Chairman's Statement

2002 is a challenging and yet dynamic year for Stone Electronic Technology Limited (the "Company") and its subsidiaries (the "Group"). While the global economy continued to be weak and uncertainty prevailed in the market, China experienced continuous economic growth following her accession into the World Trade Organisation ("WTO"). Overseas investors, as a result, has speeded up their pace of entering the China market, leading to intensified market competition. Amid this highly competitive operating environment, the Group's focus was placed on the development of core businesses such as Electronic Product Manufacture and Distribution ("Manufacture and Distribution Business") and Value-Added Technical Services, which was supported by investment in projects with growth potential. The Board of Directors is pleased to see that the Group successfully returned to a profitable position in 2002.

For the year ended 31st December 2002, the Group's turnover amounted to HK$996.0 million, representing a growth of 5.8%. Profit attributable to shareholders amounted to HK$36.7 million, a significant improvement as compared to the loss position in 2001. As the Group's business is still undergoing a period of adjustment, the Board of Directors does not recommend the payment of a final dividend.

REVIEW OF BUSINESS

The Group's Manufacture and Distribution Business experienced fierce market competition in 2002. Facing an unstable global economic environment and deflation in China, the Group adjusted its business strategy and consolidated its resources on the development and sales of products where the Group's competitive edge lies. Revenue from the Manufacture and Distribution Business increased with improvements in gross margin.

Value-Added Technical Services, one of the key directions of the Group, performed well and saw satisfactory growth during the year.

As the media industry in China was still in its infancy in both its development and operation, the Group's Media Related Business, therefore, was hampered by various obstacles during the year. The Group will continue to keep an eye on market changes and react promptly to them.

MANUFACTURE AND DISTRIBUTION BUSINESS

Foreign investors accelerated their pace of entering the China market following China's entry to WTO leading to intensified market competition. In pursuit of excellence and to boost competitiveness at the same time, the Group has incorporated Value-Added Technical Services in the Manufacture and Distribution Business. Its aim is to enhance customer loyalty and eventually increase its market share.

During the year under review, the Manufacture and Distribution Business recorded stable growth. Turnover reached HK$952.4 million, an increase of HK$30.7 million or 3.3% over the previous year. Among the various electronic products, industrial controllers and invoice printers continued to be the major revenue sources, accounting for 42.4% and 17.1% respectively of the revenue of this business.

Industrial Controllers

Prompted by the need to keep up with the rapid economic development in China, both government and commercial entities are striving to optimise operational efficiency, thus driving the surge in demand for industrial automation products and benefiting the sale of industrial controllers. The Group distributes industrial control and automation products sourced from different parts of the world. Among these, it was ranked one of the top three distributors of Siemen, Fuji, Omron and Allen Bradley in China in terms of sales in 2002.

The Group incorporated Value-Added Technical Services, e.g., application solutions, in the distribution products. This move not only helped improve customer satisfaction, but also generated positive sales growth.

Invoice Printers

After China's accession into WTO, the Chinese government lowered tariff on parts and components of printers, allowing the Group to lower production costs. Keeping the gross margin unchanged, the Group adjusted the sales price of Stone-OKI brand invoice printers to actively attract new customers. During the year, the Group launched new models of invoice printers to replace old ones, leading to the demand for the Group's invoice printers experiencing a period of transition. As a result, sales of invoice printers decreased 16.5% to HK$163.2 million. It is expected that sales of invoice printers will pick up again in 2003.

Gold Tax Products

In tandem with the implementation of the Gold Tax Project, a major project under the State Informationalisation Programme, the Group is committed to the development of sales tax control cashiers ("STC cashiers") and anti-counterfeiting tax control machines ("ATC machines") that comply with the standards stipulated by the State Tax Bureau ("STB"). Since the STB is still in the process of evaluating national design standards of STC Cashiers as well as the codes of the IC chips of ATC machines, formal hardware sales have not yet started. It is expected that the Gold Tax Project will be fully implemented after the completion of the approval process by end of this year. The Board expects this business to see better development by then.

Computers

"Stone" is a well-known brand name in the China market. To fully leverage this brand advantage, the Group joined hands with Achieva Investment Pte Ltd., a Singapore listed company, to form a joint venture company to further expand the scope of computers under the Stone brand name. The joint venture, 51% owned by the Group, will focus on brand management, product design and marketing. Computers designed by the joint venture will be manufactured on an OEM basis. This enables the Group to more efficiently allocate its resources and hence increases operational efficiency. Currently the Group owns two lines of branded products, namely "Stone" and "Stone Collaborative". We are optimistic of the prospect of this business.

As for non-branded computer products, despite the satisfactory growth in turnover, the Group decided to terminate this business due to the low profit margin when compared with branded products. Resources will be consolidated and redirected to the branded computer products.

Other Products

Digital graphical products and uninterruptible power system ("UPS") equipment recorded satisfactory sales growth of 58.1% and 21.0% respectively. This is primarily due to the price reduction from suppliers, which in turn allowed the Group to lower the selling prices to attract customers. The sales rise was also attributable to increased efforts in staff sales training as well as marketing activities.

