

Review of Operations

In 2003, the business environment for mobile handset business was difficult. The mobile handset market in China was adversely affected by the threat of atypical pneumonia worldwide and the market was further hampered by the price reduction strategy adopted by the majority of mobile handset manufacturers and the entrance of new mobile handset manufacturers into the PRC market. The combined impact of these factors have led to the Group accumulating inventory of certain models of its products at a higher level than originally anticipated and a provision was made for these slow-moving stocks. Measures have already been taken to control risk of excessive inventory in the future. In particular, pursuant to the products distribution agreement made with Qingdao Haier Telecommunications Co., Ltd. ("Haier Telecom", a subsidiary of Haier), most of the products are now sold to Haier Telecom and the Group will no longer be responsible for the inventory ordered by Haier Telecom, thus, significantly reducing our business risks.

In 2003, apart from the original design manufacturing ("ODM") of mobile handsets, we also expanded into the electronic manufacturing services ("EMS") business to manufacture mobile handsets for both international and domestic telecom companies. The EMS orders received so far have been encouraging. Other than the huge domestic market in which our strength lies, we also started to export a substantial volume of mobile handsets to overseas countries in 2003. Our business now principally includes: (i) sales of ODM mobile handsets under "Haier" brand name domestically; (ii) products manufactured under EMS arrangement for domestic telecom companies; (iii) export of ODM mobile handset products under "Haier" brand name; and (iv) products manufactured under EMS arrangement for international telecom companies.

In order to increase our share in the domestic market and to penetrate the international market, we have invested considerably in research and development. New features such as 40 polyphonic sounds, 65K true colour LCD displays, an improved version of incoming call fire walls, GPRS class 8 support and inlet 5-mode digital camera features were developed during 2003. New models of mobile handsets incorporating these popular new features were launched under our Tian Cai Xing series, Cai Zhi Xing series, Cai Duo Xing series and Ling Qiao Xing series in 2003 with very encouraging feed-back from our customers. In future, we will continue to develop more innovative and quality products with original and useful features in order to capture more market share.

