



UNRIVALED R&D

BYD'S R&D CAPABILITY HAS ALWAYS BEEN THE KEY SUCCESS FACTOR OF THE COMPANY. GRASPING THE EVER-EVOLVING MARKET TRENDS, IT HAS ALSO COMMENCED NEW DEVELOPMENTS TO MEET THE DEMANDS OF VARIOUS NEW APPLICATIONS AND TECHNOLOGIES.



MANAGEMENT DISCUSSION AND ANALYSIS



OPERATION ENVIRONMENT

During the year, the market demand for rechargeable batteries, especially in the PRC, was unaffected by the global economic slowdown and remained strong. The growing usage and shrinking product cycles of mobile phones and other portable electronic devices, as well as the increasing penetration rate of mobile communication, all contributed to the booming demand for rechargeable batteries.

Domestic sales increased significantly due to the growing demand for mobile phones in the local market. Local mobile phone manufacturers have successfully ramp up their output volume and capacity. Because of its strong sales network and largest market share in the PRC, BYD has benefited immensely from the encouraging growth momentum.

Since mobile phone handset manufacturers are facing keen competitions from the increasing number of new market entrants, they need cost effective and quality battery products to enhance their competitiveness. During 2002, BYD was committed to expanding its customer base and also soliciting greater demands of its rechargeable battery products from existing customers.

For the year ended 31st December, 2002, sales of rechargeable battery products surged from about 324

million pieces to about 485 million pieces, or about 50% increase as compared to the previous year.

In the foreseeable future, mobile phones and power tools will be the major drivers for BYD's business growth. Li-ion battery is believed to be the major source of growth in the rechargeable batteries market due to its high energy density and environmental friendliness. With the launch of the 2.5G and 3G mobile phone services and the increasing popularity of notebook computers, digital cameras, MP3 players and other personal electronic digital devices, the market potential of Li-ion batteries is enormous. In addition, BYD has successfully passed the qualification process of Black and Decker. New customer of such will further strengthen BYD's leading position in the power tools market. Coupled with its imminent entry into the notebook computer's battery market, BYD is poised to further capture market shares and takes firm step to become the No. 1 global rechargeable batteries manufacturer.

BUSINESS REVIEW

During the year, the strong market demand for rechargeable batteries, especially in the PRC, together with BYD's ability to supply quality products at competitive prices, brought forth a substantial organic growth to BYD. BYD sustained a remarkable growth of 76% in turnover, and 213% in profit

attributable to shareholders that reached about RMB2,291 million and about RMB658 million, respectively.

Overall profit margin also increased significantly during the year under review. Such increase was mainly due to the shifting of BYD's product mix to products which enjoy higher gross profit margin, and a better cost control system resulting from improved production processes, economies of scale as well as producing part of the raw materials. Currently, Li-ion batteries have already taken over NiCd batteries to become the Group's core product and it will continue to be the major income source in the future.

More importantly, BYD was able to further enhance its market leadership, with its three core battery products, namely NiCd, NiMH and Li-ion, ranking first, second and third, respectively, in the global rechargeable batteries market. These encouraging results are generated by the Company's prudent business strategies, high product quality and strong R&D capability.

Recognised for its outstanding product quality and competitive pricing strategy, the Group was not only able to build a strong customer base that includes industry giants such as Motorola, TTI, Kyocera, Panasonic, VTech, Phillips, Bosch, Bird, TCL and Konka. While achieving economies of scale and low production costs to become the market price setter, BYD's outstanding product quality also attracts new clients of both domestic and international brand, such as Nokia, Sony Ericsson, UTStarcom, Makita, AEG and Symbol, to ensure a reliable income source for the Company.

BYD's R&D capability has always been the key success factor and the key focus of the Company. Grasping the ever-evolving market trends, it has also commenced, and will continue to, new developments to meet the demands of various new applications and technologies, such as blue-tooth products, digital cameras, PDAs as well as other portable devices and electric vehicles.

BYD's current production capacity is about 500,000 Li-ion batteries per day. The Company plans to increase its capacity to meet the increasing demand of electronic device manufacturers in the Yangtze River Delta region by setting up a new production plant in Shanghai, whose commercial production is expected to commence in the second quarter of 2003. We will also maintain the growth momentum of Nickel batteries, since a number of manufacturers are exiting the market and BYD is poised to benefit from the huge economies of scale of the production of these batteries.

