

Perception Digital Holdings Limited

(a company incorporated in the Cayman Islands with limited liability)

Stock Code: 8248

First Quarterly Report 2010



CHARACTERISTICS OF THE GROWTH ENTERPRISE MARKET (“GEM”) OF THE STOCK EXCHANGE OF HONG KONG LIMITED (THE “STOCK EXCHANGE”)

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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 and no assurance is given that there will be a liquid market in the securities traded on GEM.

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This report, for which the directors (the “Directors”) of Perception Digital Holdings Limited (the “Company”) and its subsidiaries (together, the “Group”) collectively and individually accept full responsibility, includes particulars given in compliance with the Rules Governing the Listing of Securities on the GEM of the Stock Exchange (the “GEM Listing Rules”) for the purpose of giving information with regard to the Company. The Directors, having made all reasonable enquiries, confirm that, to the best of their knowledge and belief: (i) the information contained in this report is accurate and complete in all material respects and not misleading; (ii) there are no other matters the omission of which would make any statement in this report misleading; and (iii) 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.

HIGHLIGHTS

- The Group recorded a turnover of approximately HK\$71.4 million for the three months ended 31 March 2010 (2009: approximately HK\$47.4 million).
- Loss attributable to shareholders for the three months ended 31 March 2010 amounted to approximately HK\$2.5 million as compared to net loss of approximately HK\$3.2 million for the corresponding period in the previous fiscal year.
- The Directors do not recommend the payment of an interim dividend for the three months ended 31 March 2010.



First Quarterly Results (Unaudited)

The board of Directors (the "Board") is pleased to present the unaudited condensed consolidated results of the Group for the three months ended 31 March 2010 together with the comparative unaudited figures for the corresponding period in 2009, as follows:

Condensed Consolidated Income Statement & Notes

For the three months ended 31 March 2010

		Three months ended 31 March	
	Notes	2010 HK\$ (Unaudited)	2009 HK\$ (Unaudited)
REVENUE	3	71,421,678	47,433,897
Cost of sales		(58,953,402)	(38,294,942)
Gross profit		12,468,276	9,138,955
Other income		188,727	2,142
Research and development costs		(4,891,993)	(3,434,718)
Selling and distribution costs		(3,098,325)	(2,861,512)
General and administrative expenses		(6,844,641)	(7,200,162)
Other expenses, net		—	(30,612)
Finance costs	4	(551,738)	(1,042,855)
LOSS BEFORE TAX		(2,729,694)	(5,428,762)
Income tax credit	5	233,499	2,230,164
LOSS FOR THE PERIOD		(2,496,195)	(3,198,598)
Attributable to:			
Owners of the parent		(2,496,195)	(3,198,598)
LOSS PER SHARE ATTRIBUTABLE TO ORDINARY EQUITY HOLDERS OF THE PARENT			
Basic and diluted	6	HK(0.4) cents	HK(0.7) cents

Notes to the Unaudited Condensed Consolidated Quarterly Financial Statements

For the three months ended 31 March 2010

1.1 Corporate Information

The Company is a limited liability company incorporated in the Cayman Islands on 11 September 2009. The registered office of the Company is located at Cricket Square, Hutchins Drive, P.O. Box 2681, Grand Cayman, KY1-1111, Cayman Islands.

During the period, the Group was primarily involved in the research, design and development of digital signal processing ("DSP") platform and the provision of embedded firmware and "end-to-end" turnkey solutions to customers for their DSP-based consumer electronic devices.

1.2 Reorganisation and Basis of Preparation

Pursuant to a group reorganisation (the "Reorganisation") for the purpose of listing (the "Listing") the Company's ordinary shares on the Growth Enterprise Market of The Stock Exchange of Hong Kong Limited (the "Stock Exchange"), the Company was incorporated and interspersed between Perception Digital Technology (BVI) Ltd. ("Perception Digital BVI"), the direct/indirect holding company of all the other subsidiaries of the Group prior to the Reorganisation, and the equity holders of Perception Digital BVI and became the holding company of Perception Digital BVI and its subsidiaries. Further details of the Reorganisation are also set out in the section headed "Corporate Reorganisation" in Appendix VI "Statutory and General Information" to the prospectus of the Company dated 4 December 2009 (the "Prospectus") in connection with the Listing. The Company's shares have been listed on the Stock Exchange since 16 December 2009.