VALUE-ADDED TECHNICAL SERVICES

As stated in the 2001 annual report, the Group was committed to developing Value-Added Technical Services to boost its competitiveness and market share. Adhering to this course, the Group has incorporated services with high added value to the offers of its Manufacture and Distribution Business. During the year under review, the Group offered turnkey programming services to customers of industrial controllers, and software development services to customers of invoice printers, as well as technical training and installation services to ATC machine customers.

With the complement of these Value-Added Technical Services, customers are provided with all-rounded services. In addition to strengthening the relationship with customers, the Value-Added Technical Services also benefited from the established customer base of Manufacture and Distribution Business. The synergy created between the two business streams not only boosted our core businesses, but has also opened up for the Group a new revenue source. As the Group's business gradually moves back on track to positive growth, the Board expects the proportion of this business to go up.

The revenue from Value-Added Technical Services surged from HK$19.7 million in 2001 to HK$42.3 million in 2002, representing a strong growth of 114.7%.

MEDIA RELATED BUSINESS

The Group's Media Related Business can be divided into three major investment projects - the Nasdaq listed SINA Corporation ("Sina"), the Hong Kong listed Sun Media Group Holdings Ltd. ("Sun Media"), and the China Cable Information Network Co., Ltd (China Cable").

Sun Stone New Media Limited ("Sun Stone"), a subsidiary of the Group incorporated in 2001 to hold the equity interest in Sina, did not perform well during the year under review. It was the Group's original intention to develop China media related business through the stakes in Sina and this subsidiary. However, the immature China media market posed major hurdles for this business. Operating loss of this business after minority interests amounted to HK$9.1 million. A prompt decision was made to stop the operation of the subsidiary. As a result, the Group was unable to exert significant influence over Sina. The Board of Directors, having given prudent consideration heeding the best interests of shareholders, concluded that the investment in Sina will be held for profit in the short run. On this basis, the investment in Sina recorded an unrealized gain of HK$177.5 million attributable to the Group.

China Cable underwent a series of mergers and acquisitions and corporate restructure during the year under review. As a result of these restructuring moves, the Group's equity stake in this project was diluted from 25% to 9.51%. After conducting an assessment of the Group's investment in China Cable on 31st December, 2002, an impairment loss of HK$79.4 million was incurred. In spite of this, the Group considers that the project carries strategic values as a long-term investment.

The Group's investment in Sun Media will continue to be regarded as long-term investment.

OTHER INVESTMENTS

Censoft Company Ltd.("Censoft")

The Group, together with Beijing Centergate Technologies Co., Ltd. ("Centergate") and Microsoft Corporation ("Microsoft"), jointly formed Censoft, a PRC-based company, to tap the opportunities in the China software market. Censoft specializes in the development of platform software for e-government, e-commerce, e-banking projects, etc. The equity stakes of the Group, Centergate and Microsoft are 30%, 51% and 19% respectively. As the founding shareholders of Censoft have extensive experience in the IT and software sector, the outlook of this business is promising.

Dalian F.T.Z. Huaqing International Engineering & Trading Co., Ltd. ("Dalian Huaqing")

In an effort to open up new revenue streams to broaden the revenue base, the Group acquired 51% equity interest of Dalian Huaqing, a PRC logistics service company for an amount of Rmb11.0 million (HK$10.4 million). Dalian Huaqing will be engaged in the provision of e-commerce and one-stop logistics management services.

Shanghai Centek Communication Industry Company Limited ("Shanghai Centek")

During the year under review, the Group invested HK$20.3 million in the establishment of Shanghai Centek, the business of which is to provide global satellite positioning services. However, the development of the project was affected by unresolved differences in corporate vision and management culture between the Group and its partners. As such, the Group made a decisive move to terminate this business. This reflected our ability to respond quickly to operating environment by making adjustments in individual projects. The investment in this company recorded a loss of HK$12.1 million.

FUTURE OUTLOOK

Foreign investors' continual investment and participation in the China market following her accession to WTO will lead to ferocious market competition. The Group anticipates that, in a bid to increase competitiveness, both government and commercial entities will seek to increase the magnitude and speed of automation and computerization. This phenomenon will stimulate the demand for industrial controllers, computers, printers, etc creating a favourable operating environment for the Group. In addition, the Group will take advantage of the recognition of the Stone brand to develop products under our own brand name aggressively, which will allow us to excel in the market.

Having gone through business consolidation in the past years, the Group has accumulated invaluable experiences and knowledge and found the right path. Our efforts have further cemented our foundation. The Group is in a solid financial position with a sufficient reserve of capital. We will consider various forms of cooperation and acquisition if we come across suitable projects with good prospects. Looking ahead, the Group is committed to enhancing operational efficiency and controlling cost. We will adopt prudent financial management strategy to ensure value growth for our shareholders.

Negative economic factors, such as the War in Iraq and the widespread atypical pneumonia that emerged in the first half of 2003, are affecting the world economy. The Board of Directors anticipates 2003 to be a difficult and unstable year. The Group will observe the market environment closely.

Last but not least, I would like to express my gratitude to all directors on board who offered their leadership heartily. I also wish to extend my heartfelt appreciation to all our shareholders, customers, business partners as well as our staff members for their continuous support to the Group.

Duan Yongji
Chairman

Hong Kong, 25 April 2003