

MANAGEMENT DISCUSSION AND ANALYSIS

FINANCIAL RESULTS

The consolidated result of the Group for the financial year ended 31 December 2003, which amounted to a loss of HK\$89.2 million (2002: HK\$114.9 million). This represented an improvement of 22% as compared to the corresponding period for the previous financial year. The losses incurred for the year are mainly due to the following:

- (i) The loss on deemed disposal of Chinese 2000 upon the completion of the disposal and acquisition transaction in September 2003 which amounted to approximately HK\$5.3 million.
- (ii) The management's decision to provide for the quality deposits receivable from China Infohighway Communications Co., Ltd. ("IHW") of approximately HK\$44.9 million as a result of the current development with IHW on Beijing Infohighway Information and Technology Limited's ("BIHW") obligations set out under the cooperation agreement entered into by BIHW and IHW.
- (iii) The adjustment on the Group's fixed assets, in particular the manufacturing sector, amounted to approximately HK\$4.6 million as a result of a change in useful life from as long as 10 years to 5 years.
- (iv) Amortisation of goodwill arising from the acquisition of subsidiaries and associated company amounted to approximately HK\$3.7 million.
- (v) Share of losses attributable from an associated company which was acquired during the year amounted to approximately HK\$3.0 million.

The improvement noted mainly due to the decrease in operating losses of approximately HK\$11 million of the Information Technology business unit as a result of the scale down in business operation being effected in the beginning of the year 2003.

Turnover for the year ended 31 December 2003 amounted to HK\$96 million (2002: HK\$90 million), which represented an increased of 7% as compared to the same period last year. The increased was mainly due to an increased in sales from the manufacturing business unit noted as compared to the same period last year.

At the balance sheet date, the Group's net assets were HK\$16 million (2002: HK\$43 million). The dropped in net assets of approximately HK\$27 million as compared to last year is the net impact of the Group's capital raising exercise during the year which increase net asset by approximately HK\$63 million, set off against the Group's operating loss for the year amounted to approximately HK\$31.5 million, the loss on deemed disposal of Chinese 2000 Group amounted to approximately HK\$5.3 million and the impairment of the Group's assets, in particular the quality deposits receivables from IHW, in aggregate amounted to approximately HK\$53.2 million.

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FINAL DIVIDEND

The directors do not recommend the payment of a final dividend for the year ended 31 December 2003 (2002: HK\$ Nil).

THE GROUP'S LIQUIDITY AND FINANCIAL RESOURCES

Pursuant to the sale and purchase agreement on the acquisition of 51% interests in Chinese 2000 Holdings Limited entered on 18 November 2002 (the "Acquisition"), during the year under review, 170,000,000 shares of the Company was issued as consideration shares upon completion of the Acquisition on 17 January 2003.

On 8 December 2003, the Group completed the placing of warrants to subscribe for 370,000,000 (subject to adjustment) shares in the capital of the Company at a placing price of HK\$0.07 per warrant and at a subscription price of HK\$0.28 (subject to adjustment). The net proceeds received from the placing of warrants amounted to HK\$24.5 million and were used for general working capital of the Group.

At the balance sheet date, the Group had cash and bank deposits of HK\$0.4 million (2002: HK\$5.4 million) which includes foreign currency deposits of US\$nil million (2002: US\$0.4 million) and RMB0.1 million (2002: RMB0.5 million).

The Group's consolidated net borrowings dropped from last year's figure of HK\$25 million to HK\$19 million. Despite a dropped in the Group's net borrowings, the Group recorded an increased in its gearing ratio, which is expressed as a percentage of the Group's net borrowings over shareholders' equity of HK\$16 million as at 31 December 2003 (2002: HK\$43 million), from 58% to 119%. This increased in gearing ratio is attributable to the significant dropped in the Group's shareholders' equity as compared to last year.

The amount of debt due within one year at the balance sheet date amounted to HK\$18,931,000 (2002: HK\$30,035,000). The dropped in the Group's loan balance as compared to last year was due to the repayment of loans that expired during the year.

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The table below shows the type, maturity, currency and interest rate profiles of the Group's bank and other borrowings at the balance sheet date.

	2003 <i>HK\$'000</i>	2002 <i>HK\$'000</i>
DEBT MATURITY PROFILE		
Within one year	18,931	30,035
Within two to five years	–	–
Total	18,931	30,035
INTEREST RATE PROFILE		
Unhedged floating	3,375	13,550
Fixed	15,556	16,485
Total	18,931	30,035
NATURE OF DEBT		
Secured other loans	9,056	9,056
Unsecured other loans	9,875	20,979
Total	18,931	30,035
CURRENCY PROFILE		
Hong Kong Dollars	9,875	20,050
Renminbi	9,056	9,056
US Dollars	–	929
Total	18,931	30,035

At the balance sheet date, the Group's secured borrowings amounted to HK\$9 million (2002: HK\$9 million) which were secured by a legal charge on certain leasehold land and buildings of the Group situated in the PRC with carrying value of approximately HK\$18 million at the balance sheet date.