As the Reorganisation only involved inserting a new holding entity at the top of an existing group and has not resulted in any change of economic substances, the unaudited condensed consolidated first quarterly financial statements of the Group for the three months ended 31 March 2009 and have been presented as a continuation of the existing group using the pooling of interest method. Accordingly, the unaudited consolidated first quarterly income statement was prepared as if the current group structure had been in existence since 1 January 2009 rather than from the date of incorporation of the Company.



2. Basis of Preparation

The Group's unaudited condensed consolidated first quarter financial statements have been prepared in accordance with Hong Kong Financial Reporting Standards ("HKFRSs") (which include all Hong Kong Financial Reporting Standards, Hong Kong Accounting Standards ("HKASs") and Interpretations) issued by the Hong Kong Institute of Certified Public Accountants (the "HKICPA"), accounting principles generally accepted in Hong Kong and the disclosure requirements of the Hong Kong Companies Ordinance. The unaudited condensed consolidated first quarterly financial statements have been prepared under the historical cost convention and are presented in Hong Kong dollars. The accounting policies adopted in preparing the unaudited condensed consolidated first quarterly financial statements were consistent with those applied for the financial statements of the Group for the year ended 31 December 2009.

The results of subsidiaries are consolidated from the date of acquisition, being the date on which the Group obtains control, and continue to be consolidated until the date that such control ceases. All income, expenses and unrealised gains and losses resulting from intercompany transactions and intercompany balances within the Group are eliminated on consolidation in full.

3. Revenue and Operating Segment Information

Revenue, which is also the Group's turnover, represents the net invoiced value of goods sold, after allowances for returns and trade discounts; the value of services rendered; and the royalty income received and receivable during the period.

The following table sets out a breakdown of our revenue.

	Three months ended 31 March	
	2010 HK\$ (Unaudited)	2009 HK\$ (Unaudited)
Sales of products	59,058,478	42,793,994
Royalty income	2,066,748	3,764,693
Rendering of services	10,296,452	875,210
	71,421,678	47,433,897

Geographical Information

The following table presents revenue from external customers for the periods ended 31 March 2010 and 2009 by geographical areas.

	Europe HK\$ (Unaudited)	United States of America HK\$ (Unaudited)	Mainland China HK\$ (Unaudited)	Hong Kong HK\$ (Unaudited)	Others HK\$ (Unaudited)	Total HK\$ (Unaudited)
Three months ended						
31 March 2010						
Revenue from						
external customers	44,497,743	3,029,269	2,372,960	15,856,263	5,665,443	71,421,678
Three months ended						
31 March 2009						
Revenue from						
external customers	21,788,552	1,200,078	19,796,215	3,807,610	841,442	47,433,897

4. Finance Costs

	Three months ended	
	31 March	
	2010 HK\$ (Unaudited)	2009 HK\$ (Unaudited)
Interest on bank loans and overdrafts wholly repayable within five years	358,919	874,425
Bank charges	192,819	168,430
	551,738	1,042,855

5. Income Tax

Hong Kong profits tax has been provided for the current period at a rate of 16.5% on the estimated assessable profits arising in Hong Kong during the period. No provision for Hong Kong profits tax was made for the prior period as the Group had available tax losses brought forward from prior years to offset the assessable profits arising in Hong Kong generated during that period. Taxes on profits assessable elsewhere have been calculated at the rates of tax prevailing in the jurisdictions in which the Group operates.