All in all, the Company is confident that it can capture even larger market shares in all types of rechargeable batteries, and the growth momentum of the Group will continue to be strong.

FINANCIAL REVIEW

Turnover

For the year ended 31st December, 2002, our turnover increased by 76% to about RMB2,291 million as compared to 2001. The increase in turnover was mainly contributed by the increase in sales of Li-ion batteries. Li-ion batteries have leapfrogged over NiCd batteries to become the Group's most important product in terms of turnover and profit contribution.





Gross profit

The Group's gross profit increased by about 122%, from about RMB430 million for the year ended 31st December, 2001 to about RMB954 million for the year ended 31st December, 2002.

Profit attributable to shareholders

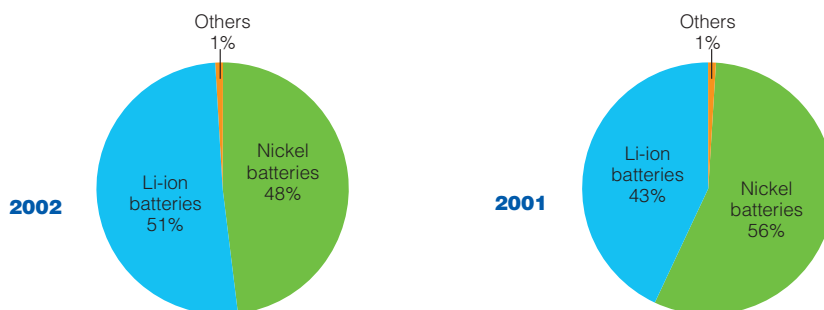
The Group's profit attributable to shareholders increased by about 213% from about RMB210 million for the year ended 31st December, 2001 to about RMB658 million for the year ended 31st December, 2002, which is 18% higher than the profit forecast as stated in the Company's IPO prospectus. The surge in profit attributable to shareholders was attributed by the increase in sales of all batteries, especially in

Li-ion batteries and sales of battery packs, increasing orders from existing major customers such as Motorola and Bird, as well as new orders from new customers.

Net profit margin

During 2002, the Group's net profit margin increased considerably to reach 29%. Such increase in net profit margin was attributable to the improvement in the production process and its ability to produce part of the raw materials to control cost. The Group has also shifted its product mix to products with higher gross profit margins. Also, the Group was able to enjoy better economies of scale by increasing its production volume.

TURNOVER BREAKDOWN BY PRODUCTS





Thanks to the Group's successful effort in controlling cost, distribution costs and administrative expenses as a percentage of turnover decreased from 3% to 2% and 10% to 6%, respectively.

Liquidity and financial resources

The Group generated a net operating cash inflow of about RMB318 million during the year ended 31st December, 2002, which has improved substantially from about RMB132 million recorded last year.

The Group received the net proceeds of its H share listing amounted to about RMB1.57 billion and all outstanding bank loans as at 31st December, 2002 have been repaid and as at the date of this report,

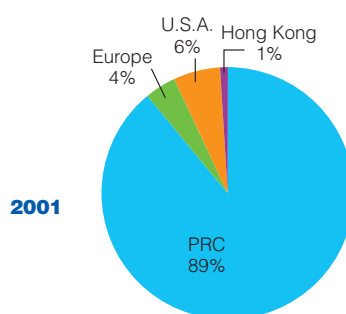
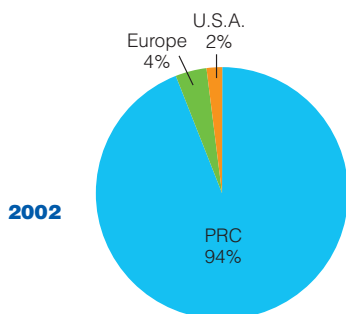
the Group is in a net cash position with cash and bank deposits balance of about RMB1,240 million.

The Group's accounts receivable turnover days were about 76 days in 2002 as compared to 81 days in the previous year. The improvement in accounts receivable turnover days was attributable to the Group's continuous effort to monitor and maintain a prudent credit policy.

Finished goods were required to be stored in the warehouse before packaging for the chemicals to become stable. Due to the increase of turnover, inventory turnover days increased from 89 days to 93 days during the year under review.

