



CHAIRMAN'S STATEMENT

On behalf of the Board of Directors of Artel Solutions Group Holdings Limited (the "Company"), I am pleased to present the annual report of the Company and its subsidiaries (the "Group") for the year ended 31 December 2003.

BUSINESS REVIEW

The Group's turnover for 2003 was HK\$2,203 million, representing an increase of 4%, as compared with HK\$2,122 million for the same period last year. The slight increase was mainly attributable to the impact resulted from the occurrence of the SARS epidemic during the year. The net profit for the year decreased from HK\$66 million to HK\$50 million as the rebate from Intel remained low.

Distribution of Intel Products

The year of 2003 was a challenging year for the computer component distribution business due to the outbreak of SARS and the low Intel rebate. After the spread of SARS was under control, fierce competition among distributors caused the drop in selling prices. As a result of the decrease in Intel rebate and selling prices, the Group's gross profit margin dropped from 5.7% to 4.2%.

For the past few years, sales of Intel products contributed more than 95% of total turnover and recorded robust growth annually. In order to reduce the reliance on Intel product lines and in light of the growing digital home market, the Group has strategically planned to diversify to the distribution of thin film transistor liquid crystal display ("LCD") products that command higher profit margins.

During the year under review, distribution of Intel products was still the Group's core business, contributing around 90% of total turnover. The Group believes that profit margins of Intel products bottomed in 2003 and will be improved in 2004 with Intel's new sales rebate policy for distributors globally.

Distribution of LCD Monitors

The cooperation with Chi Mei Corporation ("Chi Mei") is another milestone since the establishment of the Group. After entering into agreement with Chi Mei, the distribution business is divided into two major areas: Intel products and Chi Mei's LCD products.

The Group has commenced to distribute Chi Mei's LCD monitors in China since March last year. This strategic move could further utilize the existing personal computer ("PC") component distribution channels including Genuine Intel Dealers, system integrators and PC original equipment manufacturers ("OEMs").

Despite the outbreak of SARS epidemic in the second quarter, the LCD monitor revenue was still growing rapidly in 2003, thanks to the replacement cycle of PCs, rising bundling rate and price cut of LCD monitors.



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PROSPECTS

Looking forward, distribution of Intel products will remain the major source of profit contribution for the Group, particularly Intel boxed central processing units ("CPUs"). Given the stable growth of PC demand in the Mainland and Intel's role as a major player in the CPU market, the Group continues to be optimistic about the demand for Intel CPU.

Sunrise Industry

The year of 2003 was a fruitful year for the LCD products market, driven by strong demand for LCD monitors. With robust PC-driven demand, the sales of LCD monitors are expected to surge continuously in 2004. Global sales of LCD monitors will rise 48% to 71 million units in 2004, surpassing cathode-ray tube ("CRT") monitors for the first time.

In China, the shipments of LCD monitors rose 99.3% to 2.2 million units last year. In the next 5 years, the compound annual growth rate is expected to record 41.5%.

The replacement of CRT monitors should continue to be the growth driver boosting the Group's revenue and profit in the next few years, given the low penetration rate in the Mainland and continue price cut on LCD monitors.

There is no doubt that LCD TV is the fastest growing segment of LCD products market and more LCD TVs will be produced at the new fifth-generation and next-generation lines. The penetration rate of LCD TV will be determined by the adoption speed of digital broadcasting, the availability of digital TV programmes and the affordability of consumers.

Mainland shipments of LCD TVs are expected to reach 752,000 units by 2007 from 87,000 in 2003, representing a 71% compound annual growth rate according to iSuppli/Standford Resources. Nevertheless, CRT TV would continue to dominate the price-sensitive Mainland market in the coming years. While the Mainland LCD TV market has not yet been kicked off, PC makers, TV makers and other consumer electronics makers are positioning themselves for the explosive growth of demand in the Chinese flat-panel market.

China, a global production base for TVs, is forecasted to manufacture a total of 58 million sets in 2004, up 7.4% from 2003. Traditional CRT TVs now account for nearly all of China's production, of which around 40% of total production is for export. In view of the enormous potential in LCD TV market, the large scale domestic makers are investing heavily in flat-panel technology, especially LCD, in order to capitalize on the projected growth in global demand. However, domestic companies still lack the technology know-how on LCD TV panel and rely



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on foreign makers to supply panels for assembling LCD TVs. Amongst panel suppliers, South Korea and Taiwanese makers supply most of the world's LCD panels. Chinese companies use the panels in making flat-panel televisions and computer monitors, taking advantage of low-labour costs in the Mainland.

Currently, China has more than 100 million cable TV subscribers and 300 million TV sets. The digital broadcasting of the 2008 Beijing Olympic TV programs will speed up the replacement of CRT TV with flat-panel TV. Besides, price is another determining factor. Meanwhile, the price of LCD TVs are expected to have negative compound annual growth rate of 15%-24% because of lowering LCD panel production costs and intensifying competition.

In view of the potential robust demand for LCD TV and LCD panel in China, the Group successfully obtained the distribution right of LCD TVs and LCD panels in the Mainland and Hong Kong from Chi Mei in the fourth quarter of 2003 and the first quarter of 2004, respectively. It brings synergies for future business development. The Group not only further expands LCD product distribution business in LCD TV products but also diversifies into another surging market – consumer electronics OEM channel.

As our vendor, Chi Mei is one of the major panel suppliers in the world and OEM for many famous LCD TV makers in Japan and South Korea. The limited suppliers in the LCD panel industry as well as our vendor's strength in leading edge technologies and highly vertical integrated production could lead the Group to leverage demand from Mainland LCD TV assemblers

Being the distributor of Intel CPUs and Chi Mei's LCD products, the Group would benefit from the new era of digitalization.

Dividend

The Board do not recommend the payment of a final dividend for the year ended 31 December 2003.

ACKNOWLEDGEMENT

On behalf of the Board, I would like to take this opportunity to extend my gratitude to all my fellow directors and staff for their valuable commitment and hard work. I would like also to express my sincere thanks to our business partners for their supports in the past years.

Yu Pen Hung
Chairman

Hong Kong, 26 April 2004