神州数码
Digital China

DIGITAL CHINA HOLDINGS LIMITED

(神州數碼控股有限公司*)

*(Incorporated in Bermuda with limited liability)*

**(Stock Code: 0861)**

# ANNOUNCEMENT OF ANNUAL RESULTS FOR THE YEAR ENDED 31 MARCH 2007

**FINANCIAL HIGHLIGHTS**

- Turnover increased by 27.96% over the last financial year to reach approximately HK$25,418 million.
- Profit attributable to equity holders of the parent for the financial year ended 31 March 2007 was approximately HK$208 million.

The board of directors (the "**Board**") of Digital China Holdings Limited (the "**Company**") is pleased to announce the consolidated results of the Company and its subsidiaries (collectively the "**Group**") for the financial year ended 31 March 2007 together with comparative figures for the last financial year as follows:

**CONSOLIDATED INCOME STATEMENT**
**Year ended 31 March 2007**

| | Notes | 2007 HK$'000 | 2006 HK$'000 |
|---|---|---|---|
| Revenue | 4 | **25,418,398** | 19,864,897 |
| Cost of sales | | **(23,569,405)** | (18,459,683) |
| Gross profit | | **1,848,993** | 1,405,214 |
| Other income and gains | 4 | **219,938** | 122,669 |
| Selling and distribution costs | | **(1,105,296)** | (810,575) |
| Administrative expenses | | **(318,635)** | (267,471) |
| Other operating expenses, net | | **(230,263)** | (74,851) |
| Total operating expenses | 5 | **(1,654,194)** | (1,152,897) |
| Finance costs | | **(146,406)** | (95,851) |
| Share of profits and losses of: | | | |
| Jointly-controlled entities | | **(20,882)** | (5,171) |
| Associates | | **(5,505)** | (4,383) |
| Profit before tax | 6 | **241,944** | 269,581 |
| Tax | 7 | **(40,631)** | (20,970) |
| Profit for the year | | **201,313** | 248,611 |
| Attributable to: | | | |
| Equity holders of the parent | | **208,429** | 251,917 |
| Minority interests | | **(7,116)** | (3,306) |
| | | **201,313** | 248,611 |
| Dividends – Proposed final | 8 | **72,370** | 86,693 |
| Earnings per share attributable to ordinary equity holders of the parent | 9 | | |
| Basic (HK cents) | | **23.92** | 29.19 |
| Diluted (HK cents) | | **23.78** | 29.07 |

## CONSOLIDATED BALANCE SHEET
**At 31 March 2007**

| | Notes | 2007 HK$'000 | 2006 HK$'000 |
|---|---|---|---|
| **NON-CURRENT ASSETS** | | | |
| Property, plant and equipment | | **337,621** | 420,168 |
| Investment properties | | **208,226** | 184,293 |
| Prepaid land premiums | | **13,547** | 13,485 |
| Goodwill | | **-** | 28,265 |
| Intangible assets | | **19,087** | 39,324 |
| Interests in jointly-controlled entities | | **3,644** | 24,526 |
| Interests in associates | | **22,970** | 36,453 |
| Available-for-sale investments | | **31,611** | 32,944 |
| Deferred tax assets | | **25,038** | 31,150 |
| Total non-current assets | | **661,744** | 810,608 |
| **CURRENT ASSETS** | | | |
| Inventories | | **1,683,630** | 1,567,027 |
| Trade and bills receivables | *10* | **2,852,404** | 2,584,673 |
| Prepayments, deposits and other receivables | | **957,146** | 567,288 |
| Cash and bank balances | | **717,455** | 297,768 |
| | | **6,210,635** | 5,016,756 |
| Non-current asset classified as held for sale | *11* | **12,681** | - |
| Total current assets | | **6,223,316** | 5,016,756 |
| **CURRENT LIABILITIES** | | | |
| Trade and bills payables | *12* | **2,667,444** | 2,055,757 |
| Other payables and accruals | | **975,330** | 741,563 |
| Tax payable | | **31,807** | 17,991 |
| Interest-bearing bank and other borrowings | | **633,536** | 1,206,185 |
| Total current liabilities | | **4,308,117** | 4,021,496 |
| **NET CURRENT ASSETS** | | **1,915,199** | 995,260 |
| **TOTAL ASSETS LESS CURRENT LIABILITIES** | | **2,576,943** | 1,805,868 |
| **NON-CURRENT LIABILITIES** | | | |
| Interest-bearing bank borrowings | | **603,697** | - |
| Total non-current liabilities | | **603,697** | - |
| Net assets | | **1,973,246** | 1,805,868 |
| **EQUITY** | | | |
| **Equity attributable to equity holders of the parent** | | | |
| Issued capital | | **87,404** | 86,693 |
| Reserves | | **1,801,579** | 1,613,473 |
| Proposed final dividend | | **72,370** | 86,693 |
| | | **1,961,353** | 1,786,859 |
| **Minority interests** | | **11,893** | 19,009 |
| Total equity | | **1,973,246** | 1,805,868 |

## NOTES TO THE FINANCIAL STATEMENTS

### 1. Basis of presentation

These financial statements have been prepared in accordance with Hong Kong Financial Reporting Standards ("**HKFRSs**") (which also include Hong Kong Accounting Standards ("**HKASs**") and Interpretations) issued by the Hong Kong Institute of Certified Public Accountants, accounting principles generally accepted in Hong Kong and the disclosure requirements of the Hong Kong Companies Ordinance. They have been prepared under the historical cost convention, except for investment properties, which have been measured at fair value and non-current asset held for sale, which is stated at the lower of its carrying amount and fair value less cost to sell. These financial statements are presented in Hong Kong dollars ("**HK$**") and all values are rounded to the nearest thousand except when otherwise indicated.