	Three months ended 31 March	
	2010 HK\$ (Unaudited)	2009 HK\$ (Unaudited)
Current — Hong Kong:		
— Charge for the period	454,451	—
Current — Elsewhere:		
— Overprovision in prior years	—	(1,552,835)
Deferred	(687,950)	(677,329)
Total tax credit for the period	(233,499)	(2,230,164)

The Group's subsidiary established and operating in the Shenzhen Special Economic Zone of the People's Republic of China (the "PRC") is subject to the PRC's State Council Circular on the Implementation of the Transitional Concession Policies for Corporate Income Tax (Guo Fa [2007] No. 39), which provides that enterprises previously entitled to concession policies of tax rate reductions shall have a grace period of five years to comply with the requirements of the new statutory tax rate, commencing on 1 January 2008 after the implementation of the new tax law. Enterprises entitled to a 15% corporate income tax rate on or before 31 December 2007 will be subject to tax rates of 18%, 20%, 22%, 24% and 25% in 2008, 2009, 2010, 2011 and 2012, respectively. In addition, the Group's subsidiary established in the PRC had obtained the status of National High-Tech Enterprise in 2009 and, accordingly, is entitled to a lower PRC corporate income tax rate of 15%.

6. Loss Per Share Attributable to Ordinary Equity Holders of the Parent

The calculation of basic loss per share amounts is based on the loss for the period attributable to ordinary equity holders of the parent of HK\$2.5 million (2009: HK\$3.2 million), and the weighted average number of 612,833,333 ordinary shares in issue (2009: 450,000,000 ordinary shares). In determining the weighted average number of ordinary shares in issue, a total of 450,000,000 ordinary shares of the Company issued pursuant to the Reorganisation and a capitalisation issue were deemed to have been issued since 1 January 2009.

No adjustment has been made to the basic loss per share amounts presented for the three months ended 31 March 2010 and 2009 in respect of a dilution as the impact of the potential dilutive ordinary shares outstanding has an anti-dilutive effect on the basic loss per share amounts presented for the current period, and the Group had no potentially dilutive ordinary shares in issue during the prior period.

7. Dividend

The Directors do not recommend the payment of an interim dividend for the three months ended 31 March 2010.

8. Reserves

The movements of the Group's reserves during the period are as follow:

	Three months ended 31 March	
	2010 HK\$ (Unaudited)	2009 HK\$ (Unaudited)
At beginning of the period	22,252,901	(35,933,704)
Total comprehensive expenses	(2,518,978)	(3,197,957)
Issue of new shares in connection with the Over-Allotment Option	13,950,000	—
Share issue costs	(517,457)	—
Issue of share options	26,304	—
At end of the period	33,192,770	(39,131,661)

On 8 January 2010, the Company announced that the over-allotment option (the "Over-Allotment Option") referred to in the Prospectus was fully exercised in respect of an aggregate of 22,500,000 shares of the Company. The listing of and dealing in the said 22,500,000 shares commenced on the GEM of the Stock Exchange on 13 January 2010. The total number of the ordinary shares of the Group in issue was then increased from 600,000,000 shares to 622,500,000 shares.



Management Discussion and Analysis

Financial Review

During the three months ended 31 March 2010, the turnover of the Group amounted to HK\$71.4 million, representing an increase of 50.6% as compared to the corresponding period in 2009. The rise was mainly attributable to surges in both sales of products of 38.0% and service income of 1,076.5%. Our service income was mainly derived from providing project development and management, as well as marketing services. The increase in service income during the current period was mainly contributed by stepping up our sales efforts.

Research and development costs increased by 42.4% to HK\$4.9 million for the three months ended 31 March 2010 from HK\$3.4 million for the corresponding period in 2009. The increase was primarily due to the decrease in capitalisation of these costs as a result of fewer projects fulfilling our capitalisation criteria during the three months ended 31 March 2010.

Selling and distribution costs for the three months ended 31 March 2010 amounted to HK\$3.1 million, which is comparable to the amount incurred in the three months ended 31 March 2009.

General and administrative expenses experienced a slight decline by approximately HK\$0.4 million, or by 4.9%, to HK\$6.8 million for the three months ended 31 March 2010 from HK\$7.2 million for the corresponding period in 2009, primarily due to specific cost-saving measures implemented in mid 2009, including but not limited to reduction of legal and professional fees and rental expenses.

