



HI SUN GROUP LIMITED

高陽集團有限公司*

(incorporated in Bermuda with limited liability)

(Stock Code: 0818)

ANNOUNCEMENT OF INTERIM RESULTS FOR THE SIX MONTHS ENDED 30TH JUNE 2004

The Board of Directors (the “Board”) of Hi Sun Group Limited (the “Company”) is pleased to announce the unaudited consolidated results of the Company and its subsidiaries (the “Group”) for the six months ended 30th June 2004 together with the unaudited comparative figures for the corresponding period as follows: –

		Unaudited Six months ended 30th June	
		2004	2003
	<i>Note</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Turnover	2	66,650	131,165
Cost of sales		(43,775)	(86,571)
Gross profit		22,875	44,594
Other revenue		146	199
Selling and distribution expenses		(18,722)	(19,198)
Administrative expenses		(31,988)	(33,191)
Loss from operation	3	(27,689)	(7,596)
Finance costs		(496)	(964)
Loss attributable to shareholders		(28,185)	(8,560)
Basic loss per share	4	HK\$(0.08)	HK\$(0.03)

* *for identification purpose only*

Notes:

1. Basis of preparation 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 Institute of Certified Public Accountants.

These condensed accounts should be read in conjunction with the 2003 annual accounts.

The accounting policies and methods of computation used in the preparation of these condensed accounts are consistent with those used in the annual accounts for the year ended 31st December 2003.

2. Segment reporting

The Group is organised into three main business segments:

- (a) Financial solutions, services and related products – provisions of customised information system consultancy and integration services and sales of computer hardware to financial institutions and banks;
- (b) Telecommunication solutions, services and related products – provision of customised information system consultancy and integration services and sales of computer hardware to the telecommunication industries; and
- (c) Electronic payment products and services – sales of point-of-sale terminals;

In determining the Group’s geographical segments, revenues and results are attributed to the segments based on the location of the customers.

An analysis of the Group's revenue and results for the period by business segment is as follows:

	Unaudited				Group
	Six months ended 30th June 2004				
	Financial solutions, services and related products	Telecom-munications solutions, services and related products	Electronic payment products and services	Other operations	HK\$'000
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Turnover	20,559	5,872	40,119	100	66,650
Segment results	(18,501)	(7,075)	3,969	(6,228)	(27,835)
Unallocated income					146
Loss from operation					(27,689)
Finance costs					(496)
Loss attributable to shareholders					(28,185)

	Unaudited				Group
	Six months ended 30th June 2003				
	Financial solutions, services and related products	Telecom-munications solutions, services and related products	Electronic payment products and services	Other operations	HK\$'000
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Turnover	98,582	10,524	22,059	-	131,165
Segment results	1,123	(1,158)	(2,731)	(5,002)	(7,768)
Unallocated income					172
Loss from operation					(7,596)
Finance costs					(964)
Loss attributable to shareholders					(8,560)

There are no sales or other transactions between the business segments. Unallocated income represents interest income.

An analysis of the Group's turnover and contribution to operating loss for the period by geographical segment is as follows:

	Unaudited Turnover		Unaudited Loss from operation	
	Six months ended		Six months ended	
	30th June		30th June	
	2004	2003	2004	2003
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Hong Kong, Korea and South East Asia	18,729	20,312	(1,763)	(5,642)
Mainland China	47,921	110,853	(25,926)	(1,954)
	<u>66,650</u>	<u>131,165</u>	<u>(27,689)</u>	<u>(7,596)</u>

There are no sales or other transactions between the geographical segments.

3. Loss from operation

Loss from operation is stated after crediting and charging the following:

	Unaudited	
	Six months ended	
	30th June	
	2004	2003
	<i>HK\$'000</i>	<i>HK\$'000</i>
Crediting		
Reversal of provision for inventory	<u>371</u>	<u>–</u>
Charging		
Auditors' remuneration	500	600
Depreciation	4,412	4,276
Staff costs (including directors' remuneration):		
Wages and salaries	30,912	42,668
Pension contributions	1,955	1,240
<i>Less: staff costs capitalised into contract work in progress</i>	<u>(5,050)</u>	<u>(2,036)</u>
	27,817	41,872
Operating lease rentals for land and buildings	5,236	4,601
Loss on disposed and write off of fixed assets	19	320
Provision for doubtful debts	<u>–</u>	<u>1,646</u>

4. Loss per share

The calculation of basic loss per share is based on the Group's loss attributable to shareholders of HK\$28,185,000 (2003: loss of HK\$8,560,000) and on the number of 333,054,030 (2003: 333,054,030) ordinary shares in issue during the period.