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Despite that the Group sustained recurrent losses and had net current liabilities of approximately HK\$45 million at 31 December 2003, the directors of the Company are of the opinion that the Company and the Group will be able to meet their obligations as and when fall due after taking into account the following:

- (i) loan facilities totaling HK\$70 million made available to the Company from financial institutions; and
- (ii) continual financial support received from the ultimate holding company.

The directors believe that the Group will have sufficient cash resources to satisfy its future working capital and other financing requirements.

EXPOSURE TO FLUCTUATION IN EXCHANGE RATES, INTEREST RATES AND RELATED HEDGES

To manage the risk associated with an uncertain market environment, the Group pursues a funding strategy, using equity as far as possible to finance long-term investments.

The Group's borrowings and cash and cash equivalents are primarily denominated in Hong Kong dollars, Renminbi and US dollars. The Group does not hedge against foreign exchange risk, as the managements believe the Hong Kong dollar will remain pegged to the US dollar in the foreseeable future and the exchange risk associated with the Renminbi is expected to be minimal.

The interest rates profile of the Group's borrowings comprise a mixture of fixed and floating rates. The Group does not hedge against interest rates risks as the management does not expect the impact of any fluctuation in interest rates to be material to the Group.

MATERIAL ACQUISITIONS AND DISPOSAL OF SUBSIDIARIES

During the year under review, the Group completed its acquisition for an equity interests of 51% in Chinese 2000 Holdings Limited ("Chinese 2000") for a total consideration of HK\$38,250,000 which was satisfied by the issue and allotment of 170 million ordinary shares of HK\$0.05 each of the Company.

Subsequently in July 2003, the Group entered into agreements for the disposal of its entire interests in Chinese 2000 for a total consideration of HK\$91.8 million which was satisfied by the allotment and issue of 3,825 shares of US\$1.00 each in the capital of Chinese 2 Linux (Holdings) Limited ("C2L"), representing 42.5 percent interests in C2L. This transaction was then completed in September 2003.

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BUSINESS REVIEW

The Group's significant investments are investments in subsidiaries of which their performance during the year under review and their future prospects have been grouped according to their respective segments.

During the year under review, there are no significant changes in the Group's investments.

Manufacturing Business

For the year ended 31 December 2003, the manufacturing business unit continued to engaged in the manufacture of personal healthcare products which included hair clippers, shower related products and electronic toothbrushes, amongst others. Turnover of this business unit rose by 19%, to HK\$94 million (2002: HK\$79 million) as compared to the same period last year. This increased noted to be due mainly to the increased in sales order for electronic toothbrush during the year ended 31 December 2003 and the management's efforts in providing value added services to the customers.

Despite an increase in turnover for the manufacturing business unit, a loss of HK\$0.5 million (2002: HK\$2.0 million) was recorded for the year ended 31 December 2003. An operating loss was recorded mainly due to the adjustment made during the year to account for the change in useful life of the fixed assets from 10 years to 5 years which amounted to approximately HK\$4.6 million.

The Information Technology Business

During the year under review, the Group acquired 51% interests in Chinese 2000 Holdings Limited ("Chinese 2000") for a consideration of HK\$38,250,000. The transaction was completed on 17 January 2003 by securing the Company to issue 170,000,000 shares of the Company as consideration shares. Subsequent to the acquisition, the business unit went further to collaborate with Culturecom Technology Limited and Transmeta Corporation for the development of existing software application business through exploitation of Linux-based operating system. In order to facilitate the collaboration between the parties, a new company, Chinese 2 Linux (Holdings) Limited ("C2L"), was set up whereby the Group swaps its 51% interests in Chinese 2000 for a 42.5% interests in C2L of which this transaction was completed in September 2003.

The Information Technology business unit recorded a turnover of HK\$2.4 million as compared to HK\$11.3 million recorded in the previous corresponding year. The dropped in sales was due to a change in business strategy whereby the Group scale down all direct operating units and embarked on a collaboration and joint effort strategy to license, develop and promote new mobile and embedded computing products which is still at its development stage.

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Results from operation attributed by the Information Technology business unit recorded a loss of HK\$66 million as compared to a loss of HK\$81 million in the previous corresponding year. The significant loss recorded this year mainly due to the provision made on the quality deposits receivable from IHW amounted to HK\$44.9 million and the amortization of goodwill amounted to HK\$3.7 million.

Outlook

With the overall economic outlook beginning to improve towards the end of 2003, the Group looks forward to a more prosperous year ahead. In the coming year, the Group will focus on business consolidation targeting at further improving the overall efficiency and operations management to enhance profitability.

MATERIAL CONTINGENT LIABILITIES

At 31 December 2003, the Group had provided a guarantee on a joint and several basis with a third party in respect of payment obligations of service fees payable by an associated company of approximately HK\$11.8 million.

EMPLOYEES AND REMUNERATION POLICY

At the balance sheet date, the Group employed approximately 45 (2002: 45) staff in Hong Kong and approximately 760 employees (2002: 654) in Mainland China. Employee remuneration are given and reviewed based on market norms, individual performance and experience. Awards and bonuses are considered based on the Group's business results and employees' individual merit.

The Group also granted share options to certain employees of the Group on 10 July 2000, entitling them to subscribe for shares of the Company. These options are exercisable in stages commencing twelve months from the date of grant. The expiry date of the options is ten years from the date of grant. During the year under review, no option was exercised.