Xteam Software International Limited
衡浪平台軟件國際有限公司

(incorporated in the Cayman Islands with limited liability)

ANNUAL RESULTS ANNOUNCEMENT FOR THE YEAR ENDED 31 MARCH 2003

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

CHAIRMAN'S STATEMENT

STRIVING FOR A STRONGER XTEAM

The past year has seen a slowdown in information technology spending in the People's Republic of China (the "PRC") market, as a result of conservative spending by both the corporate sector and individuals. But despite slower short-term growth in IT spending in the PRC, Xteam Software International Limited (the "Company") and its subsidiaries (the "Group") see great potential in the PRC market in the years to come. Apart from taking measures to restructure inefficient and loss-making operations of the Group, we will continue to draw on our strengths and achieve long-term business growth despite unfavorable market conditions. The Group's turnover for the year ending 31 March 2003 was HK$26,694,000, an increase of 22.2% compared with a year ago. But the cost of sales and services for hardware products and products targeting the infrastructure market also increased. As a result, the Group recorded a net loss of HK$10,589,000, compared with a profit of HK$3,478,000 in 2002. The net assets of the Group as of 31 March 2003 has increased significantly to HK$48,504,000, compared with HK$35,560,000 and HK$9,603,000 for the year/period ending 31 March 2002 and 31 March 2001 respectively.

The Group understands that it is involved in a highly competitive market. During the past year, the Group continued to commit financial and technical resources in its horizontal expansion and to further increase its market share.

2002/2003 – RIDING THE STORM

BUSINESS REVIEW

The 2002/2003 year was an exciting yet challenging one for the Group. It was not a smooth road to prosperity. We lost one of our major customers as a result of its internal management reshuffle. To make up for the loss in sales, we have lowered our gross margins on products to attract new customers. As a result, despite an increase in total turnover, gross profit margins dropped significantly from 87.5% to 33.6% during the year. The substantial decrease was also attributed to lower gross profit margins in the distribution of third parties' software and the sale of the hardware products bundled with software.

STRATEGIC POSITIONING

During the past year, the Group completed the acquisition of 69% of the issued share capital of Snow Fair Co., Ltd. ("Snow Fair"). Snow Fair is the holding company that has a controlling interest in Shanghai Pantosoft Co., Ltd. ("Shanghai Pantosoft") the leading vendor in Shanghai's education software market. Pantosoft was established in Shanghai with products and services targeting the education sector. The PRC government is committed to digitalizing all of its 700,000 schools, and the Group will play a major role in meeting the needs of software growth in education. The strategic acquisition of Shanghai Pantosoft enables us not only to have a presence in a strategic location;

more importantly, it allows the Group to expand vertically into the education sector and establish a strong foothold in the Shanghai market.

To take full advantage of our expansion into eastern China, the Group will consolidate our position in the server application software market in Shanghai. There will be a negative short-term impact, because it takes time for the Group to reap extra benefits from the acquisition of Shanghai Pantosoft. These include synergies of the Group's research and development efforts, and the rationalization of distribution networks and resources. In short, the acquisition represents a promising long-term investment that will further strengthen our position in the Chinese Linux market in the PRC.

TECHNOLOGY AND PRODUCT BRIEFING

The Group has also identified the potential in the small and medium enterprises ("SMEs") market. The PRC's accession to the World Trade Organization ("WTO") has accelerated the conversion of Chinese companies into electronic-driven enterprises, as well as their readiness for globalization. The strong demand for software and server solutions, especially from the SME market, goes hand-in-hand with the Group's strength in providing flexible and customized solutions.

PRODUCT INNOVATION

Our creativity and the ability to develop new products tailored to the demands of SMEs are reasons behind the Group's strong position in the Linux open source market. The software XteamServer 4.0 d-class, a new product that illustrates the Group's key strength in server application, was launched at the end of 2002. This new server application product targeting SMEs has acquired a significant market share and received the "Editor's Choice" Award in January 2003 from China Information World, one of the leading IT publications in the PRC. The award was jointly run by the Ministry of Information Industry and China Center of Information Industry Development ("CCID"), recognizing the Group's outstanding IT products and software specifically developed for the PRC market.

The Group's Chinese Linux products have continued to gain strong brand recognition in the market. Besides, during the period under review, the Group received "The Best Linux Product Award" from CCID under the Ministry of Information Industry, in recognition of its efforts to provide professional products and services to customers.