Diluted loss per share has not been presented for the period ended 30th June 2004 as the conversion of potential ordinary shares would have anti-dilutive effect to the basic loss per share.

There were no dilutive effect on the basic loss per share for the period ended 30th June 2003.

5. Related party transactions

Significant related party transactions, which were carried out in the normal course of the Group's business are as follows:

		Unaudited	
		Six months ended	
		30th June	
		2004	2003
		<i>HK\$'000</i>	<i>HK\$'000</i>
Management fees paid to a related company	<i>(a)</i>	–	280
Consultancy fees paid to a related company	<i>(b)</i>	–	74
		_____	_____

(a) Two subsidiaries, Hi Sun Technology Holding Limited and Pax Technology Limited, received management services from Hi Sun Management Limited (“HSML”), a company owned by a director, who is also a substantial shareholder, of the Company, on terms mutually agreed between the subsidiaries and HSML.

(b) A subsidiary, Pax Technology Limited, received consultancy services from Hi Sun Information Technology Services Limited (“HSITSL”), a company owned by a director, who is also a substantial shareholder, of the Company, on terms mutually agreed between the subsidiary and HSITSL.

MANAGEMENT DISCUSSION AND ANALYSIS

Financial and business review

For the first half of 2004, the Group's turnover amounted to HK\$66.65 million, as compared to the turnover of HK\$131.17 million for the corresponding period of the previous year, and the net loss attributable to shareholders was HK\$28.19 million, while the loss for the corresponding period of the previous year was HK\$8.56 million.

Financial solutions, applications, services and related products

During the period under review, this business segment recorded a turnover of HK\$20.56 million (2003 interim: HK\$98.58 million) and a loss of HK\$18.50 million (2003 interim: profit HK\$1.12 million).

During the period, consultancy and IT services accounted for 50% and 65% respectively of the turnover and gross profit of this business segment, as compared to the 55% and 91% respectively in the corresponding period of the last year.

System integration and hardware products business accounted for 50% and 35% respectively of the turnover and gross profit of this business segment, as compared to the 45% and 9% respectively in the corresponding period of the last year.

Decline in the turnover from this segment was mainly attributed to the operating strategy formulated last year, which focused on the core business of this segment. There was a further shrinkage in the business of hardware products, turnover from which fell by approximately HK\$33.47 million as compared to the previous year. Turnover from consultancy and IT services also decreased by approximately HK\$44.55 million, partly due to turnover fall resulting from the spin-off of several business units. The major core banking system business also suffered from a delay in customers' inspection and acceptance time, which was in turn caused by the reorganisation and merger activities of the financial institutions in China during the first half of the year.

The gross profit margin, though pressurized downward a bit because of the effect of the current scale, was maintained at an acceptable level.

We achieved certain results in cost control. The sales and administrative costs decreased by HK\$7.73 million as compared to the corresponding period of last year. Nevertheless, owing to a decline in turnover and gross profit, this business segment still recorded a loss of HK\$18.50 million.

The management realised that this was only a price which the Company had to pay for its business model transformation and for establishing its long-term status in the industry. In terms of its industry status, the consultancy and IT services, which was the Group's core business under its reorganisation program, maintained the top market share in China. The Group is the only domestic company which possesses the development and application solutions based on the IBM mainframes. In China, the Group's new generation core banking system, international credit card system consultancy services and financial business operation consultancy business are at a leading position. The reorganisation and integration program carried out in the past will lead to a highly efficient and beneficial operation of this business unit, spin-off of the non-core staff, and a shift towards long-term cooperation with cooperation partners. Besides optimisation of the Company's operating system, the spin-off of the personnel was carried out properly in an orderly way and without causing any loss to customers.

Electronic payment solutions and products

This business segment recorded a turnover of HK\$40.12 million (2003 interim: HK\$22.06 million) and a profit of HK\$3.97 million (2003 interim: a loss of HK\$2.73 million). The overall gross profit margin was 34%, representing a slight drop of 5% as compared with the corresponding period of last year.