### 2. Impact of new and revised HKFRSs

The Group has adopted the following new and revised HKFRSs for the first time for the current year's financial statements.

| | |
|---|---|
| HKAS 21 Amendment | Net Investment in a Foreign Operation |
| HKAS 39 & HKFRS 4 Amendments | Financial Guarantee Contracts |
| HKAS 39 Amendment | Cash Flow Hedge Accounting of Forecast Intragroup Transactions |
| HKAS 39 Amendment | The Fair Value Option |
| HK(IFRIC)-Int 4 | Determining whether an Arrangement contains a Lease |
| HK(IFRIC)-Int 7 | Applying the Restatement Approach under HKAS 29 *Financial Reporting in Hyperinflationary Economics* |

The principal changes in accounting policies are as follows:

(a) HKAS 21 *The Effects of Changes in Foreign Exchange Rat*es

Upon the adoption of the HKAS 21 Amendment regarding a net investment in a foreign operation, all exchange differences arising from a monetary item that forms part of the Group's net investment in a foreign operation are recognised in a separate component of equity in the consolidated financial statements irrespective of the currency in which the monetary item is denominated. This change has had no material impact on these financial statements as at 31 March 2007 or 31 March 2006.

(b) HKAS 39 *Financial Instruments: Recognition and Measurement*

(i) Amendment for financial guarantee contracts

This amendment has revised the scope of HKAS 39 to require financial guarantee contracts issued that are not considered insurance contracts, to be recognised initially at fair value and to be remeasured at the higher of the amount determined in accordance with HKAS 37 *Provisions, Contingent Liabilities and Contingent Assets* and the amount initially recognised less, when appropriate, cumulative amortisation recognised in accordance with HKAS 18 *Revenue*. The adoption of this amendment has had no material impact on these financial statements.

(ii) Amendment for the fair value option

This amendment has changed the definition of a financial instrument classified as fair value through profit or loss and has restricted the use of the option to designate any financial asset or any financial liability to be measured at fair value through the income statement. The Group had not previously used this option, and hence the amendment has had no effect on these financial statements.

(iii) Amendment for cash flow hedge accounting of forecast intragroup transactions

This amendment has revised HKAS 39 to permit the foreign currency risk of a highly probable intragroup forecast transaction to qualify as a hedged item in a cash flow hedge, provided that the transaction is denominated in a currency other than the functional currency of the entity entering into that transaction and that the foreign currency risk will affect the consolidated income statement. As the Group currently has no such transactions, the amendment has had no effect on these financial statements.

(c) HK(IFRIC)-Int 4 *Determining whether an Arrangement contains a Lease*

The Group has adopted this interpretation as of 1 April 2006, which provides guidance in determining whether arrangements contain a lease to which lease accounting must be applied. This interpretation has had no material impact on these financial statements.

(d) HK(IFRIC)-Int 7 *Applying the Restatement Approach under HKAS 29 Financial Reporting in Hyperinflationary Economies*

The Group has adopted this interpretation as of 1 April 2006, which provides guidance on how to apply the requirements of HKAS 29 in a reporting period in which an entity identifies the existence of hyperinflation in the economy of its functional currency when that economy was not hyperinflationary in the prior period, causing the entity to restate its financial statements in accordance with HKAS 29. This interpretation has had no material impact on these financial statements.

## 3. Segment information

Summary details of the business segments are as follows:

(a) the "Distribution" segment engages in the distribution of general information technology ("**IT**") products which consist of notebook computers, desktop computers, PC servers, data projectors, peripherals, accessories and consumer IT products;

(b) the "Systems" segment engages in the distribution of systems products which consist of Unix servers, networking products, storage products and packaged software, as well as the provision of related value-added services; and

(c) the "Services" segment engages in the provision of systems integration, application software development, consultancy and training, etc..

**Primary reporting format - business segments**

The following table presents revenue and profit for the Group's business segments for the years ended 31 March 2007 and 2006:

| | Distribution | | Systems | | Services | | Consolidated | |
|---|---|---|---|---|---|---|---|---|
| | **2007** | 2006 | **2007** | 2006 | **2007** | 2006 | **2007** | 2006 |
| | ***HK$'000*** | *HK$'000* | ***HK$'000*** | *HK$'000* | ***HK$'000*** | *HK$'000* | ***HK$'000*** | *HK$'000* |
| Segment revenue: | | | | | | | | |
| Sales to external customers | **14,727,993** | 11,616,453 | **7,351,562** | 5,679,594 | **3,338,843** | 2,568,850 | **25,418,398** | 19,864,897 |
| Segment gross profit | **705,974** | 544,729 | **698,968** | 506,770 | **444,051** | 353,715 | **1,848,993** | 1,405,214 |
| Segment results | **267,785** | 234,155 | **207,614** | 181,192 | **(24,415)** | 50,344 | **450,984** | 465,691 |
| Interest income, unallocated revenue and gains | | | | | | | **187,358** | 92,300 |
| Unallocated expenses | | | | | | | **(223,605)** | (183,005) |
| Finance costs | | | | | | | **(146,406)** | (95,851) |
| Share of profits and losses of: | | | | | | | | |
| Jointly-controlled entities | **-** | - | **-** | - | **(20,882)** | (5,171) | **(20,882)** | (5,171) |
| Associates | **-** | - | **-** | - | **(5,505)** | (4,383) | **(5,505)** | (4,383) |
| Profit before tax | | | | | | | **241,944** | 269,581 |
| Tax | | | | | | | **(40,631)** | (20,970) |
| Profit for the year | | | | | | | **201,313** | 248,611 |

**Secondary reporting format - geographical segments**

No geographical segment information is presented as over 90% of the Group's customers and operations are located in the Mainland of the People's Republic of China ("**Mainland China**").