To continue to strengthen our leadership position in the PRC Linux market, the Group has developed a wide array of Linux-based e-government applications. They have been well received and adopted by government divisions in several cities in the PRC. In recognition of its leading role in promoting e-government applications in the PRC market, the Group was selected as one of the "Top 100 E-government IT Enterprises in China"(中國電子政務100強) by China Internet Weekly in October 2002.

In our continuous strive for product excellence, China Computer Journal also voted us the 'Best Computer Software Product' for the year 2002.

EMPHASIS ON QUALITY

The Group takes pride in its commitment to the quality of our products. We believe our quality exceeds our customers' expectations, which will help lead to future business growth. In 2002, our Shanghai office was awarded ISO 9001 certification recognizing our efforts in delivering quality products.

SALES AND SUPPORT SERVICES

WORRY-FREE SERVICES

We realize the importance of the trust that is placed behind each sales order. To cherish the trust that our customers have been giving us, we have established two sales and support offices, in addition to our full offices in Beijing and Shanghai. These cities include Guangzhou and Qingdao to provide our customers with the best attention and services.

FOSTERING NEW CUSTOMER RELATIONSHIPS

In the past year, the Group has enhanced its business ties with the government sector as well as with various industry leaders. These include the Beijing Municipal Government, The China Construction Bank, COSCO and IBM. Cementing close business relationships and establishing brand loyalty are by far more important than the face value of the contracts.

LOOKING AHEAD

The Group has the vision to provide innovative solutions, superior service, and customer satisfaction. This is through the Group's technical expertise in Linux, its vertical and horizontal expansions in the PRC's software market, and its commitment in realizing the potential of the vast PRC market.

Businesses on the mainland have been severely affected by the outbreak of Severe Acute Respiratory Syndrome ("SARS") in several cities. SARS will have a negative impact on the Group's operations and financial position, because its major operations are in Beijing. The day-to-day running of the Group, such as business meetings and operations, has been affected. But the Group is so far unable to quantify the impact of SARS on its operations and financial performance. We anticipate it will be reflected in the results in the next quarter.

Looking ahead, the Group will seek to accelerate its rate of growth and expansion by capitalizing on the opportunities in the Chinese Linux market. According to forecast by the International Data Corporation, server sales worldwide will grow by an average of 3% annually, and the market will be worth US$63.4 billion in 2006. Linux-based server operating systems are expected to be major market drivers, and sales are projected to reach US$6.5 billion in 2006.

The education sector in PRC, which accounted for 13.3% of the mainland PC market in the first half of 2002, will see a surge in PC demand because the PRC government is committed to digitalizing education. Shanghai will be leading the way and it will be crucial to the popularity of Linux in the country, according to CCID reports. The Group will penetrate the market through the presence of Shanghai Pantosoft.

WORD OF APPRECIATION

Last but not least, I would like to take this opportunity to thank our staff and fellow directors for their hard work in the past year. We are all striving for a common goal: to make our company a leading Linux player in the PRC.

MANAGEMENT DISCUSSION AND ANALYSIS

FINANCIAL RESULTS FOR THE YEAR ENDED 31 MARCH 2003

The Group report a consolidated turnover of approximately HK$26.7 million for the year ended 31 March 2003, representing an increase of approximately 22.5% over last year (2002: HK$21.8 million). The increase in turnover was mainly resulted from sales of lower gross margins products in attracting new customers.

Loss attributable to shareholders for year ended 31 March 2003 was approximately HK$10.6 million (2002: profit of HK$3.5 million). The turning over from a net profit in the last period to a net loss for the year ended 31 March 2003 was mainly attributable to the increase of cost of sales and services amounting to approximately HK$17.7 million and the increase in general and administrative expenses in particular due to a provision of approximately HK$3 million over estimated value added tax refundable. The increase in cost of sales and services are mainly caused by the increase by in volume of sales of thin margin products.

LIQUIDITY, FINANCIAL RESOURCES AND DEBT RATIO

As at 31 March 2003, the Group has an unsecured outstanding bank loan of approximately HK$1,415,000 (2002: Nil).

The gearing ratio (defined as total liabilities over equity) of the Group as at 31 March 2003 was approximately 39.1% (2002: 34.8%).

The debt ratio (defined as total liabilities over total assets) of the Group as at 31 March 2003 was approximately 28.1% (2002: 25.8%).

CAPITAL STRUCTURE, EXPOSURE TO EXCHANGE RATES FLUCTUATION

As at 31 March 2003, the Group held cash and cash equivalents denominated in Hong Kong Dollars and Renminbi.

