

On behalf of the Board of Directors (the "Board"), I am pleased to present the annual report of Sunway International Holdings Limited (the "Company") and its subsidiaries (collectively the "Group") for the year ended 30 September 2000.

BUSINESS REVIEW

Review of Operation and Results

The Group recorded a consolidated turnover of HK\$1,094.3 million, representing a slight decrease of approximately 7.2% over the previous year. Sales of the major products out of the Group's turnover in 2000 were 48% for electronic calculators, 17% for quartz crystals, 12% for watch movements, 9% for liquid crystal displays ("LCDs") and 4% for electronic watches and clocks. The People's Republic of China ("PRC") and Hong Kong markets contributed approximately 72% and 25%, respectively of the Group's total turnover in the year, playing a consistent and dominant role in the Group's overall sales performance.

During the year under review, the Group reported a drop in profitability. The Group's profit before tax for the year and the previous year were HK\$107.8 million and HK\$297.2, million respectively, with gross profit ratios standing at approximately 17% and 30%, respectively. The decline in profit before tax was explained by the combined effect of (i) a decrement in sales of approximately HK\$85 million, (ii) an increment in the costs of sales by HK\$86 million and (iii) a rise in the total operating expenses and finance costs of HK\$17 million.

The sales decline was due to the Group's strategy to lower the average selling price for electronic consumer products so as to capture a greater market share. In particular, sales for electronic calculators accelerated by approximately 7.8% over last year. For electronic components and parts such as quartz crystals and LCDs, their sales fell slightly due to increased market competition. Traditional lower end watch movements showed an unsatisfactory performance due to market saturation, hence, lowering the gross profit margin. For integrated circuits (IC), because of its falling prices, the Group recorded a drop in the turnover by about 31.5%.

Compared with last year, operating margins moved downwards in the year under review. The listing and expansion of the Company resulted in higher operating costs for the Group. Due to the expansion of the Group, more bank loans were raised as capital expenditures and together with the issue of US\$10 million convertible bonds in May 2000 (details as stated in the section headed "Capital Structure"), an increase of approximately HK\$1.9 million in finance costs including bank interests and interests on the convertible bonds was noted.



Management Discussion and Analysis



BUSINESS REVIEW *(continued)*

Review of Operation and Results *(continued)*

In view of these, the Group has planned to shift its focus to better profit-generating products such as personal data assistants ("PDAs"). Although some of the Group's traditional product lines were subject to substantial price pressure, thereby reducing the profit margin, the Board believes that in the longer term, the diversification in product innovations and stringent control in costs will help the Group to achieve improvements in both the profit margin and its profitability.

As at 30 September 2000, the Group paid up 20% deposit amounting to US\$300,000 (equivalent to approximately HK\$2,325,000) for the acquisition of 35,256 equity shares of Angstrom Joint Stock Company ("Angstrom"), representing 5.4% of its issued share capital. Angstrom is registered under the laws of Russian Federation as open joint stock company and is principally engaged in the manufacture and sale of integrated circuits. The investment is intended to be held for long term continuing purposes. The Group believes that the investment can assure the supply of IC, resulting in shorter lead-time in product delivery.

For the investment in Taiwan Communication (Fujian) Company Limited, as at 30 September 2000, the Group had paid an initial capital injection of US\$1 million (equivalent to approximately HK\$7.75 million), being half of the total contracted investment cost. The remaining capital contribution of US\$1 million was paid up on 3 November 2000. The joint venture is engaged in the manufacture and trading of telecommunications products such as fax machines.

The production of high frequency quartz crystals, which are used in such telecommunications devices as cellular phones, modems and fax machines, has also commenced in small volume near the end of the year. The management believes that once our plant runs at full capacity in the forthcoming year, its production will become a new profitable source to the Group.

For the year ended 30 September 2000, the Group does not recommend the payment of any final dividend. Basic earnings per share and diluted earnings per share was HK\$10.1 and HK\$10.0, respectively.



BUSINESS REVIEW *(continued)*

Liquidity and Financial Resources

The Group maintains a strong financial position. As at 30 September 2000, the total shareholders' equity of the Group was approximately HK\$790.7 million, an increase of 15.2% over that as at 30 September 1999. As at the balance sheet date, the cash and bank deposits balances stood at HK\$144.9 million. The bank borrowings and trust receipt loans amounted to HK\$158.9 million, an increment of 46.1% as compared to that as at 30 September 1999. The increment was mainly due to the increase in secured short term bank loans of HK\$38.9 million in order to fund the expansion in production facilities in our factory plants. The bank loans were denominated in Reminbi and US\$, which amounted to HK\$105.4 million and HK\$37.4 million, respectively. The interest coverage worked out by dividing profit before interest, tax and depreciation by total net interest expenses for the year and last year was 19.6 times and 47.0 times, respectively.

Capital Structure

During the year, 40,000,000 share options were granted to certain directors and employees of the Group for subscription for the ordinary shares of HK\$0.1 each in the capital of the Company at HK\$1.2 per share exercisable up to 24 October 2009. A total of 450,000 share options were exercised during the year and the Company had 39,550,000 outstanding share options at the balance sheet date.

