

FINANCIAL REVIEW

Comparison between Current Year and Last Period

The Group's balance sheet as at 31 December 2002 reflected only the ESL's assets and liabilities but did not include the assets and liabilities of the ESH Group, the acquisition of which was completed on 30 June 2003. Subsequent to the acquisition of the ESH Group, both assets and liabilities of the Group have been enlarged significantly due to the inclusion of the sizable operation and business of the ESH Group.

The profit and loss account for the year ended 31 December 2003 was derived mainly from the full year results of ESL plus the second half year results of the ESH Group. The profit and loss account for the fifteen months ended 31 December 2002, on the other hand, reflected only the results of approximately seven months of ESL after the Group Restructuring. With the contribution from the ESH Group after being acquired on 30 June 2003, the turnover and other profit and loss items of the Group in 2003 have increased significantly, which reflected the substantial increase in operations after acquisition of the ESH Group.

In light of the acquisition of the ESH Group by the Company, both the financial position and results of the Group for the current year have changed tremendously in comparison with that of the last period.

Acquisitions and Disposals of Material Subsidiaries and Associated Companies

Pursuant to an agreement signed on 15 May 2003 with CCT Telecom, the Company acquired from CCT Telecom the entire interest in ESH and its subsidiaries including the assignment of the interest-free shareholder's loan due from the ESH Group to the Company, at a consideration of HK\$768.0 million to be satisfied by the issue of the Company's convertible notes. The ESH Group is principally engaged in the design, development, manufacture and sale on an ODM and OEM basis of cordless telecom products including cordless phones and family radio systems. The acquisition was completed on 30 June 2003 and further details were set out in the Company's circular dated 11 June 2003.

Apart from the acquisition above, there were no other material acquisitions and disposals of subsidiaries and associated companies during the year.

The Prospects of the Group's Business

After completion of the acquisition of the ESH Group, the Group has become a major manufacturer of cordless telecom products on an ODM and OEM basis. Through the acquisition of the ESH Group and its extensive business network, solid market position and strong research and development capability, the prospects of the Group's telecom products business will be promising. The Group will continue to develop diversified hi-tech and innovative telecom products. The Company expects that the Group's business will continue to grow.

Summary of Results

<i>HK\$'000</i>	Year ended 31 Dec 2003	Period from 1 Oct 2001 to 31 Dec 2002	% Change
Turnover	1,926,258	106,385	+1,711%
Profit/(loss) from operating activities	111,380	(16,686)	N/A
— net gain attributable to the Group Restructuring	—	119,472	-100%
— finance costs	(29,020)	(3,093)	+838%
Profit before tax and minority interests	82,360	99,693	-17%
— tax and minority interests	(9,618)	(1,535)	+527%
Net profit attributable to shareholders	72,742	98,158	-26%

Turnover of the Group increased sharply to approximately HK\$1,926.3 million for the year under review, representing a growth rate of approximately 1,711% in comparison with that of the last period, which was mainly attributable to the business of telecom products acquired from CCT Telecom during the year. The Group managed to turnaround the operating loss of approximately HK\$16.7 million of the prior period (incurred before the Group Restructuring by the previous management and the then receivers) into an operating profit of approximately HK\$111.4 million and a net profit attributable to shareholders of approximately HK\$72.7 million for the year under review.

Turnover of approximately HK\$106.4 million of the prior period was solely derived from the few months operation of ESL after completion of the Group Restructuring in May 2002. Net profit attributable to shareholders of approximately HK\$98.2 million recorded in the prior period was mainly due to the one-off restructuring gain arising from the Group Restructuring.

Analysis by Business Segment

<i>HK\$'000</i>	Turnover and other revenue		Profit/(loss) from operating activities	
	Year ended 31 Dec 2003	Period from 1 Oct 2001 to 31 Dec 2002	Year ended 31 Dec 2003	Period from 1 Oct 2001 to 31 Dec 2002
Telecom products	1,937,149	106,020	119,073	6,991
Corporate items	—	2,760	(7,693)	(23,677)
	1,937,149	108,780	111,380	(16,686)

Analysis by Business Segment *(Cont'd)*

Subsequent to the acquisition of the ESH Group, the Group focused on business from the sale, manufacture, design and development of cordless telecom products on an ODM and OEM basis, which formed the major source of revenue to the Group and contributed to almost 100% the Group's turnover for the year (2002: almost 100%). The telecom products business contributed an operating profit of approximately HK\$119.1 million for the year ended 31 December 2003 (2002: approximately HK\$7.0 million). The loss of corporate segment decreased to approximately HK\$7.7 million for the current year (2002: loss of approximately HK\$23.7 million) as a result of savings on head office expenses and absence of one-off restructuring expenses that was incurred in the last period.

