

telecommunication products

new technology

"Wow...VTech's new 5.8GHz phone is a real cool product that sure exceeds my expectation."

Smith Porter
IT professional

the industry's first 5.8GHz cordless phone

The history of telecommunication products is a history of the new replacing the old. VTech's continuing ability to remain at the forefront of this evolution was demonstrated by the announcement of the launch of the world's first 5.8GHz cordless phone at CES in January 2002.

Combining R&D excellence with extensive market research, VTech's 5.8GHz model offers a range of audio and functional enhancements using pioneering technologies. These range from unique automatic audio enhancement to two-phones-in-one functionality. This product introduction seizes the window of opportunity with a product boasting new technology and very desirable consumer features.

The 5.8GHz project was the first project to leverage our Dual Brand Strategy, focusing on the Brand Values: *VTech: Vibrancy, Innovative and Competitive*; and *AT&T: Pleasure in Use, Classical Styling and Perceived Quality*. These brand values, coupled with customer segmentation research, guided the development and implementation of product features and industrial design.

The result is a product line differentiated clearly by look and feel – and key features – to meet the specific needs of targeted customer segments. Indeed, many retailers say the two brand designs look like creations from two different companies. All in all, retailers have applauded VTech's pioneering efforts and entry into a new category.



bringing cutting edge technology to consumers



understanding consumers



product development



heart of the technology



prototype development

"It was a year of tremendous change at VTech Telecommunications as we fully integrated the VTech and former Lucent operations and our dedicated team made dramatic and sustainable improvements to our entire supply chain process. These developments enabled us to improve significantly our balance sheet and return to profitability. During the course of the year, we also completed the first stage of our transition from an engineering driven company to one with much greater customer focus in all aspects of our business operations."

James C. KRALIK

Chief Executive Officer, VTech Telecommunications Ltd

Market Overview

While the global telecommunication products market has suffered in the past two years, the fixed line market has tended to follow its longer-term trends. In the most mature market, the United States, the shift from corded to cordless products has continued. The US cordless market reached 47 million units* in 2001, with newer generation 2.4GHz models accounting for approximately 18%† of the total. The market is driven partly by a switch from corded to cordless and partly by technology, as cordless users adopt newer models offering improved audio quality, range and enhanced features.

In the developing world, the fixed line market continues to expand rapidly as more lines are installed, particularly in mainland China. In 2001, mainland China added 36 million lines, a 25% increase over the previous year. Despite this, mainland China has a fixed-line penetration rate of less than 25%, showing that considerable room still exists for growth‡. Within this overall market, the cordless market is relatively undeveloped, representing approximately 10% of unit sales§.

* Source: AAT/NPD, Market Intelligence

† Source: Ministry of Information Industry, China

‡ Source: www.ccidnet.com

Performance Review

Unit volumes and turnover fell markedly during the year, as VTech Telecommunications implemented its plan to cut production of loss-making models and focus on higher margin products. Although turnover decreased 18.7% to US\$670.0 million, our profits rebounded sharply from a substantial loss in the 2001 financial year to a significant operating profit in 2002.

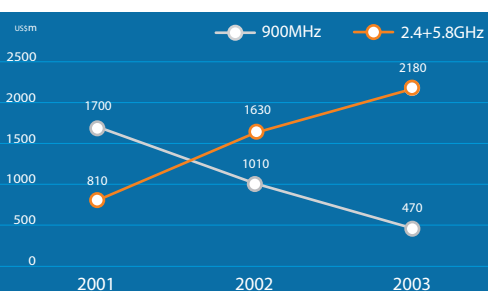
The return to profitability also reflects the successful integration of the former Lucent and VTech operations during the second half of the year, resulting in substantially lower write-offs and the emergence of the benefits of the combined operations. During the course of the year our sales support, accounting, and information technology functions were consolidated in our Beaverton, Oregon office while our distribution and returns processing were consolidated in San Antonio, Texas. At the same time, we completed the full and final integration of our US call centers into one unit in St. Louis, Missouri.

The profit rebound is further the result of our efforts to improve our management of the entire supply chain process. During the year, we instituted daily monitoring from forecasting through ordering, production and shipping. The success of this arduous operation reduced average inventory,



"Seal of Approval – Best Overall"
award by *Good Housekeeping*
magazine

US Cordless Market Value



Source:
AAT/NPD,
Market Intelligence

including units in transit, to the equivalent of two months' sales, and enabled us to avoid significant close out sales of excess inventory.

More strategically, we completed the first stage in our transition from an engineering driven company to one with much greater customer focus. We conducted market research among consumer groups to gain a better understanding of their product desires and establish the perceived brand attributes for VTech and AT&T telephony products. Our two brands, VTech and AT&T, are complementary and focus on different end-user groups at different price points. VTech products are perceived and marketed largely as innovative, vibrant and a good value that appeal to younger and more technology-oriented users, while AT&T products are aimed at those seeking classical design, pleasure in use and recognized quality.

We have incorporated these findings into our ongoing product design, sales and marketing programs. In January 2002, we were the first manufacturer to announce the development and launch of the new 5.8GHz cordless phone platform. This significant breakthrough confirms VTech as the technology leader in cordless telephony and will reap revenue and other benefits in the coming financial year.

Outlook

We remain cautiously optimistic about prospects for the telecommunication products business in the 2003 financial year. Current stability in our sales should continue, although they could be undermined if US consumers were to tighten spending significantly. We also expect competitive price

pressure on 900MHz models and potentially rising component prices. VTech will meet these challenges through increased new product development efforts and sales of higher margin products.

We further expect to make continued progress in establishing ourselves as a customer driven organization. During the first month of the year, the AT&T and VTech sales teams were integrated and client account teams reorganized to enable them to focus more effectively on the needs of our key accounts. Recognizing that our 20 leading customers represent almost 90% of sales, we created specific teams to manage each key account, ensuring a much higher level of customer service. We intend to reorganize our logistics to align the execution of orders with that of our customers' needs. This will cut costs, improve reliability and help cement retailer relationships. Additionally, we will share more market information and co-operate more closely on the full range of sales issues including pricing, product display, package design and promotional events in order to forge even closer relationships with our key retail customers.

Looking beyond the United States, we see opportunities to expand elsewhere. In the immediate future, we are targeting increased sales in Europe on an ODM basis. In the longer term, VTech is carefully evaluating opportunities presented by mainland China. VTech, with its manufacturing base long established in mainland China, has great potential in this admittedly complex market. A new team headed by the Group Chairman has been established to examine the most appropriate way to develop China business.

electronic learning products

new ideas

"My daughter loves all the VTech toys we bought for her. We have had hours of fun playing together."

Carman Bradbury
Teacher