee Lai Shing	—	3,600,000
Mr. Tong Ka Ming, Patrick	3,600,000	—

SUBSTANTIAL SHAREHOLDERS

As at 30 June 2003, the interests and short positions or persons, other than a director of the Company, in the shares and underlying shares of the Company which would fall to be disclosed to the Company under the provisions of Divisions 2 and 3 of Part XV of the SFO or, who is, directly or indirectly, interested in 10% or more of the nominal value of any class of share capital carrying rights to vote in all circumstances at general meetings of any other members of the Group, or substantial shareholders as recorded in the register required to be kept by the Company under Section 336 of the SFO were as follows:

As at 30 June 2003, according to the register of substantial shareholders maintained under section 16(1) of the SDI Ordinance, the following person is interested in 10% or more of the Company's issued share capital:

Name	Number of shares	Percentage of issued share capital
Upgrade Technology Limited (<i>Note 1</i>)	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.

COMPETING INTERESTS

None of the Directors or the management shareholders of the Company (as defined in the GEM Listing Rules) has an interest in a business which competes or may compete with the business of the Group.

PURCHASE, SALE OR REDEMPTION OF LISTED SECURITIES

During the three months ended 30 June 2003, neither the Company nor any of its subsidiaries purchased, sold or redeemed any of the Company's listed securities.

AUDIT COMMITTEE

The Company has established an audit committee with written terms of reference in compliance with Rules 5.23 to 5.25 of the GEM Listing Rules. The primary duties of the audit committee are to review and supervise the financial reporting process and internal control of the Group.

By Order of the Board

Tsoi Siu Ching, Leo

Chairman

Hong Kong, 31 December 2003