## 4. Revenue, other income and gains

Revenue, which is also the Group's turnover, represents the invoiced value of goods sold and services rendered to customers, net of business tax, value-added tax and government surcharges, and after allowances for goods returned and trade discounts.

An analysis of the Group's revenue, other income and gains is as follows:

| | **2007** | 2006 |
|---|---|---|
| | ***HK$'000*** | *HK$'000* |
| Revenue | **25,418,398** | 19,864,897 |
| Other income | | |
| Government grants | **36,830** | 26,084 |
| Bank interest income | **7,035** | 4,468 |
| Gross rental income | **34,431** | 1,246 |
| Others | **9,205** | 9,045 |
| | **87,501** | 40,843 |
| Gains | | |
| Fair value gains on investment properties, net | **1,456** | 7,368 |
| Gain on disposal of non-current asset classified as held for sale | **21,500** | 3,196 |
| Gain on forward foreign exchange contracts | **-** | 2,979 |
| Foreign exchange differences, net | **109,481** | 64,796 |
| Gain on disposal of intangible assets | **-** | 3,487 |
| | **132,437** | 81,826 |
| | **219,938** | 122,669 |

## 5. Total operating expenses

An analysis of the Group's total operating expenses by nature is as follows:

| | **2007** | 2006 |
|---|---|---|
| | ***HK$'000*** | *HK$'000* |
| Selling expenses | **140,205** | 106,787 |
| Promotion and advertising expenses | **149,810** | 97,241 |
| Staff costs included in operating expenses (including directors' remuneration) | **742,162** | 559,136 |
| Other expenses | **622,017** | 389,733 |
| | **1,654,194** | 1,152,897 |

## 6. Profit before tax

The Group's profit before tax is arrived at after charging/(crediting):

| | **2007** | 2006 |
|---|---|---|
| | ***HK$'000*** | *HK$'000* |
| Cost of inventories sold | **23,058,332** | 18,105,956 |
| Depreciation | **64,197** | 56,950 |
| Amortisation of prepaid land premiums | **352** | 162 |
| Impairment of goodwill | **28,566** | 12,894 |
| Amortisation of intangible assets | **5,019** | 7,255 |

| | | |
|---|---|---|
| Impairment of intangible assets | **16,259** | 19,781 |
| Impairment of available-for-sale investments | **2,425** | - |
| Minimum lease payments under operating leases in respect of land and buildings | **60,131** | 45,060 |
| Provisions/(reversal of provisions) and write-off of obsolete Inventories | **28,230** | (22,992) |
| Impairment and write-off of doubtful trade receivables | **64,610** | 38,664 |
| Loss on disposal of items of property, plant and equipment | **4,142** | 2,313 |

## 7. Tax

| | **2007** | 2006 |
|---|---|---|
| | ***HK$'000*** | *HK$'000* |
| Group: | | |
| Current – Hong Kong | **1,447** | - |
| Current – The People's Republic of China ("**PRC**") | **32,119** | 23,757 |
| Deferred | **7,065** | (2,787) |
| Total tax charge for the year | **40,631** | 20,970 |

(a) PRC corporate income tax represents tax charged on the estimated assessable profits arising in the PRC. In general, the subsidiaries of the Group are subject to the PRC corporate income tax rate of 33% except for certain subsidiaries which are entitled to tax holiday and preferential tax rates.

(b) During the year, Hong Kong profits tax has been provided at the rate of 17.5% on the estimated assessable profits arising in Hong Kong. No provision for Hong Kong profits tax had been made in the prior year as the Hong Kong subsidiaries of the Group had no estimated assessable profits arising in Hong Kong or had tax losses brought forward from prior years to set off assessable profits for the year ended 31 March 2006.

(c) No provision for Hong Kong profits tax has been made for the jointly-controlled entities and associates as the jointly-controlled entities and associates had no estimated assessable profits arising in Hong Kong for the years ended 31 March 2006 and 2007. PRC corporate income tax has been provided at the rate of 33% on the estimated assessable profits of the jointly-controlled entities and associates for the years ended 31 March 2006 and 2007. The share of tax credit attributable to the jointly-controlled entities of approximately HK$32,000 (2006: Nil) and the share of tax credit attributable to the associates of approximately HK$317,000 (2006: share of tax charge of approximately HK$377,000) are included in "Share of profits and losses of jointly-controlled entities" and "Share of profits and losses of associates" respectively on the face of the consolidated income statement.

On 16 March 2007, the National Peoples' Congress approved the Corporate Income Tax Law of the People's Republic of China (the "**New CIT Law**"), which will become effective on 1 January 2008. The New CIT Law introduces a wide range of changes which include, but are not limited to, the unification of the income tax rate for domestic-invested and foreign-invested enterprises at 25%. At the date of this announcement, detailed implementation and administrative requirements relating to the New CIT Law have yet to be announced. These detailed requirements include regulations concerning the computation of taxable income, as well as specific preferential tax treatments and their transitional provisions. The Group will further evaluate the impact of the New CIT Law on its operating results and financial positions of future periods as more detailed requirements are issued.