Substantially all of the revenue-generating operations of the Group are transacted in Renminbi, which is not freely convertible into foreign currencies. The Group had prudent policy to manage currency and interest rate exposures, and as most of the Group's monetary assets and liabilities are denominated in Renminbi and Hong Kong Dollars, the exchange rate risks of the Group is considered minimal.

FINANCIAL INSTRUMENTS

The carrying amounts of the Group's cash and cash equivalents, trade receivables and payable, other receivables and payables, approximately their fair values because of the short maturity of these instruments.

The Group did not enter into any foreign exchange forward contracts to hedge against fluctuations.

MATERIAL ACQUISITIONS AND DISPOSALS DURING THE YEAR AND FUTURE PLANS FOR MATERIAL INVESTMENTS

During the year, the Group acquired 69% interest in Snow Fair Co., Ltd. ("Snow Fair") for a consideration of approximately HK$15.5 million (approximately HK$13.7 million in cash and approximately HK$1.8 million fair value of the ordinary shares of the Company). Snow Fair is an investment holding company whose sole asset comprises a 51% shareholding interest in Pantosoft International Limited, which in turns holds the entire equity interest in Shanghai Pantosoft Co., Ltd. ("Shanghai Pantosoft"). Shanghai Pantosoft is a company established in the PRC which is principally engaged in the development of education software as well as digital campus in the PRC.

SEGMENTAL INFORMATION

No analysis of the Group's turnover and its contribution to profit before taxation by principal activities for the year were presented all the Group's turnover and operating results were arising from the sales of computer software and rendering of software development and related services in PRC.

STAFF

As at 31 March 2003, the Group employed 112 employees (2002: 55), including directors of the Company, at market remuneration and benefits such as defined retirement/pension contributions, employee share options and medical insurance, etc. Total staff costs for the reported year were approximately HK$7.1 million (2002: approximately HK$5.3 million).

CHARGE OF ASSETS

As at 31 March 2003, the Group did not have any charge on its assets (2002: Nil).

CONTINGENT LIABILITIES

As at 31 March 2003, the Group did not have any material contingent liabilities (2002: Nil).

DIVIDENDS

The Directors do not recommend the payment of a final dividend for the year ended 31 March 2003 (2002: Nil).

COMPARISON OF USE OF PROCEEDS

The net proceeds raised from the placing on 11 December 2001 were approximately HK$18.96 million (based on HK$0.38 placing price). The proceeds had been applied to achieve the business objectives as set out in the prospectus dated 30 November 2001 and are detailed below:

	Use of proceeds as stated in the prospectus *HK$' million*	**Actual amount utilized up to 31 March 2003** *HK$' million*
For product development or related investment through, among other things, acquisition, direct or indirect investment in other Linux based product developers	6.37	5.37
For enhancement of the Group's distribution channels through, among other things, acquisition, direct or indirect investment in other distributors	2.00	2.00
For setting up of a laboratory for e-solution project in Beijing, the PRC	2.50	2.50
For setting up Linux Training and Certificate Programme in Beijing, the PRC	1.00	1.00
For setting up the Group's Shanghai sales office	1.50	1.50
For advertising and marketing activities of the Group to promote the brand awareness and products of the Group	3.07	2.87
General working capital	0.80	0.60
Placed with banks	0.00	3.12

Unused net proceeds of approximately HK$3.12 million were placed with licenced banks in Hong Kong and PRC, and would be used to achieve objectives as stated in the prospectus.

REVIEW OF BUSINESS OBJECTIVES

Objectives up to 31 March 2003 as stated in the prospectus dated 30 November 2001	Actual business progress up to 31 March 2003
Product launches, sales and marketing	
• Continue to launch additional series of XteamServer and solutions to cover more sectors	The Group continues to expand XteamServer series
• Continue to co-operate with the hardware vendors and distributors to deploy more embedded systems	The Group is working with hardware vendors and distributors to deploy more embedded systems
• Improve e-solution through strengthening its collaboration with software vendors and distributors	The Group is working with software vendors and distributors to provide e-solutions
• Expand its sales and distribution channels	The Group had improved sales and distribution channels
• Establish a second subsidiary to promote the Group's sales	The Group has successfully acquired a software company in Shanghai which can also assist to promote the Group's sales
• Launch upgraded XteamServer series	In progress
Business development	
• Develop a program for applications development and marketing	In progress
• Explore opportunities to set up consulting business	In progress
• Improve support services and explore opportunities to provide enterprise consulting services	In progress
• Establish Xteam Companion which is based on Internet sales and service consultancy business to provide tailor-made all-round support to sales network and end-users	In progress