In May 2000, the Group has also raised new funding by way of an issue of an aggregate principal amount of US\$10 million 3% unsecured convertible bonds due 2003 to Credit Suisse First Boston (Hong Kong) Limited ("CSFB") and The SCM Growth Fund II L.P. ("SCM"). The net proceeds derived from the issue of the convertible bonds will be used for capital expenditure in connection with the expansion of certain production and manufacturing facilities and general working capital purposes. Accordingly, the gearing ratio, which was computed by dividing the current liabilities and long term debt by shareholders' equity, has increased from 40.0% to 41.4%. Borrowings are closely monitored by the Group to maintain gearing at a reasonable level. During the year, CSFB converted twice in the total sum of US\$300,000 bonds into ordinary shares of the Company. Accordingly, the issued share capital of the Company has been increased to HK\$100,219,863 as at 30 September 2000. Subsequent to the balance sheet date in November 2000, SCM converted US\$100,000 bonds into ordinary shares of the Company which further resulted in an increase in the issued share capital of the Company to HK\$100,358,200.

Pledge of Assets

The investment property, certain leasehold land and buildings, and plant and machinery and certain time deposits of the Group, together with the corporate guarantees of certain related companies and the Company, are used to secure banking facilities of the Group. Details of charges on group assets are set out in note 19 to the financial statements.

Management Discussion and Analysis

BUSINESS REVIEW *(continued)*

Application of Proceeds of Share Offer

As at 30 September 2000, the net proceeds of about HK\$270 million raised from the share offer in September 1999 were applied as follows:

- Approximately HK\$38 million was used to purchase additional machinery, equipment and other facilities and for the construction of factory plant to expand and upgrade liquid crystal display production capacity;
- Approximately HK\$40 million was used to purchase additional machinery, equipment and other facilities and for the construction of factory plant to expand and upgrade quartz crystal production capacity;
- Approximately HK\$19.7 million was used to invest in Taiwan Communication;
- Approximately HK\$2.3 million was paid as deposit to acquire the 5.4% interest in Angstrom; and
- Approximately HK\$2 million for the expansion in the market research and product development division.

The remaining balance of about HK\$168 million of the net proceeds is intended to be applied to the following main purposes:

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|---|-------------------|
| • Acquisition of 5.4% interest in Angstrom | HK\$9.3 million |
| • Expansion of LCDs production capacity | HK\$12 million |
| • Investment in Taiwan Communication | HK\$140.3 million |
| • Expansion of the Group's market research and product development division | HK\$1 million |

The actual and intended applications of the net proceeds of the share offer are in line with the plans set out in the prospectus of the Company dated 25 August 1999 except the acquisition in Angstrom was delayed because of Angstrom's re-organisation in December 1999.

EMPLOYEES AND REMUNERATION POLICIES

As at 30 September 2000, the Group employed approximately 18,000 full time management, administrative and production staff in the PRC and in Hong Kong. The Group remunerates its employees based on their performance, experience and prevailing industry practice. The Group has a share option scheme and provides rent-free quarters to its employees in the PRC. For details of the directors' and employees' emoluments, please refer to note 6 to the financial statements.

PROSPECTS

The Group's strategy to implement its development plans is to segment our markets and to become more market-oriented in order to consolidate the Group's relationship with its broad customer base in both local and oversea markets. With China's imminent entry into the World Trade Organisation, the Group foresees increasing investment opportunities and a more open and favourable business environment in China. The Group expects that sales and profit will be rebound to higher levels.

Besides, the Group is planning to make an investment in the production of PDAs in the year ahead. The product brand's name has been registered as "Supermate". The first lot of production of about 20,000 pieces will commence in March 2001, with the PRC targeted as the line's primary market and the business executives and professionals as the end-users. Our PDAs will incorporate two special functions: electric light (EL) power support and linkage with computers. It is expected that this will bring diversity and a new revenue stream to the Group since they are positioned as higher margin products.

The investments in Angstrom and Taiwan Communication will be carried out as planned and full investments are expected by 2001 and 2002 respectively. The acquisition in Angstrom will cement the Group's relationship with such major IC producer in order to ensure a stable supply.

Looking ahead, the Group will continue to develop its core businesses - design, manufacture and sale of the electronic components and consumer electronic products. It will develop new technological processes that will enable the Group to operate more efficiently and reduce operating costs. The Group believes that the telecommunications industry will offer great development potential, and has been taking steps to expand its existing production lines to meet the anticipated growth in demand for components used in telecommunications products.

In view of the results of the current year, more effort will be put into reducing production costs and more resources will be allocated to the development of new products. The Directors will also consider new related businesses so that the Group may increase its profitability and the returns for the Company's shareholders.



Management Discussion and Analysis

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APPRECIATION

On behalf of the Board, I would like to express my sincere gratitude to our shareholders, fellow directors, staff, customers, suppliers and business associates for their continuous support. We look forward to a better set of results in the year ahead.

Hong Kong
22 January 2001

By Order of the Board
Wong Choi Kam
Chairman

