

MANAGEMENT DISCUSSION AND ANALYSIS

OVERALL PERFORMANCE

Following to the restructure of the Group's business in 2003, the Group's results were significantly improved. The turnover for the year ended 31 December 2003 increased by 100% to HK\$625.0 million compared to last year turnover of HK\$311.9 million and the gross profit for the year ended 31 December 2003 increased by 6% to HK\$56.7 million compared to last year gross profit of HK\$53.5 million. The Group's audited consolidated loss after tax and minority interests for the year was narrowed by 73% to HK\$22.8 million (2002: loss of HK\$86.0 million).

The result improvement was mainly due to acquisition of the distribution business ("Distribution business") of information technology ("IT") products which was completed in July 2003 and recorded a turnover of HK\$444.6 million and segmental profit of HK\$5.4 million in the second half year of 2003. On the other hand, the segmental loss of software solutions and services business ("Software business") reduced by 77% to HK\$6.8 million (2002: loss of HK\$30.2 million). Also, there is no impairment of goodwill in 2003 (2002: HK\$36.5 million). As a result, the loss before tax for continuing operations for the year ended 31 December 2003 reduced by 97% to HK\$2.4 million as compared to loss of HK\$68.6 million in 2002.

OPERATING REVIEW AND PROSPECTS

CONTINUING OPERATIONS

(A) Distribution of information products ("Distribution business")

In July 2003, the Group completed the acquisition of the Distribution business by acquiring the entire interests of Beijing Founder Century Information System Co. Ltd. and Founder Century (Hong Kong) Limited from its controlling shareholder – Founder Holdings Limited ("FHL"). The Group recorded the results of the Distribution business for the first time in the second half of year 2003 and this sector contributed turnover of HK\$444.6 million and segmental profit of HK\$5.4 million to the Group.

The Distribution business is mainly focused on the distribution of IT products include servers, workstations, data storage devices and networking products of various international brand names such as HP, IBM, 華為3 COM, SUN, Netgear and Apple. Significant efforts were made by management to reduce the inventory level and tighten up the credit control systems. Also, the management has strengthened the logistic process to enhance the efficiency and reduction of overhead costs. As a result, the 2003 annual result of the Distribution business was significantly improved by an increase of 47% in turnover to HK\$756.8 million (2002: HK\$514.6 million) and turnaround to record segmental profit of HK\$6.9 million (2002: loss of HK\$20.7 million).

The Distribution business has gained its ranking from the 11th place in 2002 to the 7th place in 2003 among the top 100 enterprises in the distribution business in PRC. Besides the headquarter in Beijing, it has established branch offices in Shanghai, Guangzhou and Chengdu.

The internal demand for IT products in the PRC will remain strong as the PRC's gross domestic products is expected to continue to increase at an annual growth rate of approximately 7% to 8% for the next ten years. Also, after PRC's accession into the World Trade Organisation and the running up of the Olympic Games of 2008 to be held in Beijing, it is expected the investments in the IT sector will grow with a double digit compound annual rate over the next five years. Hence, it is expected the Distribution business will continue to grow with the IT market in the future.

(B) Software solutions and services business (“Software business”)

The turnover of Software business for the year decreased by 12% to HK\$62.2 million (2002: HK\$70.8 million) and segmental loss reduced by 77% to HK\$6.8 million (2002: loss of HK\$30.2 million).

The Software business was still facing fierce competition in the PRC market and the turnover in 2003 decreased by 12% than last year. The Group has cautiously reduced the operating expenses by: streamlined the departmental structure by closing down those loss making departments and reduced the headcount by 16%. As a result, the segment loss in 2003 was reduced by 77% compared to 2002.

The Software business mainly focused on the provision of systems integration services – especially for the financial institutes, selling and distribution of self-developed information security products – Founder FireGate (方正方御防火牆) and selling and distribution of other software products such as Geographic Information System. The system integration services is based on the application software systems to develop consolidated solutions for e-government, e-finance and enterprises. The applications are mainly used in the area of government, resources companies and digitalise cities. At the same time, it also provides comprehensive financial products, customer services products and solutions for institutes and companies such as banks, brokerage and securities, fund management and insurance industries. The self-developed information security products is a leading network security solution in the PRC. The product can be applied as a professional system in different industries and at the same time it can be applied as total solution for small and medium enterprises. Our software business clients include China Construction Bank (中國建設銀行), The People’s Bank of China (中國人民銀行), oil & petroleum companies such as PetroChina (中國石油天然氣公司), telecommunication companies and Government bureaus – such as Military Police bureau (武警), tax bureau and education bureau.