Analysis of Turnover and Other Revenue by Geographical Segment

<i>HK\$'000</i>	Year ended		Period from	
	31 Dec 2003	Relative %	1 Oct 2001 to 31 Dec 2002	Relative %
United States	1,244,344	64%	—	—
PRC (including Hong Kong)	354,778	19%	108,780	100%
European Union	64,996	3%	—	—
Others	273,031	14%	—	—
Total	1,937,149	100%	108,780	100%

As the ESH Group is one of the world's major suppliers of cordless telecom products, most of the Group's turnover was derived from the export of telecom products to its world-wide customers for the year under review. In contrast, turnover of the last period came mainly from the sale of electric components by ESL to the ESH Group. This explains the significant changes in geographical mix of turnover between the current year and the last period. The United States was the primary market of the Group, accounting for approximately 64% (2002: 0%) of the Group's total turnover for the current year. The PRC (including Hong Kong) ranked the second accounting for approximately 19% (2002: 100%) of the Group's total turnover.

Liquidity and Financial Resources

<i>HK\$'000</i>	At 31 Dec 2003	At 31 Dec 2002
Current assets	1,306,369	101,482
Current liabilities	1,105,313	37,488
	118%	271%

The Group's cash balance increased significantly to approximately HK\$549.8 million at 31 December 2003 (2002: approximately HK\$68.0 million) attributable to the inclusion of cash balance of the ESH Group. Cash generated from the Group's operations and funds available from bank facilities are expected to be sufficient to cover all cash requirements, including working capital and capital expenditure needs. Current ratio (a ratio of current assets over current liabilities) as at 31 December 2003 stood at 118% (2002: 271%), remains healthy and reflects the inclusion of the ESH Group.

Capital Structure and Gearing Ratio

HK\$'000	At 31 Dec 2003		At 31 Dec 2002	
	Amount	Relative %	Amount	Relative %
Bank borrowings	111,181	10%	2,578	2%
Convertible notes	831,000	77%	65,000	57%
Finance lease payables	1,274	0%	—	—
Total borrowings	943,455	87%	67,578	59%
Equity	142,143	13%	46,401	41%
Total capital employed	1,085,598	100%	113,979	100%

At the balance sheet date, the total outstanding convertible notes issued by the Company amounted to HK\$831.0 million (2002: HK\$65.0 million) which comprised:

- (i) HK\$45.0 million zero coupon convertible notes due 2005 to CCT Telecom, with a conversion price of HK\$0.01 per share;
- (ii) HK\$8.0 million at 5% per annum convertible notes due 2004 to an independent third party, with a conversion price of HK\$0.01 per share;
- (iii) HK\$10.0 million at 2% per annum convertible notes due 2005 to several independent third parties, with a conversion price of HK\$0.01 per share; and
- (iv) HK\$768.0 million at prime or best lending rate plus 2% per annum convertible notes due 2008 to CCT Telecom, with a conversion price of HK\$0.014 per share.

Due to the inclusion of borrowings of the acquired ESH Group, the Group's outstanding bank borrowings increased to approximately HK\$111.2 million at 31 December 2003 (2002: approximately HK\$2.6 million). All of the bank borrowings of the Group were arranged on a short-term basis for ordinary business operations and are repayable within one year. There is no material effect of seasonality on the Group's borrowings requirements.

Certain of the ESH Group's assets were acquired by way of finance leases and the total outstanding finance lease payables for the Group at 31 December 2003 amounted to approximately HK\$1.3 million (2002: Nil).

The Group's gearing ratio, calculated on the basis of the Group's total borrowings over total capital employed (equity plus total borrowings), increased to 87% at 31 December 2003 (2002: 59%). The sharp increase in total borrowings was mainly attributable to: (i) the issue of HK\$768.0 million convertible notes to CCT Telecom as the consideration for the acquisition of the ESH Group; and (ii) the inclusion of the bank borrowings of approximately HK\$111.2 million of the acquired ESH Group. Of the outstanding convertible notes, approximately HK\$813.0 million in principal amount is due to the Group's ultimate holding company, CCT Telecom, and are attached with a relatively long maturity period of redemption. In other words, the Group will not have immediate repayment pressure.