Following the profit generated last year, although the period under review was a traditionally slack period, the PAX brand name can still generate a reasonable profit contribution. This was mainly attributed to a relatively significant sales increase in the China domestic market and the robust trend of growth of the PAX brand name in the international market. As compared with the first half of the previous year, the market of this year was free from any impact of any special factors (e.g. the outbreak of SARS in the previous year) which might pose a drag upon the performance of contracts. To control the operating costs,

certain procedures were adopted including a further optimisation of corporate management and an intensification of internal control systems and the financial costs were successfully reduced in tandem with a strengthening of the cashflow management.

Currently, PAX has already become a leading supplier in the EFT-POS terminal market in China. In the first half of 2004, PAX's market share of ChinaUnionPay increased to 30%, and its share in the China market increased to 25%. Undoubtedly, following the rapid development of ChinaUnionPay, the market position of PAX in the mainland China market will further be strengthened. In the meantime, PAX also had obvious advantages to compete in the EFT-POS terminal market in Southeast Asia. The PAX brand name has won extensive recognition from customers, including international prestigious banks, such as The Hongkong and Shanghai Banking Corporation Limited, Bank of China (Hong Kong) Limited, Citibank N.A., Standard Chartered Bank and United Overseas Bank Limited, which have already become the important clients of PAX. Besides the abovementioned countries and areas, PAX also developed its own cooperation partners in countries like Indonesia, India and Nigeria. It is envisaged that PAX will make a development breakthrough in these markets in the near future. With the lapse of time and by leveraging on the opportunity and momentum offered by the shift towards Europay Mastercard Visa ("EMV") standards, a further strengthening of the advantages of PAX is certain and an opportunity is looming for its rapid development outside the mainland China market.

Regarding the research and development of new products, PAX has launched the following new products:

1. P60-S1 detachable EFT-POS terminal
2. MP51-C desk-top wireless EFT-POS terminal

Regarding the development of new markets, PAX has successfully obtained orders from the following customers in Hong Kong:

1. The Hongkong and Shanghai Banking Corporation Limited
2. Bank of China (Hong Kong) Limited
3. Citibank N.A.
4. Wing Hang Bank Limited
5. International Bank of Asia Limited
6. United Overseas Bank Limited

During the period under review and up to now, PAX obtained the following product certification:

1. Security Evaluation on PAX's P60-S1 POS Terminal (15th March 2004)
2. ChinaUnionPay Hong Kong Front-end System Direct Link to POS network integration Test Certificate (P70-S P60-S1) (26th March 2004)

3. P60-S1 3C Certification (26th April 2004)
4. P60-S1 Bank Magnetic Stripe Card Outlets Terminal Products network integration Permit (27th May 2004)
5. P70-T 3C Certification (23rd June 2004)
6. P70-T Bank Magnetic Stripe Card Outlets Terminal Products network integration Permit (12th July 2004)
7. P60-S1 EMV Level 1 (19th July 2004)
8. P60-S1 EMV Level 2 (20th July 2004)
9. P60-S1 Tax Control Function Test (9th August 2004)

Telecommunication solutions, services and related products

During the period under review, a turnover of HK\$5.87 million (2003 interim: HK\$10.52 million) and a loss of HK\$7.08 million (2003 interim: a loss of HK\$1.16 million) were recorded.

During the period under review, there was a decline of approximately HK\$8.03 million in the turnover from traditional system integration services, while the new Interactive Voice Response (“IVR”) value-added business generated a turnover contribution of HK\$3.38 million for this segment. As mentioned in the management discussion and analysis of last year, this business segment was gradually developing towards high margin value-added services and withdrawing from low margin business and product lines. Despite a turnover decline, there was an increase in the gross profit margin of system integration services. Owing to the seasonal factors in China, the completion of the major contracts of traditional system integration services will be completed in the second half of the year and the management believes that the integrated business will eventually generate benefits.

IVR business, which is still in its initial stage of development, has made a fairly good contribution to the turnover during the period under review. It is envisaged that the business, though it was still in the red during the period under review, will enjoy good prospects of growth in the future and will become a profit contributor to the Group. This business unit is the only networkwise IVR operator for China Mobile. The Company was undergoing a transformation from a traditional system integrator to a value-added services provider. Its successful bid for a Satellite Communication Company’s (衛通) Fee Calculation and Settlement System demonstrates its expansion and enhancement in the core telecommunication business. Slashing the low margin production lines and downsizing the personnel and scale of system integration business unit brought about a corresponding reduction in the costs of this segment. The overall increase of the costs of this segment was mainly due to the front-end development and operation costs of the new IVR business.