## 8. Dividends

| | **2007** *HK$'000* | 2006 *HK$'000* |
|---|---:|---:|
| Proposed final dividend – 8.28 HK cents (2006: 10.00 HK cents) per ordinary share | **72,370** | 86,693 |

The proposed final dividend for the year is subject to the approval of the Company's shareholders at the forthcoming annual general meeting.

## 9. Earnings per share attributable to ordinary equity holders of the parent

The calculation of basic earnings per share amounts is based on the profit for the year attributable to ordinary equity holders of the parent of approximately HK$208,429,000 (2006: HK$251,917,000), and the weighted average of 871,479,182 (2006: 862,916,065) ordinary shares in issue during the year.

The calculation of diluted earnings per share amounts is based on the profit for the year attributable to ordinary equity holders of the parent of approximately HK$208,429,000 (2006: HK$251,917,000) and 876,317,035 (2006: 866,515,404) ordinary shares, which was the weighted average of 871,479,182 (2006: 862,916,065) ordinary shares in issue during the year, and the weighted average of 4,837,853 (2006: 3,599,339) ordinary shares deemed to have been issued at no consideration on the deemed exercise of all the outstanding share options during the year.

## 10. Trade and bills receivables

The Group's trading terms with its customers are mainly on credit, except for new customers, where payment in advance is normally required. The credit period is generally for a period of 30 days to 180 days. An aged analysis of the Group's trade and bills receivables as at the balance sheet date and net of impairment is as follows:

| | **2007** *HK$'000* | 2006 *HK$'000* |
|---|---:|---:|
| Within 30 days | **1,445,863** | 1,444,990 |
| 31 to 60 days | **327,043** | 339,584 |
| 61 to 90 days | **277,791** | 250,167 |
| 91 to 180 days | **447,396** | 324,812 |
| Over 180 days | **354,311** | 225,120 |
| | **2,852,404** | 2,584,673 |

## 11. Non-current asset classified as held for sale

During the year, the Group has entered into a share transfer agreement with a third party to dispose of its entire interest in an associate, Nanjing Mercuries DC Financial Systems Ltd. The disposal has not yet been completed as at 31 March 2007 and the directors anticipate that the disposal will be completed by the end of July 2007.

## 12. Trade and bills payables

An aged analysis of the Group's trade and bills payables as at the balance sheet date is as follows:

| | **2007** *HK$'000* | 2006 *HK$'000* |
|---|---:|---:|
| Within 30 days | **1,400,964** | 778,527 |
| 31 to 60 days | **876,647** | 765,235 |

| | | |
|---|---|---|
| 61 to 90 days | **212,180** | 267,857 |
| Over 90 days | **177,653** | 244,138 |
| | **2,667,444** | 2,055,757 |

## DIVIDENDS

The Board recommends the payment of a final dividend of 8.28 HK cents (2006: 10 HK cents) per share for the year ended 31 March 2007 to the shareholders whose names appear on the register of members of the Company on 22 August 2007. Subject to the shareholders' approval at the forthcoming annual general meeting of the Company, the final dividend will be paid on or before 5 September 2007.

## ANNUAL GENERAL MEETING

The annual general meeting of the Company will be held at Granville Room, Lower Lobby, Conrad Hong Kong, Pacific Place, 88 Queensway, Hong Kong on Wednesday, 22 August 2007 at 9:30 a.m.. Notice of the annual general meeting will be issued in due course.

## CLOSURE OF REGISTER OF MEMBERS

The register of members of the Company will be closed from Wednesday, 15 August 2007 to Wednesday, 22 August 2007 (both days inclusive) during which period no transfer of shares will be effected. In order to qualify for the proposed final dividend, all completed transfer documents, accompanied by the relevant share certificates, must be lodged with the Company's branch share registrar, Abacus Share Registrars Limited (to be renamed as Tricor Abacus Limited with effect from 1 August 2007) at 26/F., Tesbury Centre, 28 Queen's Road East, Wanchai, Hong Kong, for registration not later than 4: 00 p.m. on Tuesday, 14 August 2007.

## MANAGEMENT DISCUSSION AND ANALYSIS

### 1. Overall Business Performance

**During the year ended 31 March 2007, the Group basically achieved the businesses and management targets set for this financial year. Its principal business grew and its overall profit remained stable. Moreover, the Group's operating cash flow, cash cycle and other aspects also achieved good performance. The Group basically realized a balanced development between business growth and risk control, thereby laying a solid foundation for the Group's development in the second five-year period after its listing.**

**The growth of the Group's turnover in this financial year surpassed that of the overall domestic market, which reinforced its market position.** According to an analysis report provided by IDC in May 2007, the annual growth rate of PRC IT market for 2006 was 15.7%. The Group recorded a turnover of HK$25,418 million for the year ended 31 March 2007, representing an increase of 27.96% comparing to HK$19,865 million of last financial year. In order to better implement the Group's business directive of catering to the transformation of IT services, the Group continued to cooperate with suppliers, actively explore new cooperation opportunities, strengthen channel development and deepen the cooperation with channels for the Distribution business and Systems business. The Group made intensive endeavor to focus on the finance, telecommunications and government sectors for the Services business so as to achieve stronger growth. The Group's profitability during this financial year also improved as the overall gross profit margin reached 7.27%, up from 7.07% of the same period of last financial year.

