Management Discussion and Analysis

RESULTS AND DIVIDENDS

Audited net loss from ordinary activities attributable to shareholders for the year amounted to HK$322,718,000. Loss per share was 58.8 cents. The directors do not recommend the payment of any dividend for the year ended 31 December 2002.

OPERATING ENVIRONMENT AND DIVERSIFICATION

Over the past few years, worldwide economic instability, geopolitical environment risks and the overall uncertainty had certain impact on the Group's planned business diversification and progress. During the five year period since 1995, banking on the prospects of blazing technology, most investors pursued high-tech dot com investments in the absence of underlying earnings fundamentals; many mergers and acquisitions were consummated with high premium payouts in the telecommunication related field. Uptill the year 2000, many such investors had to review and make significant provisions on their investments. In addition, the "September 11" incident in 2001, the accounting scandals of major American enterprises in 2002, and more recently, the war in Iraq and the outbreak of severe acute respiratory syndrome (SARS) in 2003, all had direct negative impact on the economic performance and confidence of consumers. A number of global conglomerates last year faced dire financial crisis and even went bankrupt. Thus, investors' confidence and market performance are severely dented. With this in mind, in planning for the future, the Group needs to take an extremely conversative approach. Nevertheless, the capital market now seems to place focus on industries with solid performance and substantive growth. The market is still immensely interested in outstanding achievers and high return investment opportunities.

According to authoritative market researchers, the China market with a population of 1.3 billion people will be the focus of investors in the 21st century. Her pharmaceutical industry is one of the fastest growing dawning industries in the country. The industry is at the verge of gradual opening up on a unified basis, allowing competition by strength. Based on careful assessments, the Group having formed partnership with 中國葯材集團公司 (China National Group Corporation of Traditional and Herbal Medicine – "China National Medicine") in 2002 – 華頤葯業有限公司 (Huayi Pharmaceutical Company Limited) ("Huayi"), a sino-foreign joint venture, which has strategic implications enabling the Group to penetrate the high potential China pharmaceutical market. This formation enables the Group to diversify its business profile successfully, helps to achieve attractive returns on pharmaceutical business investments making it the Group's core business activity in the years to come.

BUSINESS REVIEW

The Group's turnover in 2002 was HK$185,187,000 (2001: HK$175,486,000), a slight increase of 6% from prior year, reflecting the progress of our new business formation. Since 1997, turnover of our Group experienced significant decline. In the later part of 2002, our new pharmaceutical business was successfully established and brought new impetus to the Group. On one hand, our sales turnover in an unfavorable business environment experienced a slight improvement; on the other hand, the pharmaceutical business also brought the Group earnings contribution. However, in the year, the Group suffered operating loss on its traditional electronics manufacturing business coupled with substantial provisions as deemed necessary by the management on past investment projects. As a result, loss attributable to shareholders was HK$322,718,000 (2001 (restated): HK$76,201,000).

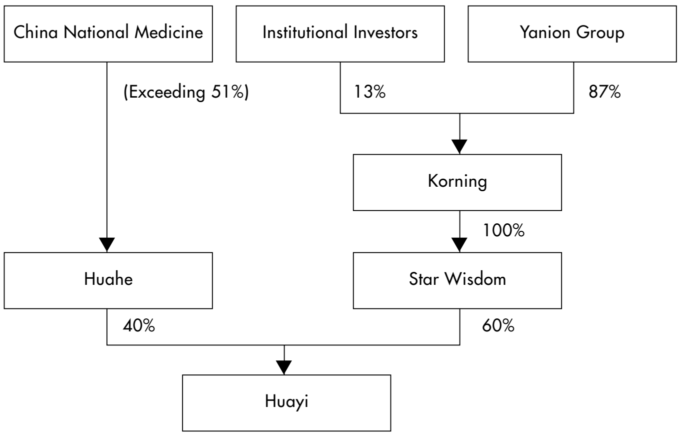
In the year under review, the Group energetically diversified and transformed its business profile with focus on the high growth potential industries in China. So far, the Group has successfully formed a cooperative strategic partnership with China National Medicine. By virtue of such cooperation, the Group could penetrate the huge Chinese pharmaceutical and health food market of 1.3 billion population to develop related businesses. In terms of traditional electronics manufacturing business, declining demand of electronic products coupled with cut-throat competition and sluggish consumption due to a worldwide gloomy economic climate affected the overall turnover performance.