PROSPECTS

Finance

The finance industry in China, including banking, insurance and securities industry, is ripe for a new round of reform. The financial institutions in China are on its way to reforming their core business services. In addition to deepening their core business capabilities, they are turning their increasing attention to the need to outsource their IT infrastructure buildup and services to concentrate on upgrading and improving their core businesses. To capitalise on this development trend and opportunities, the Group's financial business segment is gearing up and has mobilised a considerable amount of resources, including:

- 1) strengthening of the expertise lineup of the business consultancy capabilities by employing a number of overseas experts;
- 2) commencing application management service ("AMS") on a trial basis; meeting outsourcing related international standards; obtaining certification for its core engineering work; implementing a technology and skilled personnel reserve program; and utilising AMS as a means for providing outsourcing services nationwide; and
- 3) cooperating with experienced multinational IT service providers, to work on large-scale outsourcing projects.

Telecommunication

On the basis of cooperation with China Mobile, after years of accumulation and through future involvement, the telecommunication business unit will certainly occupy a leading position in China in terms of IVR platform outsourcing services and wireless value-added services.

The research and development of the fixed-line ring tone was completed early this year, and the products have been launched onto the market. Currently, the Group focuses its efforts on the OEM of UTstarcom Telecom's project and the Netcom's ring tone project. Ring tone is an important component of the development of telecommunication value-added services. On the ring tone platform, we may continue to develop businesses such as sound tone and voice tone. At the same time, we are also discussing the cooperation of OEM of ring tone with UTstarcom Telecom, an attempt to develop into the field of the application software outsourcing.

In respect of development planning, the transformation from a traditional system integrator into a service provider and the strategy of shifting to the value-added business oriented telecommunication business will become the development direction for the years to come. We anticipate that China Mobile will record a significant increase in voice value-added business, and the market capacity for the entire year will amount to hundreds of millions of dollars, and the speed of growth will even be higher in the future.

Electronic payment terminals

As far as this business segment is concerned, 2004 is a year in which it continues its steady growth in the mainland market. It is expected that the total capacity of the market will increase by more than 30%, and that the rate of growth may even be higher in the several years leading to the Beijing Olympics 2008 coupled with the development of finance sector.

It is our aim in this industry to develop new products which meets market demand, to improve the quality of products on a continual basis, to provide quality technical support and after sales services to customers, to raise the prestige and recognition of our brands, and to research and develop new products with higher profit margin. As to the China market, the opportunities and challenges we have been encountered are the market development opportunities arising from the Beijing Olympics 2008 and Shanghai Expo 2010. In particular, the rapid development of ChinaUnionPay has provided both a solid foundation for further developing the EFT-POS market and the momentum of growth. In respect of the international market, the global trend for the migration to EMV will certainly provide a valuable development opportunity for EFT-POS manufacturers. PAX will continue utilising the experiences it has accumulated in the EMV drive to secure new markets and customers through its excellent price performance ratio, stable product performance and quality, and outstanding technical support services.

We plan to launch a series of new products within the first half of next year. The new generation of EFT-POS terminals display the most advanced features in the industry worldwide. It will provide customers with an even better prices performance ratio, and will earn us higher gross profit margin. It will be a powerful weapon for PAX to penetrate the markets in Japan, Europe and America, and it will also become an important profit contributor to the Group.

The efforts spent in the enhancement of consultancy capabilities, the development of value added services and the research and development of solutions and products have consumed the most of the Group's resources and contributed to the underperformance as reflected in the results for the period under review. Nevertheless, the Group is confident that we are on the right track towards being the premier provider of IT consulting, outsourcing and technology services and products.

Looking ahead, given the solid foundation laid and the prosperous market development, we are confident that the Group will generate significant result improvement in the rest of the year.

Liquidity and financial resources

As at 30th June 2004, the Group recorded a total assets of HK\$151.73 million, which were financed by liabilities of HK\$119.16 million and equity of HK\$32.57 million. The net assets value is HK\$32.57 million (31st December 2003: HK\$60.76 million). It amounted to HK\$0.10 per share as compared to HK\$0.18 per share as at 31st December 2003.