Objectives up to 31 March 2003 as stated in the prospectus dated 30 November 2001	Actual business progress up to 31 March 2003
Research and development	
• Continue research and development for embedded system and e-solution	In progress
• Upgrade XteamServer series	In progress
Human resources, operations and administration	
• Recruit additional development engineers	The Group will access the Group's development strategy from time to time in order to meet the human resources requirement
• Strengthen the Group's support services and start to provide enterprise consulting services	The Group will access the Group's development strategy from time to time in order to meet the human resources requirement
Strategic acquisitions and alliances	
• Explore opportunities to acquire or form alliances with companies providing synergies and technological support	The Group has successfully acquired a software company in Shanghai which can also provide certain technological support. In addition, the Group is still continuing to explore opportunities to acquire or form alliances with companies providing synergies and technological support

AUDITED CONSOLIDATED RESULTS 2003

The audited consolidated results of the Group for the year ended 31 March 2003, together with comparative figures for the year ended 31 March 2002 are as follows:

	Note	**2003** *HK$'000*	2002 *HK$'000*
Turnover	*2*	**26,694**	21,835
Cost of sales and services		**(17,730)**	(2,734)
Gross profit		**8,964**	19,101
Other revenue	*2*	**542**	159
Selling and marketing expenses		**(4,035)**	(1,978)
General and administrative expenses		**(10,371)**	(7,468)
Research and development costs		**(5,227)**	(6,100)
(Loss)/profit from operating activities	*3*	**(10,127)**	3,714
Finance costs		**(200)**	(236)
(Loss)/profit before taxation		**(10,327)**	3,478
Taxation	*4*	**(117)**	–
(Loss)/profit for the year		**(10,444)**	3,478
Minority interests		**(145)**	–
(Loss)/profit attributable to shareholders	*5*	**(10,589)**	3,478
(Loss)/earnings per share	*6*		
– Basic		**(1.84 cents)**	0.72 cent
– Diluted		**(1.75 cents)**	0.68 cent

Notes:

1. **Corporate information**

The Company was incorporated in the Cayman Islands on 24 May 2001 as an exempted company with limited liability under the Companies Law (2001 Second Revision) of the Cayman Islands. The shares of the Company have been listed on the Growth Enterprise Market ("GEM") of The Stock Exchange of Hong Kong Limited ("Stock Exchange") since 11 December 2001.

During the year, the Group acquired 69% interest in Snow Fair Co., Ltd. ("Snow Fair") for a consideration of approximately HK$15.5 million (approximately HK$13.7 million in cash and approximately HK$1.8 million fair value of the ordinary shares of the Company). Snow Fair is an investment holding company whose sole asset comprises a 51% shareholding interest in Pantosoft International Limited, which in turns holds the entire equity interest in Shanghai Pantosoft Co., Ltd. ("Shanghai Pantosoft"). Shanghai Pantosoft is a company established in the PRC which is principally engaged in the development of education software as well as digital campus in the PRC.

During the year, the Group was principally engaged in software development and provision of the Chinese Linux operating system with kernel rewritten to cater for Chinese users and software based on the Linux operating platform for various hardware appliances including servers and personal computers in the PRC. It also provided technical support and after-sales services to its customers.

2. **Revenue and turnover**

Revenue recognised during the year are as follows:–

	2003	2002
	HK$'000	*HK$'000*
Turnover		
Sales of computer software	**21,596**	21,605
Income from provision of system integration and related services	**4,500**	–
Provision of software development and related services	**598**	230
	26,694	21,835
Other revenue		
Bank interest income	**138**	119
Sundry income	**404**	40
	542	159
	27,236	21,994

3. (Loss)/profit from operating activities

(Loss)/profit from operating activities is arrived at after charging:

	2003	2002
	HK$'000	*HK$'000*
Amortisation of goodwill	**253**	–
Amortisation of intangible assets	**4,625**	2,702
Auditors' remuneration	**400**	335
Bad and doubtful debts (recovery)	**44**	(1,126)
Depreciation of fixed assets	**485**	452
Loss on disposal of fixed assets	**–**	168
Operating lease rentals in respect of land and buildings	**1,406**	1,508
Staff costs:		
Wages and salaries (including directors' emoluments)	**6,789**	4,690
Contributions to retirement/pension schemes and other benefits	**309**	578

4. Taxation

The amount of taxation in the consolidation income statement represents:

	2003	2002
	HK$'000	*HK$'000*
Hong Kong profit tax *(Note (a))*	–	–
Overseas taxation *(Note (b))*	**117**	–
	117	–

(a) No provision for profits tax has been made as no income was earned or derived from Hong Kong during the year.

