

CEO's Newsletter

September 2006

Dear Shareholder,

This has been a busy month with a very hectic visit to the Far East and the interim results to finalise. Because the interim report gives a fairly detailed breakdown of the current state of the company, this month's CEO letter is somewhat shorter than the norm. Nonetheless, I do want to take the chance to brief you on some of the developments that have arisen from our Asian trip. The visit to the Far East undertaken by me and Paul Barwick, our sales Director, was one of the best we have had. It's very clear, both that Cyan is maturing in the marketplace, and that our extended product range is exciting considerable interest. The Japanese leg was to negotiate with a large local distributor, but the other locations were all end-customer focused. We expect good news to come from this visit in the future and will inform you as and when things happen.

China Customer - Tax Control ePOS

All the investigations we have made indicate that this market is real and very big. We are in discussions with several licensed manufacturers and we get the same information from all of them. They all say that the roll out of tax control terminals to retailers is stalled for the time being. Meanwhile, according to our customer, the central tax office IT systems are all complete and working and indeed are used when manufacturers compliance test their products. We have also confirmed through other independent sources that January 2005 was to be the start of the roll out, although not to all provinces at once. This fits with our existing customer's original planned production ramp up starting last year. So it does seem to stack up, that the only hold up is the government pushing the button.

As it happens our customer has not been sitting back and doing nothing. He has used the time to change his business model to be primarily a supplier to others, thereby increasing his overall market share potential. Our customer is very close to the market having already secured, according to him, 20% market share of ePOS terminals in China. Equally importantly, he has developed an extended product range, in which all the new products incorporate Cyan microcontrollers, installed extensive domestic Chinese production capacity and provides after sales service and support for his existing line of non tax control ePOS terminals. In contrast, he believes that his competitors have yet to leave the starting gate in most of these key areas. In consequence, our customer is convinced that he will at the very least hold on to the 20% market share he currently enjoys with the potential to grow this substantially. Having seen the production capacity at first hand and met with the people running the business, who have a proven and successful track record in this market having supplied over one million ePOS terminals to European brand names, we remain convinced that we have a first class partner for this exciting market opportunity.

While the delay in roll out is frustrating, both to us, and I'm sure to you, it is clear that delay is causing the government to lose substantial tax revenues. Given the general environment and the difficulty in ensuring tax compliance, the government has to mandate the installation of the terminal, but also to encourage retail transactions to take place through these tax control terminals; the government has taken active steps to encourage customers to ask for a till receipt and thereby ensure that the transaction goes through the till. This has been achieved by issuing the customer with a free government lottery scratch card along with his till receipt! We have seen this in action. Having placed reform of its fiscal infrastructure high on its list of priorities and with official government spending of 27.4% of GDP relative to the OECD average of 44.5% (OECD study : Challenges for China's Public Spending, published 14/02/06) , the government certainly have the incentive to move forward sooner rather than later.

Sales Metrics

We chart the number of people registering and downloading our tools as this bears a resemblance to the number of design wins we have or can expect. You will notice that in August we broke through 3,000 registrations. Currently the design wins we have would represent almost **2 million** units per annum if they were all in full production at the same time. If we converted all opportunities to design wins and then production they would represent an additional **19.5 million** units per annum.

Cumulative Website Registrations - Jan 04 to Aug 06