As at 30th June 2004, the Group had cash of HK\$15.65 million and bank borrowings of HK\$2.37 million. The net cash position as at that date was HK\$13.28 million as compared to HK\$18.04 million as at 31st December 2003. All the borrowings are short-term loans and overdrafts utilised to fund the Group's working capital requirements. The gearing ratio (defined as total interest bearing debts divided by shareholders' equity) was 0.07 compared to 0.40 as at 31st December 2003. The gearing ratio is considered healthy and suitable for the continued growth of the Group's business.

Capital structure and details of charges

The Group's bank borrowings are short term loans and overdrafts with interests charged at floating rates. As at 30th June 2004, bank loans amounting to Renminbi 2.15 million (equivalent to HK\$2.01 million) are denominated in Renminbi with average interest rates of 5.31% per annum. Bank overdrafts amounted to HK\$0.36 million is denominated in Hong Kong dollar. The Hong Kong dollar bank overdrafts was charged at Hong Kong Prime Lending Rate.

Approximately HK\$8.65 million, HK\$2.34 million and HK\$4.66 million of the Group's cash balances are denominated in Renminbi, Hong Kong dollar and US dollar respectively.

The bank loans were secured by deposits in bank guaranteed funds of HK\$4.37 million and a personal guarantee of HK\$7 million from a director of the Company and corporate guarantee of HK\$30 million of the Company.

Exposure to fluctuations in exchange rates and related hedges

The Group derives its revenue, makes purchases and incurs expenses denominated mainly in US dollar, Renminbi and Hong Kong dollar. Currently, the Group has not entered into agreements or purchased instruments to hedge the Group's exchange rate risks. Any material fluctuation in the exchange rates of Hong Kong dollars or Renminbi may have an impact on the operating results of the Group.

Contingent liabilities

The Group had no contingent liability as at 30th June 2004.

Employees

The total number of employees of the Group as at 30th June 2004 was 559. The breakdown of employees by division is as follows:–

Financial solutions, services and related products	308
Electronic payment solutions and products	70
Telecommunication solutions, services and related products	77
IVR operation	87
Corporate office	17
	<hr style="border-top: 1px solid black;"/>
	559

The Group ensures that its remuneration packages are comprehensive and competitive. Employees are remunerated with a fixed monthly income plus annual performance related bonuses. The Group also sponsors selected employees to attend external training courses that suit the needs of the Group's businesses.

Share options

To provide further incentive to motivate talented employees, the Company adopted a share option scheme in November 2001 ("Scheme"). On 18th March 2004, 33,000,000 share options were granted to Directors and employees at HK\$0.374 (the average closing price of the shares as quoted in the daily quotations sheets issued by The Stock Exchange of Hong Kong Limited for the five business days immediately preceding 18th March 2004) with an expiry date of 17th March 2014. The details term of the Scheme were disclosed in the 2003 annual report and the movements in the Company's share options during the period will be disclosed in the 2004 interim report.

INTERIM DIVIDEND

The Directors do not recommend the payment of interim dividend for the period (2003: Nil).

COMPLIANCE WITH THE CODE OF BEST PRACTICE OF THE LISTING RULES

Throughout the period, the Company was in compliance with the Code of Best Practice as set out in Appendix 14 of the Listing Rules of The Stock Exchange of Hong Kong Limited, except that the independent non-executive directors of the Company are not appointed for specific terms, but are subject to retirement by rotation pursuant to the Company's bye-laws.

PURCHASE, SALE OR REDEMPTION OF SHARES

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

AUDIT COMMITTEE

The Audit Committee, which comprises two independent non-executive directors of the Company, has reviewed with management the accounting principles and practices adopted by the Group and discussed internal controls and financial reporting matters including a review of the unaudited condensed accounts for the six months ended 30th June 2004 with the directors.

PUBLICATION OF INTERIM REPORT

The 2004 Interim Report containing all the information required by paragraphs 46(1) to 46(6) of Appendix 16 to the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited will be submitted for publication on the website of The Stock Exchange of Hong Kong Limited in due course.

By Order of the Board

Li Wenjin

Executive Director

Hong Kong, 22nd September 2004

As at the date of this announcement, the Board is comprised of nine executive directors, namely, Cheung Yuk Fung, Kui Man Chun, Lo Siu Yu, Xu Wensheng, Li Wenjin, Chan Yiu Kwong, Su Terry Lumin, Xu Chang Jun and Zhou Jian and two independent non-executive directors namely Tam Chun Fai and Xu Sitao.

“Please also refer to the published version of this announcement in The Standard.”