PHARMACEUTICAL BUSINESS

On 26 July 2002, a sino-foreign joint venture, Huayi was formed, which in effect marked the Group's strategic partnership with China National Medicine. The affinity of cooperation stemmed from China National Medicine's relentless pursued of reform. It was looking for a pivotal platform to act as a catalyst allowing the quickening of modernization and internationalization. Reform is being pursued through different levels, to ensure the industry will continue to remain competitive post WTO. With China National Medicine's mission in mind, the Huayi joint venture becomes the natural platform. The new joint venture dispensed with many of the burden associated with state owned enterprises. Propelled by new capital, new operating philosophy and management culture, Huayi's strengths will become obvious. It is developing into an aggressive market orientation momentum guided by the principles of effectiveness and efficiency. Huayi is developing into a new force to be recognized with for commercialization of new concepts and products, and for the achievement of modernization and internationalization. Initially, Yanion and China National Medicine took over an operating entity, 北京華頤葯廠 (Beijing Huayi Pharmaceutical Factory) ("Beijing Huayi"), which is owned by 華禾葯業有限公司 (Huahe Pharmaceutical Co. Ltd.) ("Huahe"), a subsidiary of China National Medicine and restructured Beijing Huayi to form a new sino-foreign joint venture – Huayi. Through the process of personnel arrangement and facilities improvement, Huayi has become a very competitive Chinese pharmaceutical enterprise and would contribute significant earnings to the Group. It is conceived by the partners that in the near future, the Group could become China National Medicine's flagship for developing the Chinese medicine business overseas.

PHARMACEUTICAL BUSINESS (continued)

The Group acquired an 87% equity interest in Korning, which beneficially owns an indirect 60% interest of the aforesaid joint venture. The total investment and registered capital of Huayi are both RMB126,000,000. The structure of the joint venture is as follows:–



The PRC holding company, China National Medicine, formerly known as 中國葯材公司, is an authoritative and unequivocal leader in the Chinese pharmaceutical business in the PRC. It reports directly to the Large Enterprise Supervisory Committee of the State Council. China National Medicine was founded in 1955 and was a supervising body of the traditional Chinese medicine industry in the PRC. It has 39 corporate members including 11 wholly-owned subsidiaries, 11 controlling entities and 17 joint ventures. The principal business includes Chinese herbs, Chinese herbal medicine and patented Chinese medicines, etc. China National Medicine has been responsible for collecting business data relating to Chinese medicines for 38 years and is the institution carrying the largest medical technology/data information in China. Over the past half of a century, it has contributed immensely in the Chinese medical field benefiting the Chinese people at large.

China National Medicine established a system overseeing Chinese medical herbal plantation, production, operation and management in the PRC and has sales outlets widely spread over the PRC, Japan, South East Asia and Europe. Pursuant to the joint venture agreement and a subsequent arrangement, the PRC party, Huahe, has injected tangible and intangible assets into Huayi. This encompasses all approvals (including the approval from the State Drug Administration in Beijing in relation to the transfer of 16 medicines to Huayi), related medicine production certificates and other intellectual property rights, machineries and equipment, inventories and accounts receivable relating to the 16 Chinese medicines. These 16 Chinese medicines and their functions are listed below.

(i) 威麥寧膠囊 (for treating lung cancers);
(ii) 咽速康氣霧劑 (for treating sore throats);
(iii) 七厘膠囊 (for treating pains in joints and strained tendons);
(iv) 通樂顆粒 (for treating constipation problems);
(v) 小柴胡沖劑 (for treating fever and inflammation of the respiratory system);
(vi) 元胡止痛片 (for treating various pains);
(vii) 利膽排石片 (for treating cholelithiasis);

PHARMACEUTICAL BUSINESS (continued)

(viii) 感冒止咳沖劑 (for treating influenza);
(ix) 感冒止咳沖劑 (無糖型) (for treating influenza);
(x) 清熱化痰口服液 (for treating acute bronchitis);
(xi) 芪冬解毒口服液 (for treating myocarditis caused by virus);
(xii) 玉屏風口服液 (for treating influenza);
(xiii) 威麥寧粉 (for treating lung cancers);
(xiv) 明目上清片 (for treating eye related diseases);
(xv) 銀翹解毒膠囊 (for treating fever, headaches and sore throats); and
(xvi) 冠保顆粒 (for treating angina pectoris and coronary heart disease).

