



2003-2004

Third 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.

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This report, for which the directors of Arcontech 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 Arcontech 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.

THIRD 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 nine months and three months ended 31 December 2003, together with the comparative unaudited figures for the corresponding periods in 2002 (the “Relevant Periods”) as follows:

		Nine months ended 31 December		Three months ended 31 December	
		2003	2002	2003	2002
	Note	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Turnover	2	100,810	567,914	20,237	179,441
Cost of sales		(66,279)	(458,527)	(849)	(146,665)
Gross profit		34,531	109,387	19,388	32,776
Other revenues	2	260	636	117	196
Selling and distribution expenses		(3,093)	(7,631)	(2,614)	(1,707)
General and administrative expenses		(21,220)	(39,489)	(2,995)	(13,077)
Depreciation		(22,200)	(15,379)	(11,867)	(5,021)
Loss on deemed disposal of interest in a subsidiary		(20)	–	–	–
Disposal of fixed assets		(1,766)	(821)	–	(821)
Operating (loss)/profit	3	(13,508)	46,703	2,029	12,346
Finance costs	5	(7,040)	(4,934)	(2,510)	(2,122)
(Loss)/profit before taxation		(20,548)	41,769	(481)	10,224
Taxation	6	–	(8,000)	–	(2,190)
(Loss)/profit after taxation		(20,548)	33,769	(481)	8,034
Minority interests		4,903	(21)	1,498	842
(Loss)/profit attributable to shareholders		(15,645)	33,748	1,017	8,876
Interim dividend per share		<u>nil</u>	<u>1.05 cents</u>	<u>nil</u>	<u>0.20 cent</u>
(Loss)/earnings per share – basic	7	<u>(1.91) cents</u>	<u>4.17 cents</u>	<u>0.12 cent</u>	<u>1.08 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 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 the location-based technology devices and applications (“GPS”) in Hong Kong. Revenues recognised during the Relevant Periods are as follows:

	Nine months ended 31 December		Three months ended 31 December	
	2003	2002	2003	2002
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Turnover				
Sales of goods at invoiced value, net of returns and discounts	100,810	553,926	20,237	174,489
Royalty income	–	13,988	–	4,952
	<u>100,810</u>	<u>567,914</u>	<u>20,237</u>	<u>179,441</u>
Other revenues				
Interest income	2	479	–	112
Operating lease rental income from investment property	133	–	36	–
Software and internet service income	–	157	–	84
Sundry income	125	–	81	–
	<u>260</u>	<u>636</u>	<u>117</u>	<u>196</u>
Total revenues	<u>101,070</u>	<u>568,550</u>	<u>20,354</u>	<u>179,637</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 excluding GPS	Sales of software and engineering solutions excluding GPS	Sales of GPS	Sales of GPS	Group	Group
	For the nine months ended 31 December 2003 HK\$'000	For the nine months ended 31 December 2002 HK\$'000	For the nine months ended 31 December 2003 HK\$'000	For the nine months ended 31 December 2002 HK\$'000	For the nine months ended 31 December 2003 HK\$'000	For the nine months ended 31 December 2002 HK\$'000
Turnover	<u>86,153</u>	<u>510,779</u>	<u>14,657</u>	<u>57,135</u>	<u>100,810</u>	<u>567,914</u>
Segment results	<u>803</u>	<u>46,660</u>	<u>(14,311)</u>	<u>43</u>	(13,508)	46,703
Finance costs					(7,040)	(4,934)
(Loss)/profit before taxation					(20,548)	41,769
Taxation					–	(8,000)
(Loss)/profit after taxation					(20,548)	33,769
Minority interests					4,903	(21)
(Loss)/profit attributable to shareholders					<u>(15,645)</u>	<u>33,748</u>

3. Operating (loss)/profit

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

	For the nine months ended 31 December 2003 HK\$'000	For the nine months ended 31 December 2002 HK\$'000
Depreciation:		
Owned fixed assets	21,915	15,094
Leased fixed assets	285	285
Loss on disposal of fixed assets	1,766	821
	<u>23,966</u>	<u>16,200</u>

4. Staff costs

	For the nine months ended 31 December 2003 HK\$'000	For the nine months ended 31 December 2002 HK\$'000
Basic salaries, allowances and other benefits in kind	11,403	22,302
Retirement scheme contributions	(11)	473
	<u>11,392</u>	<u>22,775</u>

5. Finance costs

	Nine months ended 31 December		Three months ended 31 December	
	2003 HK\$'000	2002 HK\$'000	2003 HK\$'000	2002 HK\$'000
Interest on bank loans and overdrafts	7,021	4,878	2,510	2,104
Interest element of finance leases	19	56	–	18
	<u>7,040</u>	<u>4,934</u>	<u>2,510</u>	<u>2,122</u>

6. Taxation

No provision for Hong Kong profits tax has been made as the Group has no assessable profit for the period ended 31 December 2003.