Finance costs declined by approximately HK\$0.5 million, or approximately 47.1%, to HK\$0.6 million for the period under review from HK\$1.1 million for the corresponding period in 2009. The decrease mainly resulted from the repayment of some of our bank loans in December 2009.

Despite the significant increase in research and development costs during the current period under review, the loss before tax of our Group for the current period significantly reduced by 49.7% from the HK\$5.4 million incurred in the corresponding period in 2009 to approximately HK\$2.7 million due to substantial increase in revenue, effective cost reduction measures and reduced finance costs.

Income tax credit for the three months ended 31 March 2009 amounted to HK\$2.2 million, which was significantly higher than the amount in the three months ended 31 March 2010. This was mainly attributable to an overprovision of income tax in relation to prior years, which amounted to HK\$1.6 million, being adjusted in the three months ended 31 March 2009.

Business Review

The turnover of the Group during the current period under review increased by approximately 50.6% to HK\$71.4 million, from HK\$47.4 million during the corresponding period in the last fiscal year.

Due to our unparalleled design supply chain solutions, some of our customers opted to engage our total solutions spanning from design, manufacturing and packaging, instead of solely licensing our technology during the current period under review. Therefore, our royalty income for the current period under review decreased by approximately 45.1% while sales of products increased by 38.0%. At the same time, the product mix in current period under review was different than the same period in the prior year. The overall gross profit margin decreased from 19.3% in the corresponding period in 2009 to 17.5%, as the royalty income from licensing our technology commanded relatively higher profit margin and with different product mix, but the negative effect was offset by increased revenue from sales of products.

In terms of our revenue breakdown, our revenue from sales of goods, royalty fees and income from rendering of services contributed approximately 82.7% (2009: 90.2%), 2.9% (2009: 8.0%) and 14.4% (2009: 1.8%), respectively. The majority of our products were shipped to Europe in the three months ended 31 March for the period under review and in 2009.



Outlook

During fiscal year 2010, we will continue to expand our strategic partnerships to co-develop new products and target wider market demand. We will also enhance our “Live-Lite” series of products by introducing additional features such as lower power consumption, enhanced G-sensor algorithm and GFS functions. Our new applications in the “Live-Lite” series, which cater for sports such as cycling, sporting, rowing and swimming, are expected to debut in the second quarter of 2010. In addition, our first Android-based mobile Internet device is also expected to be launched within the current year. Our strong research and development team, unique design and supply chain services, and our continuous effort to create innovative products reinforce our confidence that the Group is well positioned for future growth and good prospects in the years ahead.

Directors’ Interests and Short Positions in Shares and Underlying Shares

As at 31 March 2010, the interests and short positions of the Directors and chief executive of the Company in the ordinary shares (the “Shares”), underlying shares and debentures of the Company or its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance (the “SFO”)), as recorded in the register required to be kept by the Company pursuant to Section 352 of the SFO, or as otherwise notified to the Company and the Stock Exchange pursuant to Rule 5.46 of the GEM Listing Rules, were as follows:

Long position in the Shares:

Name of Director	Notes	Capacity/ Nature of interest	Number of Shares interested	Percentage of the Company's issued share capital
Dr. Lau, Jack ("Dr. Lau")	(a)	Interest of spouse	179,421,037	28.82%
Mr. Chui, Shing Yip Jeff ("Mr. Chui")	(b)	Interest in a controlled corporation	16,666,540	2.68%
Prof. Cheng, Shu Kwan Roger ("Prof. Cheng")	(c)	Interest in a controlled corporation	2,976,655	0.48%
Prof. Tsui Chi Ying ("Prof. Tsui")	(d)	Interest in a controlled corporation	11,903,210	1.91%
Dr. Wu, Po Him Philip ("Dr. Wu")		Beneficial owner	1,599,142	0.26%
			212,566,584	34.15%