Use of Proceeds

The Group raised net proceeds of approximately HK\$57.8 million as a result of the placement of convertible notes and shares in 2002 and 2003. All such proceeds have been used by the Group in accordance with the intended purposes as announced on 6 June 2002 and 17 April 2003, respectively.

Capital Commitments

There were outstanding capital commitments related to the purchases of moulds, equipment and machinery and the total amount contracted by the Group but not yet provided for in the accounts was approximately HK\$2.3 million as at 31 December 2003 (2002: Nil), all of which would be financed internally.

Treasury Management

The Group employs a conservative approach to cash management and risk control. To achieve better risk control and efficient fund management, the Group's treasury activities are centralised.

During the year, the Group's receipts were mainly denominated in United States dollar, with some in Hong Kong dollar and Euro dollar. Payments were mainly made in Hong Kong dollar and United States dollar, with some in Renminbi and Euro dollar. Cash was generally placed in short-term deposits denominated in Hong Kong dollar and United States dollar. At 31 December 2003, all of the Group's outstanding borrowings were denominated in Hong Kong dollar. Other than the convertible notes in principle amount of HK\$18.0 million with fixed interest rate and HK\$45.0 million with zero interest rate, the Group's borrowings were principally made on a floating rate basis.

The objective of the Group's treasury policies is to minimize risks and exposures due to the fluctuations in foreign currency exchange rates and interest rates. The Group does not have any significant interest rate risk as the interest rate is stable and remains at low level. Since Hong Kong dollar remains pegged to United States dollar, the Group does not foresee a substantial exposure in United States dollar receipts and payments. The Group's exposure to foreign exchange risk is not substantial and forward exchange contracts will be entered into to minimize such risk when necessary and appropriate.

Significant Investment

The Group did not hold any significant investment at 31 December 2003 (2002: Nil).

Pledge of Assets

At 31 December 2003, certain of the Group's time deposits of approximately HK\$100.2 million, all of which belonging to the ESH Group, (2002: approximately HK\$5.0 million) were pledged to secure general banking facilities granted to the Group.

Contingent Liabilities

At 31 December 2003, the Group had contingent liability in respect of possible future long service payments to employees, mainly of the ESH Group, amounted to approximately HK\$4.7 million (2002: approximately HK\$0.2 million). Save as aforesaid, the Group did not have any other significant contingent liabilities at 31 December 2003.

Employees and Remuneration Policy

The total number of employees in the Group, including those employees of the ESH Group, as at 31 December 2003 was 15,545 (2002: 1,107). Remuneration packages are normally reviewed on an annual basis. Apart from salary payments, there are other staff benefits including provident fund, medical insurance and performance related bonus. Share options may also be granted to eligible employees and persons of the Group. At 31 December 2003, there were outstanding share options of approximately 1,083 million (2002: Nil).

Auditors' Modified Opinion Regarding the Comparative Amounts

In the opinion of auditors, the financial statements give a true and fair view of the state of affairs of the Company and of the Group at 31 December 2003 and of the profit and cash flows of the Group for the year then ended and have been properly prepared in accordance with the disclosure requirements of the Hong Kong Companies Ordinance.

Without qualifying their opinion for the year ended 31 December 2003, the auditors draw attention to the fact that their opinion on the financial statements of the Group and the Company for the fifteen months period from 1 October 2001 to 31 December 2002 included in the auditors' report dated 15 April 2003, was disclaimed due to certain limitations of scope. Accordingly, the comparative amounts shown in these financial statements may not be comparable with the amounts for the current year.

In particular, since S. Meggatel Sdn. Bhd., a 70%-owned subsidiary of the Group in Malaysia, had incomplete books and records for the period from 1 October 2001 to 31 December 2002, the auditors were unable to satisfy themselves as to the nature, completeness, appropriateness, classification and disclosure in respect of the transactions undertaken by S. Meggatel Sdn. Bhd. for the period from 1 October 2001 to 31 December 2002 and the related balances as at 31 December 2002. During the current year, this subsidiary became immaterial to the Group and accordingly the scope limitations in the prior period had no material impact to the Group's current year's financial statements.