As the 16 Chinese medicines are well protected by intellectual property rights, they can be widely promoted to a variety of hospitals, clinics, citizens and users all over China. Since the mainland market is very substantial, sales prospect of such medicines is most encouraging.

It was mutually agreed that China National Medicine and Huahe would use their best efforts and experience in the pharmaceutical business to support Huayi to achieve a profit target of RMB50,000,000 in the first 12 months of its establishment. This has been incorporated in the joint venture agreement.

After the establishment of Huayi, its business has been very promising and recorded a profit of HK$13,948,000 before amortisation of goodwill and intangible assets, and depreciation for the first five months ended 31 December 2002. Within the past 5 months, the sino-foreign joint venture only marketed 4 items out of the above 16 Chinese medicines and the result was promising. This clearly confirms that the equity joint venture is successful in pioneering the reform. Through secondments of leaders from within the China National Medicine organization, knowledgeable and experienced experts are assigned to the joint venture. With clear reform mission, a new style of management focus is evident – actions are guided by efficiencies, customer focus and market orientation. The joint venture is expected to thrive in the expanding Chinese Medicine industry. Due to business development, high quality staff was recruited in China to reinforce the management and sales teams to cover more regional areas expanding its influence. Room for further development of new business is perceivable enormous. The Board believes that the partnership enables the Group to establish a more solid business cooperation foundation and a close, unique relationship with China National Medicine. At the same time, it helps to achieve reform, modernization and internationalisation. By leveraging on China National Medicine's advance technology, information, supply and distribution channels and resources, the Group's long term competitive advantage in the pharmaceutical industry would be strengthened. As more related business development opportunities are being evaluated, the earning prospects of the Group could be improved.

ELECTRONICS MANUFACTURING BUSINESS

Sale of the existing high-end audio and visual products of the Group for 2002, which included CD/VCD players/ mechanisms, amplifiers and other high-end mini-audio products amounted to HK$116,946,000, representing 63% of the Group's turnover (2001: HK$84,985,000 and 49% respectively). Sale of components and parts, including cassette deck mechanisms, car audio mechanisms, high precision springs and different types of metal and plastic parts, amounted to HK$42,191,000, representing 23% of the Group's turnover (2001: HK$58,588,000 and 33% respectively). Sale of other non-audio products amounted to HK$1,800,000, representing 1% of the Group's turnover (2001: HK$31,913,000 and 18% respectively). Sale of the Chinese pharmaceutical medicines amounted to HK$24,250,000, equivalent to 13% of the Group's turnover (2001: Nil).

Geographically, sales to America, Europe, China, Hong Kong and other Asian markets for the Group were 35%, 30%, 20%, 10%, and 5% respectively (2001: 17%, 41%, 14%, 21% and 7% respectively).

In respect of traditional manufacturing business, the Group will strive to secure more original design manufacturing (ODM) and original equipment manufacturing (OEM) orders from internationally renowned clientele. Positive contribution to the Group from Chinese pharmaceutical medicines versus the prospect that traditional manufacturing business, which having performed unsatisfactorily in the past five years and is not expected to turn around in the foreseeable future due to the very poor market condition. The Board will, at appropriate time, assess whether traditional electronics manufacturing is still in the best interest of the Group over the long term. Also, the Board will consider proposals including identifying suitable strategic co-operative partners or interested appropriate investors to unload the electronic manufacturing business for reasonable considerations as to avoid the risk of further pro-longed drain of resources of the Group in the future.