Notes:

- (a) Of the 179,421,037 Shares, 53,828,697 Shares are held by Masteray Limited ("Masteray") and 125,592,340 Shares are held by Swanland Management Limited ("Swanland"). Dr. Lau is deemed to be interested in the Shares held by Masteray and Swanland by virtue of these two companies are being controlled by Ms. Loh, Jiah Yee Katherine ("Ms. Loh"), the spouse of Dr. Lau.
- (b) The 16,666,540 Shares are held by Glory Wood Limited ("Glory Wood"), which is wholly-owned by Mr. Chui. Hence, Mr. Chui is deemed to be interested in the Shares held by Glory Wood by virtue of Glory Wood being controlled by Mr. Chui.
- (c) The 2,976,655 Shares are held by Rochdale Consultancy Limited ("Rochdale"), which is owned as to 50% by Prof. Cheng. Hence, Prof. Cheng is deemed to be interested in the Shares held by Rochdale by virtue of Rochdale being controlled by Prof. Cheng.
- (d) The 11,903,210 Shares are held by Excel Direct Technology Limited ("Excel Direct"), which is owned as to 50% by Prof. Tsui. Hence, Prof. Tsui is deemed to be interested in the Shares held by Excel Direct by virtue of Excel Direct being controlled by Prof. Tsui.

Save as disclosed above, as at 31 March 2010, none of the Directors or chief executive of the Company or their respective associates had registered any interest or short position in the shares, underlying shares or debentures of the Company or any of its associated corporations that was required to be recorded pursuant to section 352 of the SFO, or as otherwise notified to the Company and the Stock Exchange pursuant to Rule 5.46 of the GEM Listing Rules.

Substantial Shareholders' Interests and Short Positions in Shares and Underlying Shares

As at 31 March 2010, the following interests and short positions of 5% or more of the issued share capital of the Company were recorded in the register of interests required to be kept by the Company pursuant to section 336 of the SFO:

Long position in Shares:

Name	Notes	Capacity/ Nature of interest	Number of Shares interested	Percentage of the Company's issued share capital
Swanland		Beneficial owner	125,592,340	20.17%
Masteray		Beneficial owner	53,828,697	8.65%
	(a)	Interest in a controlled corporation	125,592,340	20.17%
Ms. Loh	(b)	Interest in a controlled corporation	179,421,037	28.82%
UGH Investment Holding Limited ("UGH")		Beneficial owner	140,482,433	22.57%
Leung, Yee Li Lana ("Ms. Leung")	(c)	Interest in a controlled corporation	140,482,433	22.57%
Notable Success Investments Limited ("Notable Success")	(d)	Beneficial owner	54,196,943	8.71%
Successful Link Limited ("Successful Link")	(d)	Interest in a controlled corporation	54,196,943	8.71%
Paulo Lam ("Mr. Lam")	(d)	Interest in a controlled corporation	54,196,943	8.71%

Notes:

- (a) Masteray is interested in 51% of the issued share capital in Swanland and hence is deemed to be interested in all the Shares held by Swanland.
- (b) Ms. Loh is the sole beneficial owner of Masteray and hence is deemed to be interested in all the Shares held by Masteray.
- (c) Ms. Leung is the sole beneficial owner of UGH and hence is deemed to be interested in all the Shares held by UGH by virtue of the SFO.
- (d) Notable Success is wholly-owned by Successful Link, which is in turn wholly-owned by Mr. Lam. Therefore, Successful Link is deemed to be interested in all the Shares held by Notable Success and Mr. Lam is deemed to be interested in all the Shares held by Successful Link through Notable Success.

Save as disclosed above, as at 31 March 2010, no person, other than the Directors whose interests are set out in the section "Directors' interests and short positions in shares and underlying shares" above, had registered an interest or a short position in the shares or underlying Shares of the Company that was required to be recorded pursuant to section 336 of the SFO.

