

# Management Discussion and Analysis

## FINANCIAL PERFORMANCE

For the year ended 31 December 2002, the Group recorded a turnover of approximately HK\$130 million, representing a decrease of 53% over the previous year. During the year under review, the Group recorded a loss of HK\$52 million, compared to last year's profit of HK\$32 million.

Reference was made to the announcement made by the Company on 2 May 2003, which was published on the Standard and the Hong Kong Economic Times on 3 May 2003 regarding, among other matters, the unaudited consolidated income statement of the Group for the year ended 31 December 2002 ("2002 Unaudited Financial Statement"). There is an increase of approximately HK\$22.46 million in the loss attributable to shareholders in the Company's audited final results in 2002 set out in the audited consolidated income statement on page 22 of this report as compared to that of the 2002 Unaudited Financial Statement. Such difference was mainly due to the following reasons:

1. The Company made a preliminary provision for bad and doubtful debt of approximately HK\$15 million only when preparing the 2002 Unaudited Financial Statement as the recovery assessment on our accounts receivable was not yet completed. Owing to the global economic downturn, the business environment for computer and electronics sectors rapidly deteriorated at the end of 2002. As a result, some of our customers experienced cashflow difficulties and defaulted on payment. Subsequent to a comprehensive and complete assessment on our customers around the world, the Company tracked down a list of customers with worsening financial position, who had already defaulted on payment from 7 months to over 1 year. Such customers with accounts receivable which was comparatively more difficult to recover were mainly from Vienna, Italy, France, Hamburg and South Africa. The Company made full provision for the accounts receivable from those customers defaulting on payment for over 1 year and those with accounts receivable which was comparatively more difficult to recover and a 50% provision for the accounts receivable from those defaulting on payment for 6 months or above, totaling an aggregate amount of approximately HK\$30.66 million as shown in the consolidated audited income statement for the year ended 31 December 2002 of the Company. The Company has demanded a return of goods delivered from and stopped all delivery orders to such customers. Also, on a case-by-case basis, the Company intends to institute legal proceedings through its lawyer to claim the outstanding payments from them.
2. The Company made a preliminary provision of about HK\$2.753 million for those products no longer produced by the Group in preparation of the 2002 Unaudited Financial Statement. As the Company was undergoing a transformation of products from low-end computer peripherals to high-end computer peripherals in 2002, it made a further provision of about HK\$4.267 million for those slow-moving low-end computer peripherals and their raw materials in stock with market prices lower than their costs, totaling of about HK\$7.02 million as shown in the audited consolidated income statement for the year ended 31 December 2002.

In addition to the sluggish economic environment, the Group's business restructuring was another major reason for the lower turnover and loss for the year. The Group intentionally took no orders for iron PC products from March 2002 in order to cater for the growing demand for aluminum alloy products, most of which was on OEM/ODM basis. These OEM/ODM projects took greater development efforts and longer cycles to conclude the contracts. The move to premium products has also caused a reduction in the Group's customer number, thus affecting the financial performance particularly in the second half of 2002. However, with the launch of lower-priced aluminum alloy-feel (zincum) computer chassis and computer products, which received excellent responses in the market, old customers returned to the Group with new orders;

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however, the increased orders of the Group in the second half of the year were still not enough to cover the reduced sales in the first half of the year. As such, it inevitably resulted in a lower full year profit, though the Group has completed its restructuring to form a strong base for reigniting long-term growth.

The overall gross profit margin decreased from 24% to 10%, resulted from a stock provision of about HK\$7 million and the decrease in sales. The increase in distribution costs was due to the Group increased its marketing activities during the year. The provision for doubtful debts of about HK\$30 million had a direct impact on the Group's bottom line as well as the net loss in the year under review.

## BUSINESS REVIEW

### Core Businesses

During the year under review, revenue was mainly derived from Personal Computer Peripherals, Networking Products and Computer Accessories, with each accounting for 71%, 24% and 5% of the Group's turnover respectively.