OTHER BUSINESES

Following the downturn of the global economy and the surfacing of unanticipated risk factors, the Group's past investment projects faced certain degree of difficulties in operation and competition. During the period covering our business diversification plan, the Group had invested in a re-engineering project of cable television stations in China in 2000 and an internet phone business in 2001. Faced with the adverse operating environment, the Group unavoidably suffered losses from these projects. Considering the re-orientation of the longer term business focus of the Group as discussed in the pharmaceutical business section, the management has adopted the prudent policy of making provisions on certain investments/assets including the following two items. In the future, the management will adopt a much more stringent assessment and critical appraisal criteria of any potential investment opportunities.

a. *Internet Phone*

This business principally involves the selling and distribution of internet phone sets and prepaid stored value phone cards in major cities in the PRC. Owing to latest intense competition and price cutting in the domestic fixed line and mobile phone markets, the inability to launch our low cost, new products quick enough due to major adjustments to product design, this investment had been negatively impacted. So far, the Group has destined minimal investment in this item resulting in insufficient resources for further development. Should such business be significantly developed, it would require additional investment funds and result in much higher risks that the Group would face. As such, the management now closely monitors changes in the market and the future prospect of telecommunication business in China. To adopt a prudent and conservative accounting policy, a provision of HK$14,015,000 has been made.

OTHER BUSINESES (continued)

b. Video-on-demand System

Video-on-demand ("VOD") system is an investment in the re-engineering of cable television stations in the PRC. By the end of 2002, the Group beneficially owned a 27% interest in the associated company, Global Cyber. The principal asset of Global Cyber is an 80% equity interest in Shanghai Dazheng, a sino-foreign joint venture. The PRC party is a Shanghai company with many years' experience in research, development and implementation of digitized VOD system in the PRC, involving the re-engineering of the cable television stations in the PRC by employing related softwares, servers and set top boxes. However, the main frame product has not yet been officially approved by the controlling authority in China and for recognition as certified for China cable television stations. In addition, the Group is currently in dispute with the PRC party in relation to the ownership of the underlying intellectual property rights of the VOD softwares. The business is temporarily suspended. The Group has on several occasions sought solution including the retention of PRC lawyers to take legal proceedings in the PRC to protect the investment interests of the Group. In view of the possible long drawn out legal proceedings and, after consultation with the Group's auditors, the Group adopted the prudent and conservative accounting policy to make full provision on the total investment of HK$250,000,000.

LIQUIDITY AND FINANCIAL RESOURCES

As at 31 December 2002, the Group's current assets amounted to HK$143,067,000, representing an increase of approximately HK$61,343,000 as compared to the end of last year. Accounts receivable increased by HK$22,996,000 to HK$32,571,000, representing 17.6% of the turnover HK$185,187,000; cash and cash equivalents increased by HK$5,237,000 to HK$31,658,000; pledged deposits decreased by HK$9,203,000 to HK$4,636,000; inventories increased by HK$3,330,000 to HK$31,406,000; prepayments and other receivables increased by HK$15,568,000 to HK$19,381,000; short term investment increased to HK$23,415,000. Save for the planned capital commitment of HK$52,374,000 for the pharmaceutical business, the Group does not have any commitment at present.

Current liabilities amounted to HK$85,622,000, representing an increase of HK$15,614,000 compared to the end of last year. Accounts payable increased by HK$15,533,000 to HK$36,811,000; other payables and accruals increased by HK$7,367,000 to HK$25,907,000; interest-bearing bank loans and other borrowings decreased by HK$13,656,000 to HK$12,615,000; amount due to related companies and a director increased by HK$6,282,000 to HK$7,285,000. Net current assets amounted to HK$57,445,000, representing an increase of HK$45,729,000 as compared to the end of last year. Most liabilities were short term in nature and were mainly in Hong Kong dollars. Bank loans were Hong Kong prime rate based. As at 31 December 2002, current asset of the Group expanded while current liabilities remained relatively stable. The current ratio (the ratio of current assets to current liabilities) was approximately 1.67, a significant improvement over prior year.

Non-current assets, amounted to HK$176,070,000, representing a decrease of HK$247,759,000 as compared to the end of last year. Deposits decreased by HK$101,500,000; goodwill increased by HK$91,307,000 to HK$98,539,000; fixed assets reduced by HK$9,186,000 to HK$53,826,000; intangible assets increased by HK$21,620,000 to HK$22,705,000; interests in associates decreased by HK$250,000,000. The Group's non-current liabilities were HK$2,268,000, resulting in the overall gearing ratio (the ratio of total liabilities to shareholders' equity) to be approximately 49%.