**As a leading IT products distributor and service provider in the Mainland, the principal businesses of the Group continued to maintain a superior position during this financial year.** According to an analysis report provided by IDC in April 2007, Digital China topped the list of IT product distributors and service providers on the Mainland. According to an analysis report of Sm@rtPartner in May 2007, the Distribution and Systems businesses of the Group continued to occupy approximately 50% of the market share of the top four distributors of the Mainland market during 2006, consolidating its role as a market leader. According to an analysis report of IDC in April 2007, the Group's Services business ranked first among the local service providers in the same industry, and also ranked the first in the two segment markets – government and banking segments, as a local provider.

**During this financial year, the Group adopted, following prudence principle, financial treatments on certain special items not arose in this financial year with contingency risks. On the other hand, in order to focus on corporate innovation and the buildup of capabilities to maintain sustainable business development, enhance the brand attractiveness, the Group further increased its input to the software product development and market development, and organized a series of large scale publicity activities. As a result of the above two aspects, the Group's profit attributable to equity holders of the parent (profit attributable to shareholders) during this financial year was affected. Relevant factors were illustrated as follows:**

(1) The Group recorded an exchange gain of approximately HK$109 million for this financial year, representing an increase of HK$44 million over HK$65 million of last financial year;

(2) After the completion of merger and acquisition of Beijing Si-Tech Information Technology Co., Ltd. ("**STQ**") by the Group in the last financial year, the new company fully expanded its integration business with telecommunications customers and marketing for software development services. In order to reflect the future profit and loss of this new company in a clearer manner, based on prudence principle, the Group charged in full the goodwill arising from the acquisition of STQ of approximately HK$29 million as impairment in this financial year. In addition, an investment loss of approximately HK$12 million was recognized as a result of impairment for the intangible assets contributed into Digital China System Access Holding Limited, a jointly-controlled entity, by both joint venture parties;

(3) During the third quarter of this financial year, the Group recovered HK$8 million through a lawsuit, being part of an amount of approximately HK$12 million trade receivable balance with a systems business customer. Nevertheless, a bad debt loss of approximately HK$4 million was eventually incurred;

(4) During this financial year, the Group amortised and impaired an aggregate amount of approximately HK$21 million in respect of the intangible assets (development costs capitalised) capitalised in previous financial years. No additional development costs were capitalised in this financial year (additional development costs capitalised in the last financial year exceeded the amount amortised and impaired by approximately HK$7 million);

(5) The Group launched a series of large scale activities during this financial year, including: "Annual Innovation Meeting" (創新年會) on the Theme of "Digitization. Innovation. China" (數字中國) , the "2006 Summit of Digital China Channel Partners" (2006 神州數碼渠道夥伴峰會) on the Theme of "Power of Flying" (飛翔的力量), the "2006 Summit of Digital China Value-added Services Senior Partners" (2006 年神州數碼增值服務高級合作夥伴峰會) on the Theme of "Innovating Your World" (創新你的世界) and the ceremonies celebrating the establishment of Digital China (Hefei) Company Limited (神州數碼（合肥）有限公司), Fuzhou Digital China Company Limited (福州神州數碼有限公司) and Changsha Digital China Company Limited (長沙神州數碼有限公司). These activities not only upgraded the brand image of the Company in the industry, but also enhanced cooperation with local governments, channels and customers, and promoted the Group's in-depth business development in different regions. However, the expense of organizing large conferences and channel marketing activities and of the establishment of the subsidiaries had certain impact on the Group’s profit during this financial year.

**The Group's profit attributable to equity holders of the parent during this financial year was approximately HK$208 million, the return on shareholders' equity was 10.63%, representing a slight decrease comparing to last financial year.** Basic earnings per share and diluted earnings per share were 23.92 HK cents and 23.78 HK cents.

**The Group aimed at creating healthy cashflow during this financial year, and insisted on the implementation of healthy business operation strategies, and the Group's operating cash flow and cash cycle also achieved good performance.** Net cash inflow from operating activities of the Group for the year ended 31 March 2007 amounted to approximately HK$571 million, representing an increase of approximately HK$441 million comparing to the last financial year. The increase was mainly attributable to the increase of trade and bill payables. For the year ended 31 March 2007, the Group's cash cycle was 27.44 days, representing a decrease of 7.16 days comparing to the last financial year, while the turnover days of the inventory and the trade receivables decreased by 2.97 days and 3.99 days respectively.

**2. Business Review**

**2.1 Distribution business**

The Group's Distribution business experienced robust growth in this financial year. The turnover of the Group's Distribution business for the year ended 31 March 2007 reached HK$14,728 million, representing an increase of 26.79% from last financial year, far exceeding the growth rate of the PRC IT market. The Distribution business of the Group emphasized the balance between business growth and profitability. The gross profit margin for this financial year increased to 4.79%, comparing to 4.69% of last financial year.

**2.1.1 New product operation gradually entered a steady growth stage**

During this financial year, the Group's Distribution business recorded rapid growth in the turnover of its various major business sectors. The turnover of notebook computers of the Group for this financial year grew by 41.73% from last financial year. The turnover of consumer IT products increased by 46.74% from last financial year. The turnover of PC servers increased by 41.27% from last financial year. The turnover of accessories increased by 38.16% from last financial year. The ACER notebook and desktop computers business, and the FULFILLMENT business of the HP desktop computers, which was introduced by the Group during last financial year, has brought a turnover of exceeded HK$3,466 million for the year ended 31 March 2007, representing an increase of HK$2,054 million from last financial year.