The merger of Distribution business and Software business is complementary to each other. The Software business can now leverage on the strong selling and distribution channels of the Distribution business. On the other hand, the Distribution business has solid technical support and services from the Software business to provide more comprehensive and total solutions to the clients.

DISCONTINUED OPERATIONS

(A) Electronic products business

The Group decided to concentrate the resources on the IT business and therefore disposed of the Electronic products business which was completed in September 2003.

The turnover of Electronic products business for the year decreased by 39% to HK\$118.1 million (2002: HK\$192.8 million) and segmental loss of HK\$18.3 million (2002: profit of HK\$4.6 million). The loss was mainly due to increase in the material costs, overhead costs and the disposal loss of business.

(B) Electronic components business

The Electronic components business was disposed of in June 2002 and therefore no turnover of Electronic components business was not recorded in the year 2003 (2002: HK\$48.3 million) and no record of segmental results (2002: segmental loss of HK\$17.0 million).

MANAGEMENT DISCUSSION AND ANALYSIS

FINANCIAL REVIEW

Liquidity, financial resources and capital commitments

As at 31 December 2003, the Group recorded total assets of HK\$457.9 million (2002: HK\$223.9 million) which were financed by liabilities of HK\$281.8 million (2002: HK\$85.3 million) and equity of HK\$176.1 million (2002: HK\$138.6 million). The Group's net asset value as at 31 December 2003 increased by 27% to HK\$176.1 million as compared to HK\$138.6 million as at 31 December 2002.

The Group had total cash and bank balances of HK\$159.5 million as at 31 December 2003 (2002: HK\$62.9 million). The Group had no bank loan and overdraft as at 31 December 2003 (2002: HK\$12.2 million), hence the Group recorded a net cash balance of HK\$159.5 million as at 31 December 2003 as compared to HK\$50.7 million as at 31 December 2002. As at 31 December 2003, the Group's current ratio was 1.50 (2002: 1.79) and the Group had no long term debt as at 31 December 2003 as compared to a long term debt to equity ratio of 0.4% in 2002 with equity being defined as the total of capital and reserves.

As at 31 December 2003, the Group did not have any material capital expenditure commitments.

Treasury policies

The Group adopts conservative treasury policies and controls tightly over its cash and risk management. The Group's cash and cash equivalents are held mainly in Hong Kong dollars, Renminbi and United States dollars. Surplus cash is generally placed in short term deposits denominated in Hong Kong dollars and United States dollars.

Contracts

As at 31 December 2003, the major contracts in hand for the Software business amounted to HK\$13 million, which are all expected to be completed within eighteen months.

Material acquisitions and disposals of subsidiaries and associates

In July 2003, the Group completed the acquisition of Distribution business from the controlling shareholder of the Company, FHL. The total fair consideration of acquisition in the amount of HK\$74,720,000 was satisfied by issuing 280,000,000 ordinary shares of the Company and cash consideration of HK\$10,320,000. The results of the Distribution business contributed a segmental profit of HK\$5.4 million to the Group for the year 2003 and the Group recorded goodwill on acquisition of HK\$3.2 million.

In September 2003, the Group completed the disposal of Electronic products business to a director of the Company for a total cash consideration of HK\$45.5 million. The results of the Electronic products business recorded a segmental loss of HK\$18.3 million to the Group for the year 2003.

Employees

As at 31 December 2003, the Group had 238 and 187 employees for the Distribution business and Software business, respectively. These employees of which almost all work in the Mainland China. The Company has also established share option schemes and the share options are granted at Directors' discretion to motivate and reward the employees with outstanding performance.

Charges on Assets

As at 31 December 2003, bank deposits of approximately HK\$17.4 million were pledged to banks to secure general banking facilities granted.

MANAGEMENT DISCUSSION AND ANALYSIS

Exposure to fluctuations in exchange rates and related hedges

Most of the Group's borrowings are denominated in Hong Kong dollars, Renminbi and United States dollars while the turnover of the Group are mainly denominated in Hong Kong dollars, Renminbi and United States dollars. As the exchange rates of United States dollars and Renminbi against Hong Kong dollars were relatively stable during the year under review, the Group's exposure to fluctuations in exchange rates is considered minimal and no financial instruments have been used for hedging purposes.

Contingent liabilities

As at 31 December 2003, the Company had contingent liabilities in relation to guarantees given to suppliers in connection with credit facilities granted to certain subsidiaries amounting to HK\$19.4 million.