SEGMENTAL INFORMATION

TURNOVER BREAKDOWN BY OPERATING SEGMENTS



USE OF IPO PROCEEDS

	HKD million	
	Planned	Latest allocation
Expansion in production capacity and R&D of Li-ion batteries	189	Fully utilized
Development and manufacture of chemical compounds in Li-ion batteries	94	73.5
Product R&D and manufacture of:		
- rechargeable batteries for electric vehicles	85	0.09
- fuel cells and solar cells	85	—
- monochrome and colour STN-LCDs	142	71.1
Repayment of bank loans	377	Fully utilized
Potential acquisition(s)	189	—

DETAILS OF THE GROUP'S ASSETS PLEDGED

As at the date of this report, no assets of the Group are pledged.

EXPOSURE TO FOREIGN EXCHANGE RISK

Most of the income and expenditure of the Group are denominated in RMB and USD. The Group has not experienced any material difficulties or effects on its operations or liquidity as a result of fluctuations in currency exchange rates during the period under review. The Directors believe that the Group will have sufficient foreign exchange to meet its foreign exchange requirements.

EMPLOYMENT, TRAINING AND DEVELOPMENT

As at 31st December, 2002, the Group has a total of about 17,000 employees, an increase of about 6,000 as compared to the same period in 2001, and total staff costs amounted to about 10% of total turnover. Employees are remunerated based on their

performance, experience and the prevailing industry practices, with compensation policies and packages being reviewed on a regular basis. Bonuses and commissions may be awarded to employees based on performance evaluation. There are drives and encouragements for personal performance.

PURCHASE, SALE OR REDEMPTION OF SHARES

The Company has not redeemed any of its shares since the listing on 31st July, 2002 up to the date of this report. Neither the Company nor any of its subsidiaries has purchased or sold any of the Company's shares during the same period.

CONTINGENT LIABILITY

The Group is currently involved in, among others, a litigation proceeding in U.S.A. in relation to the alleged infringement of two patent registrations relating to lithium secondary battery and cell which secure the reliability of a protective circuit. The

complainant alleged to be the exclusive licensee of the aforesaid patents and is seeking remedies against the Company and BYD America Corporation, a subsidiary of the Company, details of which were disclosed in the announcements of the Company dated 25th September, 2002 and 3rd October, 2002. Due to the fact that such proceeding is still at an initial stage, it is impracticable and premature for the Directors to assess the impact of such proceeding on the Group and its operation. The Directors believe that the Group has not committed the alleged infringements. The Group would vigorously defend against all claims made under the proceeding.

OUTLOOK

In future, the Company will continue to focus on the R&D, manufacturing and sale of rechargeable batteries products, including Li-ion and Nickel batteries. At present, BYD already ranks third in the global Li-ion batteries market. The increasing number of Li-ion batteries are becoming the major profit driver of BYD, and the increasing demand for BYD's Li-ion batteries will be driven by the increasing number of orders from existing major customers, including Motorola and Bird and the addition of new customers, such as Nokia. Overall, we expect that domestic handset manufacturers will provide more businesses for BYD.

Entering into the 3G digital era, the global usage of various portable electronic devices, as well as the use of both traditional and new technologies, has continued to grow at an exceptional speed. As one

of the leading rechargeable batteries manufacturers in the world, BYD would not rest on its laurels. Looking ahead, it will be even more focused on strengthening its production quality and capacity, R&D capability and product diversity to sustain our leading position in the global rechargeable batteries market.

On 22nd January, 2003, BYD announced that it has entered into two agreements to acquire an aggregate of 77% stake in Xian Qin Chuan Automobile Limited Liability Company ("XQC Automobile") for a total cash consideration of about RMB270 million, which will be funded by the Group's internal cash reserve and the H shares IPO proceeds will not be applied in this acquisition. The completion of the acquisition is expected to take place by March of 2003. The core product of XQC Automobile is a compact 800c.c. mini-car under the "Flyer" brand. The acquisition of XQC Automobile will enable BYD to have a solid and immediate platform for its R&D on electric vehicle rechargeable batteries and speed up the entire development process. In the long run, the XQC Automobile mini-car is an appropriate starting point for entering the electric car market in China. Coupled with BYD's manufacturing capability and solid battery business, the development and potentials of the new venture will be maximized. In addition, since XQC Automobile is one of fast growing manufacturers in the expanding car market in China, it will serve as a gateway for BYD to cooperate with international leading car manufacturers who wish to explore the promising Chinese car market. Such an opportunity will help enhance profitability of the Company.