Hong Kong profits tax has been calculated at 16% on the estimated assessable profits of the Group for the nine months and three months ended 31 December 2002.

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.

7. (Loss)/earnings per share

The calculation of basic loss per share for the nine months ended 31 December 2003 is based on the Group's loss attributable to shareholders of approximately HK\$15,645,000 (2002: profit of HK\$33,748,000) and 820,000,000 ordinary shares (2002: 809,818,182 ordinary shares) in issue during the period.

The calculation of basic earnings per share for the three months ended 31 December 2003 is based on the Group's profit attributable to shareholders of approximately HK\$1,017,000 (2002: HK\$8,876,000) and 820,000,000 ordinary shares (2002: 820,000,000 ordinary shares) in issue during the period.

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

8. Movement of reserves

	Share premium <i>HK\$'000</i>	Merger reserve <i>HK\$'000</i>	Exchange reserve <i>HK\$'000</i>	Retained earnings/ losses) <i>HK\$'000</i>	Total <i>HK\$'000</i>
As at 1 April 2003	183,387	20,943	(230)	(267,504)	(63,404)
Loss for the period	–	–	–	(15,645)	(15,645)
Exchange differences	–	–	(2)	–	(2)
	<u>183,387</u>	<u>20,943</u>	<u>(232)</u>	<u>(283,149)</u>	<u>(79,051)</u>
As 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	–	–	–	33,748	33,748
2002 Final dividend	–	–	–	(8,200)	(8,200)
2003 Interim dividend	–	–	–	(6,970)	(6,970)
2003 Proposed interim dividend	–	–	–	(1,640)	(1,640)
Exchange differences	–	–	(119)	–	(119)
	<u>183,387</u>	<u>20,943</u>	<u>(241)</u>	<u>187,351</u>	<u>391,440</u>

INTERIM DIVIDENDS

The Board does not recommend the payment of interim dividend for the nine months ended 31 December 2003 (2002: HK0.20 cent).

MANAGEMENT DISCUSSION AND ANALYSIS

Financial Performance

For the nine months ended 31 December 2003, the Group has recorded a turnover of HK\$100.8 million and recorded a loss attributable to shareholders of HK\$15.6 million. This represents a decrease of 82.2% in sales turnover and a drop of profit attributable to shareholders from HK\$33.8 million to a loss of HK\$15.6 million as compared with those in the corresponding period last year. The loss per share for the nine months ended 31 December 2003 was HK\$1.91 cents.

Business Review

During the past nine months, the Group faced extreme challenges as one of the bank creditors of the Group commenced winding up proceedings against the Company and some of its customers. The operations of the Group was severely affected, and the Group faced difficulties in securing sales and supplies. The Group therefore during this period turned its attention on internal restructure on streamlining operation expense in order to address the extremely difficult operating environment. The Group has exercised stringent measures to reduce operating costs, and has been selective in its focus on products and customers so as to minimize requirements on cash flow. The Group's overall operating expenses has continued to decline as a result of such measures. During this period, the Group sold certain stock which were provided in previous periods and were therefore sold at a profit. Sale of those stock suggest that there is a shortage of supplies in the market but may not reflect the true operating environment in the market.

Financial Resources And Liquidity

As at 31 December 2003, the Group has total assets of HK\$266 million, which were mainly financed by current liabilities of HK\$244 million approximately and shareholders' funds amounting to HK\$3 million approximately.

Current assets amounted to HK\$206 million which mainly comprised of HK\$82 million accounts receivable and HK\$4 million cash and bank deposits. The Group had a working capital ratio of approximately 0.84. Fixed assets of the Group amounted to approximately HK\$60 million.

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.

The banking facilities of the group previously obtained were not available as at 31 December 2003 due to the winding up petition by a bank creditor.

Business Outlook

Given the positive signs of recovery of the global economy, the Group's products, particularly those used in consumer electronics industry continue to be in demand. The extreme measures taken by the Group in its internal restructure and cost control measures has given the Group a platform to take advantage of the recovery in the market.

During this period, the Group has commenced its research on Liquid Crystal on Silicon Technology ("LCOS") for application in plasma LCD-TFT display and other products. The Group intends to focus its research and development capabilities on LCOS related products in the coming period.

DIRECTORS' INTEREST IN SHARES AND OPTIONS

As at 31 December 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 of Director	Type of interest	Number of shares	Percentage of issued share capital
Mr. Tsoi Siu Ching, Leo	Corporate (<i>Note 1</i>)	472,384,000	57.61%

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 Deferred Shares (<i>Note 3</i>)	5,000,000 Deferred Shares (<i>Note 2 and 3</i>)	15,250,000 Deferred Shares (<i>Note 3</i>)

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 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 31 December 2003, no other options has been granted under the Scheme and none of the options has been exercised. However, options to subscribe for 28,800,000 shares have lapsed 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>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

SUBSTANTIAL SHAREHOLDERS

As at 31 December 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:

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.

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 December 2003.

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 nine months ended 31 December 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, 13 February 2004