Competing Interests

For the three months ended 31 March 2010, the Directors are not aware of any business or interest for the Directors, the management shareholders or the controlling shareholders of the Company and their associates (as defined under GEM Listing Rules) that compete or may compete, directly or indirectly, with the business of the Company and any other conflicts of interests which any such person has or may have with the Company.

Share Option Scheme

A total of 15,500,000 share options have been granted to the Company's employees and consultant under the existing share option scheme of the Company on 26 March 2010. As at the date of this report, 20,000 share options have been lapsed and/or cancelled and nil share options have been exercised.



Interests of the Compliance Adviser

As notified by Quam Capital Limited (“Quam”), the compliance adviser of the Company, neither Quam nor any of its directors, employees or associates (as referred to in Rule 6A.32 of the GEM Listing Rules) had any interests in the securities of the Company, or any rights to subscribe for or to nominate persons to subscribe for the securities of the Company as at 31 March 2010. Pursuant to the compliance advisory agreement dated 30 November 2009 entered into between Quam and the Company, Quam had received and will receive fees for acting as the compliance adviser of the Company.

Purchase, Redemption or Sale of Listed Securities of the Company

Neither the Company, nor any of its subsidiaries purchased, redeemed or sold any of the Company’s listed securities during the three months ended 31 March 2010.

Corporate Governance

The Company has complied with the code provisions set out in the Code on Corporate Governance Practices contained in Appendix 15 of the GEM Listing Rules (the “CG Code”) throughout the period under review, except for the following deviations:

The code provision A.2.1 stipulates that the roles of the chairman of the Board (the “Chairman”) and the chief executive officer (the “CEO”) should be separate and should not be performed by the same individual.

Dr. Jack Lau was the Chairman and the CEO during the period under review, responsible for the management of the Board and the operations of the Group. The Board considered that Dr. Jack Lau has thorough understanding and expertise regarding the business operations of the Group and thus enabling him to make appropriate decisions on a timely manner which are in the interests of the shareholders of the Company as a whole. Considering the present size of the Company and the scope of business of the Group, there is no imminent need to separate the roles of the Chairman and the CEO. However, the Board will continue to review the effectiveness of the corporate governance structure of the Group in order to assess whether separation of the roles of the Chairman and the CEO is necessary.

Securities Transactions by Directors

The Company has adopted the rules set out in Rules 5.48 to 5.67 of the GEM Listing Rules as the code of conduct for dealing in securities of the Company by the Directors (the “Required Standards of Dealings”). The Company periodically issues notices to its Directors reminding them of the general prohibition on dealing in the Company’s listed securities during the blackout periods before the publication of announcements of results. The Company has confirmed, having made specific enquiry of the Directors, all the Directors have complied with the Required Standards of Dealings throughout the period under review.

Audit Committee

The Company established an audit committee on 27 November 2009 with written terms of reference in compliance with Rules 5.28 to 5.29 of the GEM Listing Rules. The audit committee comprises three INEDs, namely, Dr. Lam Lee, Kiu Yue Alice Piera, Dr. Wu, Po Him Philip and Mr. Shu, Wa Tung Laurence. The committee is chaired by Mr. Shu, Wa Tung Laurence. The primary duties of the audit committee are to supervise the internal control policies, the financial reporting systems and procedures of the Company, to review the financial statements and reports of the Group, and to review the terms of engagement and scope of audit work of the external auditors. The unaudited financial statements of the Group for the three months ended 31 March 2010 have been reviewed by the audit committee.

By order of the Board
Perception Digital Holdings Limited
Dr. Jack Lau
Chairman and Executive Director

Hong Kong, 7 May 2010

As at the date of this report, the executive Directors are Dr. Lau, Jack, and Mr. Chui, Shing Yip Jeff; the non-executive Director are Prof. Cheng, Shu Kwan Roger and Prof. Tsui, Chi Ying; and the independent non-executive Directors are Prof. Chu Ching Wu, Paul, Dr. Lam Lee, Kiu Yue Alice Piera, Dr. Wu, Po Him Philip and Mr. Shu, Wa Tung Laurence.