(b) No provision for profits tax has been provided in respect of the Cayman Islands or the British Virgin Islands as there were no assessable profits for the year in those jurisdictions. Overseas taxation represented tax charges on the assessable profits of certain subsidiaries operating in the PRC calculated at the applicable rates.

(c) No provision for deferred tax has been made as the Group and overall deferred tax benefits which will be recognised when realisation of such benefit is assured beyond reasonable doubt.

5. Loss for the year attributable to shareholders

The net loss attributable to shareholders dealt with in the financial statements of the Company amounted to HK$2,670,000 (2002: HK$1,156,000).

6. (Loss)/earnings per share

The basic (loss)/earnings per share is calculated based on the Group's (loss)/earnings attributable to shareholders of HK$10,589,000 (2002: profit of HK$3,478,000) and on the weighted average of 574,075,967 (2002: 481,335,823) ordinary shares in issue during the year.

The diluted earnings per share is based on 604,696,820 (2002: 481,335,823) ordinary shares which is the weighted average number of ordinary shares in issue during the year plus the weighed average of 30,620,853 (2002: 28,561,411) ordinary shares deemed to be issued if all outstanding options had been exercised at the date they were granted.

7. Movements of reserves

	Share premium account	Exchange reserves	Accumulated losses	Total
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*
Group				
1 April 2001	10,867	–	(9,672)	1,195
Share issued on the Reorganisation	8,397	–	–	8,397
Issue of new shares	31,791	–	–	31,791
Share issue expenses	(10,337)	–	–	(10,337)
Capitalisation issue	(4,470)	–	–	(4,470)
Exchange adjustments arising on consolidation	–	3	–	3
Transfer to profit and loss account	–	(3)	3	–
Profit for the year	–	–	3,478	3,478
31 March 2002	36,248	–	(6,191)	30,057
1 April 2002	36,248	–	(6,191)	30,057
Issue of new shares	23,499	–	–	23,499
Adjustment on over estimated share issue expense	1,058	–	–	1,058
Share issue expenses	(1,404)	–	–	(1,404)
Loss for the year	–	–	(10,589)	(10,589)
31 March 2003	59,401	–	(16,780)	42,621

	Share premium account *HK$'000*	Exchange reserves *HK$'000*	Accumulated losses *HK$'000*	Total *HK$'000*
Company				
Issue of new shares	31,791	–	–	31,791
Share swap	3,927	–	–	3,927
Share issue expenses	(10,337)	–	–	(10,337)
Loss for the year	–	–	(1,156)	(1,156)
31 March 2002	25,381	–	(1,156)	24,225
1 April 2002	25,381	–	(1,156)	24,225
Issue of new shares	23,499	–	–	23,499
Adjustment on over estimated share issue expense	1,058	–	–	1,058
Share issue expenses	(1,404)	–	–	(1,404)
Loss for the year	–	–	(2,670)	(2,670)
31 March 2003	48,534	–	(3,826)	44,708

Distributable reserves of the Company at 31 March 2003, determined in accordance with section 34 of the Companies law (2001 Second Revision) of the Cayman Island, amounted to approximately HK$44.7 million (2002: HK$24.2 million)

COMPLIANCE WITH THE BOARD PRACTICES AND PROCEDURES

In the opinion of the Directors, the Company has complied with the "Board Practices and Procedures" as set out in Rules 5.28 to 5.39 of the GEM Listing Rules of the Stock Exchange.

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

Up to 31 March 2003, neither the Company nor any of its subsidiaries purchased, sold or redeemed any of the Company's securities.

AUDIT COMMITTEE

As required by Rules 5.23 of the GEM Listing Rules, the Company has established an audit committee on 21 November 2001 with written terms of reference which deal with its authority and duties. The audit committee's principal duties are the review and supervision of the Company's financial reporting process and internal control systems. The audit committee comprises of the two independent non-executive Directors, namely Mr. Cheng Shu Wing and Mr. Wang Shi Yu.

During the year, the Committee has held four meetings to review the financial statements, quarterly reports, interim report and annual report of the Company.

On behalf of the Board,
Mak To Wai
Director

Hong Kong, 26 June 2003

This announcement will remain on the GEM website at www.hkgem.com on the "Latest Company Announcements" page for at least 7 days from the date of its publication.