**2.1.2 Strengthened channel development and deepened channel cooperation**

The Group continued to reinforce its cooperation with channels for the Group's Distribution business. The "2006 Summit of Digital China Channel Partners" (2006 神州數碼渠道夥伴峰會) on the Theme of "Power of Flying" (飛翔的力量) held in Zhuhai on 5-7 December 2006 was attended by over 800 excellent channels. The initiation of "Flying Project" (飛翔工程), a project aimed to further enhance the cooperation with the channels, drew tremendous responses. As at 31 March 2007, the number of effective channels for its Distribution business reached 5,956, representing an increase of 31.39% from the end of last financial year.

**2.1.3 Continued optimization of internal operation process and strengthening of operation and management capability**

Regarding the Group's Distribution business, the Group further optimized its business processes on the basis of its business process management system. The Group focused on the optimization of order process this financial year: continued the working method of CPI (Continuous Process Innovation) adopted from last financial year and conducted quantitative analysis on the factors affecting order efficiency and continued to improve and optimize so as to improve the efficiency of the Distribution business in handling orders and enhance operating efficiency and customers' satisfaction.

**2.2 Systems business**

The turnover of the Group's Systems business for the year ended 31 March 2007 reached HK$7,352 million, representing an increase of 29.44% comparing to last financial year. While expanding the business scale, the Group maintained its profitability through the in-depth cooperation with channels partners. Gross profit margin for this financial year increased to 9.51% comparing to 8.92% of last financial year.

**2.2.1 Actively catering to the expansion strategy of suppliers led to remarkable business growth**

During this financial year, the Group's Systems business recorded significant growth in the turnover of its various major business sectors comparing to the last financial year. The turnover of network products increased by 28.03% comparing to last financial year. The turnover of packaged software increased by 23.74% comparing to last financial year. The turnover of storage products increased by 14.28% comparing to last financial year. The turnover of UNIX servers increased by 13.98% comparing to last financial year. By adopting the strategy of meeting suppliers' business requirements for expansion into medium and small cities, the Group recorded substantial growth in the turnover of its four major products during this financial year, and further consolidated its advantageous position in the UNIX server, network product and packaged software sectors.

**2.2.2 In-depth development in different regions strengthened through synergistic development with channels**

The Group's Systems business reinforced the expansion of regional channels during this financial year. Comparing to 31 March 2006, the total number of channels increased by 16% as at 31 March 2007. During this financial year, the Group's Systems business organized "2006 Conference of Channels in Tier 2 and 3 Cities" (2006 夥伴關愛之旅) in 18 provinces and autonomous regions, and the "2006 Summit of Digital

China Value-added Services Senior Partners" (2006 年神州數碼增值服務高級合作夥伴峰會) on the Theme of "Innovating Your World" (創新你的世界). Meanwhile, persistent efforts were made to promote a series of cooperative programs with the Core Channels, and Core Channels Authorizing Conference（核心渠道峰會以及授牌） was organized to reinforce the support and management to the channels and enhance business values.

**2.2.3 Reinforcement in service capability through internal measures**

The Group continued to reinforce its service capability during this financial year. The number of technical staff increased from 178 persons as at 31 March 2006 to 208 persons as at 31 March 2007. The Group has adjusted its service and product portfolio and completed the compilation of the service and product manual of the Systems business. Services business of the Group's Systems business achieved remarkable results and the turnover of services business recorded a 114% growth comparing to last financial year.

**2.3 Services business**

The Group's Services business maintained rapid grow. For the year ended 31 March 2007, the turnover of the Services business of the Group recorded HK$3,339 million, representing a 29.97% growth comparing to last financial year. While expanding the business scale, the Group maintained its profitability and its overall gross profit margin reached 13.30%.

**2.3.1 Customer-oriented and maintained steady development in various sectors**

During this financial year, the Group continued to adhere to its customer-oriented principle in its Services business, which contributed to the steady growth of different sectors. The Group maintained its advantageous position in key sectors such as the finance, telecommunications and government sectors. In the telecommunications sector, the Group continued to cooperate with leading telecommunication operators such as China Mobile and China Network Communications, with whom the Group has entered into a number of billion-worth contracts. After the acquisition of STQ, the Group added four core mobile customers, successfully secured the contract of Anhui Unicom's BSS project and became an system integrator of the mobile agent service (MAS) for the headquarter of China Mobile, and expanded the traditional business support system. Regarding the tax sector, the Group has achieved remarkable results in managing large clients such as the State Administration of Taxation, Shenzhen Municipal office of the State Administration of Taxation, Liaoning Bureau of Local Taxation. In the government sector, the Group has achieved steady progress and secured new major clients such as PetroChina and the Ministry of Science and Technology.

**2.3.2 Rapid development in service scale as a result of the improvement in products support and the IT outsourcing and maintenance services**

Regarding improvement of the service system, the Group established the products support and IT outsourcing and maintenance service delivery centre in this financial year in order to lay a foundation for service process and cost reduction. The Group also established a technological operation platform to improve utilization efficiency of resources and strengthen process control. Besides, the Group increased its investment in the commercialization and standardization of services. The Group also passed the international certification of IT service management (ITIL/ITSM) system ISO 20000, and became the first enterprise obtaining such certification in the PRC after such international standard was upgraded to ISO20000:2005.