#### *Personal Computer Peripherals*

From the second half of 2002, market demand for aluminum alloy-feel (zincum) computer chassis and computer products introduced by the Group had been encouraging. The Group's multi-media speaker and power supply pack products also received favorable responses especially from the "Do-It-Yourself" (DIY) markets. However, the Group's decision to stop taking orders of iron PC peripherals as well as the reduction of product prices by around 20% during the first half of 2002, led to a 49% decrease in sales of this business for the full year. It is the Group's aim to shorten the gap with its competitors and take the possession of the computer markets. Gross margin of this product category recorded a decrease of 61% as a result of technical popularisation.

#### *Networking Products*

In the area of networking products, sales accounted for 24% of the total turnover as compared to 30% in 2001. The decrease in turnover by 62% was due to changes in customer behaviour when ordering power supplies for their network systems. Gross profit in this product category also decreased 81%, while the gross profit margin decreased to 17% (2001: 35%).

#### *Computer Accessories*

As the Company looks on computer accessories as complementary products offered to meet customers' comprehensive needs, this product category does not constitute a major source of revenue for the Group. Its share over the overall turnover was around 5% in the year under review.

### Research and Development Achievements

Riding on the Group's experience and accurate perception of market trends, the Company's research and development professionals have concentrated on the development of new products to cater for evolving market needs. During the year under review, the Group successfully launched a range of new products including high-end aluminum alloy barebone systems MPC 2200/2201(RFS), Aluminum PC case of PSR 46 series, PSR 56 series, IMC 62 series, VMC 7288 and Networking product of Gigabit Ethernet Switches Hub

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with Auto MDI/MDIX, 10/100/1000 Mbps Networking Interface Card, 2 to 8 ports Keyboard/Mouse Switch and 15" & 17" LCD Monitor. This comprehensive product mix is tailored for different scale and scope of individual users.

In addition, the Group obtained technology patents for functionality front panel, CDR flip cover, Anodizing technology as well as EMI/EMC International Safety Standard Accreditation. These recognitions further demonstrate the capabilities of the Group's research and development professionals as well as the high quality that the Company embraces.

### **OEM/ODM Business & Agents Networks**

Concurrent with the business restructuring plan, the Group placed tremendous effort into expanding its OEM/ODM client base and agents network for the aluminum alloy and aluminum alloy-feel (zincum) computer chassis and computer products. The latter products not only captured most of the old clients who used to purchase iron chassis, but also attracted new customers to the Group. More OEM/ODM contracts keep flowing in from new clients, including the renowned Taiwan-based motherboard manufacturers, VIA, Shuttle Inc., Jetway, Freetech, and a PRC computer manufacturer Great Wall Computer, Langchao Group, Hisense and Furistock.

The Group's participation in the Computex Taipei 2002 in June and Comdex Fall Las Vegas in November 2002 brought fruitful results as the Group signed cooperation agreements with a number of new agents. These new agents include Liata in Canada, AMAX, Leadertech System of Chicago, Maxtop Technology Corp. and Mwave, A-Top and Fudin in the United States; Bonchic, EET Riga, Gtek, Microplex, Quad Computer, Premier & Jet in Germany; Morex and Time in England; iCute, Enermax and Green Choice in Taiwan; and BCN, DMA, EYO, Westan and Anyware in Australia. The Group also appointed new agents in Hong Kong including the Eurone Group, Genteelord International Limited, Hornington, 099 Power and Crown Joy.

The Company has taken a significant step forward to channel its sophisticated aluminum alloy and aluminum alloy-feel (zincum) computer chassis and computer products through the agents' extensive distribution networks. As a result, a number of systems integration companies and computer manufacturers in the United States, such as Pacific Magtron International Corp. and Everin America Inc., have also placed PC chassis orders to the Group. The agents' network not only help the Group to stay ahead of its competitors, but also extend the Group's brand-name to worldwide markets, raising the growth potential of the Group.

### **Geographical Analysis**

For the year ended 2002, 36% of the Group's sales were generated from North America. At the same time the Asia Pacific surpassed Europe, accounted for 34% of total sales. The Group successfully recorded its first sales in the PRC which successfully enhances its business performance in the Asia Pacific. Europe accounted for 26% of the Group's overall sales. South Africa has also shown stable sales as compared to the corresponding period last year.