In respect of contingent liabilities, as at 31 December 2002, bills discounted with recourse was HK$3,685,000, an increase of HK$1,264,000 from last year. The Company has given guarantees to three banks for a total sum of HK$34,000,000 in connection with facilities granted to subsidiaries, of which only one bank guarantee for the sum of HK$15,027,000 was utilized as at 31 December 2002.

LIQUIDITY AND FINANCIAL RESOURCES (continued)

The Group's liquidity remained stable and its financial resources were improving. The Board considered that raising funds by way of placements would enable the Group to allocate more resources to high earning potential and high growth businesses.

CAPITAL STRUCTURE AND PLACING OF SHARES

On 12 June 2002, in order to cope with the business development of the Group, the Group successfully placed 50,900,000 new shares in the capital market and raised HK$69,500,000 to acquire 87% interest in Korning, which effectively owns 60% of Huayi, to meet the capital contribution requirement by the Group and for general working capital purposes. The number of issued shares has increased to 571,650,673 as at 31 December 2002. However, the Group adopted the prudent accounting policy to make full provisions on the balance of certain past invested projects such that the shareholders' equity of the Group decreased to HK$179,010,000.

PLEDGE OF ASSETS

At as 31 December 2002, the Group pledged assets to banks with total book value of HK$11,708,000 (2001: HK$21,924,000), including the industrial property located in Hong Kong with carrying amount of HK$7,072,000 (2001: HK$8,085,000) and bank deposits of approximately HK$4,636,000 (2001: HK$13,839,000), to secure the Group's general bank facilities.

PROSPECTS

As the Group mainly focuses on mainland China for business development, it has leveraged on the alliance with China's leading pharmaceutical enterprise – China National Medicine. China National Medicine has seconded a group of outstanding personnel to staff Huayi. On basis of their working experience, professional qualifications and industry knowledge, it would enable Huayi to maximize its earning ability and competitive edge. As the cultural backgrounds of the personnel of the joint venture may vary, it would take certain lead time to consolidate the sino-foreign cultures before it will maximize on its potentials. However, Huayi could explore more business opportunities including the extension of its sales/distribution network, research and development of new effective Chinese pharmaceutical medicine, upgrade modern and scientific management quality, change in traditional distribution methods and adoption of new chain business models of production, supply and sales to increase long term competitive edge. Also, it involves strengthening marketing and promotion to establish Chinese medicine brand recognition and the creation of numerous high potential investment opportunities. The Group is currently in negotiation with China National Medicine on several cooperative plans. It includes the possibility of further injection into Huayi additional Chinese pharmaceutical medicines. It would speed up the leading role of Huayi in the field. For long term benefits, both Yanion and China National Medicine recognize that Huayi will be nurtured into a major enterprise. Should there be any concrete business plans or any agreements being entered into, formal announcements will be published as soon as possible. The Board believes and is confident that the Chinese pharmaceutical medicine business invested by the Group would bring attractive earnings and substantial growth.

PROSPECTS (continued)

Since the Chinese economy continues to grow, it provides plenty of high return investment opportunities. Thus, the Group would consider, where appropriate, to raise more equity funds from the capital market to strengthen our capital base and enhance cash flow to cope with diversified development plans of our China pharmaceutical medicine business. By virtue of capturing investors' interest in the dawning industry and potential earning prospects, the Group believes that return for shareholders can be maximized.

EMPLOYEES

As at 31 December 2002, there were approximately 1,500 management, administrative, production and selling staff located in Hong Kong and the PRC. The Company has adopted an employee share option scheme and housing benefits were provided for certain Hong Kong and PRC employees. Salaries of employees were determined taking into account job performance and professional experience of the employees concerned and the general practice within the industry. Since December 2000, all employees and directors in Hong Kong have joined the mandatory provident fund scheme implemented by the Hong Kong Government.

APPRECIATION

The Directors wish to express their sincere thanks to the banks, customers, suppliers and all parties concerned for their support and to all staff of the Group for their hard work during the year.

ON BEHALF OF THE BOARD

Cheng Kwok Choi
Director

Hong Kong
23 April 2003