For the year ended 31 March 2007, the products support and IT outsourcing and maintenance services of the Group's Services business concluded contracts valued over HK$400 million, representing an increase of more than 50% from last financial year. The Group concluded million-worth contracts with all of the four leading telecommunication operators. The Services business of the Group also successfully secured new major clients in the non-telecommunications sectors, such as the banking, insurance and tax sectors.

**2.3.3 Steady progress in three core transformation strategies**

For the year ended 31 March 2007, the Group's Services business devoted additional efforts on transformation by establishing and promoting three core capabilities. Firstly, transforming from customer on-site development to centralized development – the Group's Services business significantly enhanced the infrastructure capabilities of its Xi'an software development base. The construction of infrastructure facilities was basically completed and substantial investment was also made in the expansion and training of workforce. Secondly, transforming from application software development business to IT operation outsourcing business – building up the capability of providing comprehensive operation outsourcing services of labour, equipment and facilities. Thirdly, transforming from customized software development to software product development – the Group's Services business increased its contribution in software product development for its major sectors such as finance, telecommunications and government, leading to enhancement of its software product capabilities and improvement of delivery efficiencies.

**3. Management Review**

The financial year 2006/07 is the first year of the Group's new five-year plan. The Group's management capabilities will be facing new tests again. Besides promoting business development by stepping up the persistent efforts on the key scopes of R (Risk), D (Development), C (Customer), the Group commenced work in various aspects to improve capabilities in brand, resource and culture management.

(1) Brand promotion centering around the strategic theme of "IT Services Innovation" began to bear fruit. The success of the innovative conferences and the large scale marketing activities launched by the Distribution and Systems businesses respectively contributed significantly to deepening the Group's brand identity in IT services and promoting the Group's innovative concepts. The effective promotion of brand identity created more favourable conditions for the expansion of the Group's various businesses. Meanwhile, Digital China (Hefei) Company Limited (神州數碼（合肥）有限公司), Fuzhou Digital China Company Limited (福州神州數碼有限公司) and Changsha Digital China Company Limited (長沙神州數碼有限公司) were established during this financial year. This not only effectively enhanced communications with local governments and different sectors, but also upgraded Digital China's brand image and provided impetus for the Group's in-depth business development in these three provinces.

(2) Regarding human resource management, the Group's management stepped up the training of talents with high calibre and potentials and tried to explore a set of proven and effective talent training methods and mechanism, so as to lay the foundation for the Company's talent ladder. The Group reactivated the "talent programme" in the campus again and upgraded its employer's image in all the pivotalcolleges and universities.

(3) The Group continued to strengthen its fund and process management and risk control during this financial year. By raising awareness of fund efficiency and innovating financial tools on an on-going basis, the Group gradually established its core competitiveness centering at the overall risk management system of increasing fund returns.

(4) The Group has stepped up the development of corporate culture to enhance corporate cohesion, motivate and encourage staff to innovate new ideas. During this financial year, the Group organized a series of corporate culture activities targeting at technical staff, sales personnel and supportive staff and received overwhelming responses from the staff.

**4. Outlook**

The management of the Group are satisfied with the Group's outstanding business and management results achieved in this financial year. In the coming year, the Group will, under the directive of IT service transformation, continue to deepen its customer-oriented business model, innovate and enhance value, and deepen the development of RDC capabilities.

At the same time, the Group will still face huge pressures and challenges internally or externally. Firstly, due to intensified market competition, the Group still faces the risk of decline in gross profit margin for Distribution and Systems businesses; Secondly, increase in the interest rate of RMB and USD borrowings leads to increase in the finance costs of the Group; Thirdly, amortisation of the Group’s intangible assets (development costs capitalised) remained; Fourthly, the Group will increase its investment in human resources and research and development capabilities of IT services business so as to further improve the core competitiveness of the Group’s Services business; and Fifthly, in order to improve its market influence and competitiveness, the Group will maintain its cordial relationship with the government, suppliers and business partners, and continue its input on brand advertising and promotion.

The management will formulate its annual plan and budget under a pragmatic principle and execute policies under an effective implementation assurance system. The management is confident that the result of the Group will record growth in the financial year of 2007/08, which will lay a more solid foundation for its development in the next five years.

**Capital Expenditure, Liquidity and Financial Resources**

The Group mainly finances its operations with internally generated cash flows, bank loans and banking facilities.

The Group had total assets of HK$6,885 million at 31 March 2007 which were financed by total liabilities of HK$4,912 million, minority interests of HK$12 million and equity attributable to equity holders of the parent of HK$1,961 million. The Group’s current ratio at 31 March 2007 was 1.44 as compared to 1.25 at 31

March 2006.

During the year ended 31 March 2007, capital expenditure of HK$81 million was incurred for the acquisition of office equipment and leasehold improvements of buildings in Beijing.

The aggregate interest-bearing borrowings as a ratio of equity attributable to equity holders of the parent was 0.63 at 31 March 2007 as compared to 0.68 at 31 March 2006. The computation of the said ratio was based on the total interest-bearing borrowings of HK$1,237 million (31 March 2006: HK$1,206 million) and equity attributable to equity holders of the parent of HK$1,961 million (31 March 2006: HK$1,787 million).