### **LIQUIDITY AND FINANCIAL RESOURCES**

As at 31 December 2002, the Group had cash and bank balances of a total amount of approximately HK\$15.9 million and net current assets of approximately HK\$62.4 million. The Group has consistently maintained a solid working capital base during the period under review. As at 31 December 2002, the current liabilities of the Group was approximately HK\$61.8 million whilst the Group had outstanding borrowings of approximately HK\$12.3 million. The Group's banking facilities are secured by a property of the Group. The gearing ratio (total liabilities to total assets) was 35.5% (at 31 December 2001: 40.5%).

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## TREASURY POLICIES

With the focus on risk management, the Group adopts a conservative approach towards its treasury policies in order to monitor its foreign exchange risk, credit risk and liquidity risk. Monetary assets of the Group include cash, trade receivables, prepayments and other receivables. Monetary liabilities of the Group include trade payables, secured bank loans, accrued expenses and other payables. The Group strives to minimise the foreign exchange risk by achieving a balance between monetary assets and monetary liabilities in foreign currencies against Hong Kong dollars. To reduce exposure to credit risk, the Group performs ongoing credit evaluations of the financial condition of its customers. To manage liquidity risk, the Group closely monitors its liquidity to ensure that the liquidity structure of the Group's assets, liabilities and commitments can meet its funding needs.

## USE OF PROCEEDS

The net proceeds raised from the placing and public offer of the Company's shares on The Stock Exchange of Hong Kong Limited (the "Stock Exchange") amounted to approximately HK\$45 million. As at 31 December 2002, the Group has utilised a total of approximately HK\$41 million of the net proceeds. Approximately HK\$16.7 million, HK\$11.4 million, HK\$2.9 million and HK\$10.6 million had been applied towards sales development, research & development, production facility and working capital expenses respectively. The remaining net proceeds are placed on interest-bearing deposits with licensed banks in Hong Kong. The use of the net proceeds was in line with the disclosure made in the Prospectus.

## CONTINGENT LIABILITIES

At 31 December 2002, there were contingent liabilities in respect of banking facilities utilised by certain subsidiaries and guaranteed by the Company amounting to approximately HK\$10,439,000 (2001 : Nil).

## EMPLOYMENT AND REMUNERATION POLICY

As at 31 December 2002, the Group had 1,166 employees in the PRC (including Hong Kong and Taiwan) and overseas. During the year, the remuneration for the employees amounted to approximately HK\$17,574,000. In order to maintain competitiveness, the salary and bonus of the staff are based on their individual performance. Apart from basic salaries, discretionary bonus, contribution to the statutory retirement scheme and a share options scheme for its staff in Hong Kong, Taiwan and PRC, the Group has also provided them with various training and development programs.

## PROSPECTS

As the business transformation basically completed in 2002, the Group is set to optimise the utilisation of its resources and improve return on invested capital in 2003 and onward. With a refined business focus and medium to premium products, the Board and the management are confident of the Group's future outlook.

Apart from seeing greater contribution from the new products launched last year, the Group will continue with its new product initiatives in 2003. In addition to aluminum alloy-feel (Zincum) computer chassis and computer products, the Group will continue to leverage on its research and development capabilities for the launch of Bronze-feel Chassis and 17" LCD monitors, raising penetration in the market. These innovative products will reinforce the Company's pioneering position in the industry.

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An ongoing commitment of the Group is to expand ODM business and agents' network. The Group has made significant progress in this area to date, as the leading aluminum alloy and aluminum alloy-steel (zincum) computer chassis and computer products have captured the attention of distinguished market players worldwide. These include VIA Technologies Inc., ANTEC, ASI, CompUSA Inc., Jetway, Freetech, LG, Hisense and First International Computer etc, who began to place orders for the Company's products in April of 2002, from computer chassis (Series: IPX 8201, VMC 7288, INC 6266, 6272 & ATX 56 series), power supply packs, keyboards, mouse units, subwoofers, speakers etc. To reach worldwide potential clients with its sophisticated products, the Company will continue to proactively take part in scalable computer exhibitions around the globe.

Fueled by buoyant consumer spending and its entry to the World Trade Organisation (WTO), the PRC continues to thrive as one of Asia's leading economies. Therefore, the Group will establish new sales and marketing channels in each of the major provinces and municipalities in the PRC in order to capture the growing demand for computer peripherals and networking products there. Together with stronger sales and marketing channels in the existing markets, the Group is confident of achieving better results for the coming year.