At 31 March 2007, the denomination of the interest-bearing borrowings of the Group was shown as follows:

| | Denominated in United States dollar *HK$'000* | Denominated in Renminbi *HK$'000* | Total *HK$'000* |
|---|---|---|---|
| **Current** | | | |
| Interest-bearing bank borrowings, unsecured | 599,887 | - | 599,887 |
| Interest-bearing bank borrowing, secured | - | 33,649 | 33,649 |
| | 599,887 | 33,649 | 633,536 |
| **Non-current** | | | |
| Interest-bearing bank borrowings, unsecured | - | 603,697 | 603,697 |
| Total | 599,887 | 637,346 | 1,237,233 |

The Group's current borrowings of approximately HK$34 million extended by financial institutions to a subsidiary of the Group, Beijing Si-Tech Information Technology Co., Ltd. ("**STQ**"), were secured by a property situated in the Mainland China with a value of approximately HK$16 million at 31 March 2007 and 14,061,976 issued shares of STQ in favour of Beijing Zhongguancun Sci-Tech Guaranty Co. Ltd. (the "**Pledgee**"), an independent third party, for securing a guarantee issued by such Pledgee on behalf of STQ. The Group's non-current bank borrowings of approximately HK$604 million represented the term loans and are repayable from Year 2008 to 2012.

The Group's total available credit facilities at 31 March 2007 amounted to HK$7,361 million, of which HK$1,000 million were in term loan facilities, HK$4,524 million were in trade lines and HK$1,837 million were in short-term and revolving money market facilities. At 31 March 2007, the facility drawn down was HK$604 million in term loan facilities, HK$2,150 million in trade lines and HK$313 million in short-term and revolving money market facilities.

Under the normal course of business, the Group has issued performance bonds to some customers for potential claims of non-performance in order to satisfy the specific requirements of these customers. As no material claims had been made by the customers under such performance bonds in the past, the management considers that the possibility of realisation of any actual material liabilities arising from such performance bonds is remote.

**Human Resources**

At 31 March 2007, the Group had approximately 6,700 (31 March 2006: approximately 5,400) full-time employees. The majority of these employees work in the PRC. The Group offers remuneration packages in line with industry practice. Employees' remuneration includes basic salaries and bonuses. With the increase in the total number of staff to cope with its business requirements, the Group has recorded a 37.13% increase in staff costs to approximately HK$878 million for the year ended 31 March 2007 as compared with an approximate sum of approximately HK$640 million for the last financial year. In order to attract and retain a high caliber of capable and motivated workforce, the Company offers share options to staff based on the individual performance and the achievements of the Company's targets. The Group is committed to providing its staff with various in-house and external training and development programs.

## AUDIT COMMITTEE

The audit committee has reviewed with the management and the auditors of the Company the accounting principles and practices adopted by the Group and discussed auditing, internal control and financial reporting matters including the review of the financial statements of the Group for the year ended 31 March 2007.

## CORPORATE GOVERNANCE

Subsequent to the publication of the Corporate Governance Report in the 2005/06 annual report, a special resolution was passed at the annual general meeting of the Company held on 23 August 2006 to amend the Company's Bye-Laws to the effect that: (i) any Director or Directors or Chairman of the meeting who, individually or collectively, hold proxies in respect of shares representing 5% or more of the total voting rights at a general meeting may demand a poll; and (ii) the Company in general meeting will have the power by ordinary resolution, instead of special resolution, to remove a Director before the expiration of his period of office.

The Company has complied with the Code on Corporate Governance Practices as set out in Appendix 14 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited throughout the year ended 31 March 2007, except for the following deviations:

### Code Provision A.4.1

This code provision stipulates that non-executive directors should be appointed for a specific term, subject to re-election.

All Directors of the Company (including executive and non-executive Directors) were not appointed for any specific term. However, all Directors (save for Chairman or Managing Director) are subject to retirement by rotation at each annual general meeting in accordance with the Company's Bye-Laws and shall be eligible for re-election. The Board of Directors shall ensure all Directors (including the Chairman and Managing Director) shall be subject to retirement by rotation at least once every three years so as to accomplish the same purpose as a specific term of appointment.

### Code Provision A.4.2

The second part of this code provision stipulates that every director, including those appointed for a specific term, should be subject to retirement by rotation at least once every three years.

Under the Company's Bye-Laws, at each annual general meeting one-third of the Directors for the time being or, if their number is not three or a multiple of three, the number nearest to one-third shall retire from office provided that notwithstanding anything herein, the Chairman of the Board and the Managing Director shall not, whilst holding such office, be subject to retirement by rotation or be taken into account in determining the number of Directors to retire in each year. In view of good corporate governance practices, the Chairman of the Company voluntarily retires from his office once every three years notwithstanding that he is not required to do so by the Bye-Laws.

## PURCHASE, SALE OR REDEMPTION OF THE COMPANY'S LISTED SECURITIES

During the year ended 31 March 2007, neither the Company nor any of its subsidiaries had purchased, sold or redeemed any of the Company's listed securities.

On behalf of the Board
**LI Qin**
*Chairman*

Hong Kong, 12 July 2007

As at the date of this announcement, the Board comprises ten directors namely:

*Executive Directors*: Mr. LI Qin *(Chairman)*, Mr. GUO Wei *(Vice Chairman, President and Chief Executive Officer)*, Mr. ZENG Maochao, Mr. LIN Yang and Mr. HUA Zhinian.

*Non-executive Director*: Mr. William O. GRABE.

*Independent Non-executive Directors*: Mr. HU Zhao Guang, Professor WU Jinglian, Mr. WONG Man Chung, Francis and Mr. KWAN Ming Heung, Peter.

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*(* For identification purpose only)*