

(2) **Summary of analysis of operational performance and financial position**

1. **Analysis of reasons for movements of principal financial indicators (Prepared under the PRC accounting system, unaudited)**

Items	January to	January to	Unit: RMB Change %
	June 2004	June 2003	
Revenue from principal operations	1,230,728,722.68	1,523,034,474.64	(19.19)
Profits from principal operations	135,375,818.67	148,974,057.61	(9.13)
Net profit	58,001,551.57	32,853,390.62	76.55
Increase in cash and cash equivalents	(423,936,023.13)	(415,524,486.77)	(2.02)
Items	30 June 2004	31 December 2003	Change %
Total assets	4,659,023,852.69	3,592,429,930.02	29.69
Shareholders' funds	1,186,975,535.86	1,128,973,984.29	5.14

Note: Increase of 76.55% in net profit was mainly due to the significant increase in investment income.

2. **Liquidity of capital**

In accordance with the accounting principles generally accepted in Hong Kong, as of 30 June 2004, the Company's consolidated gearing ratio was 71.04%, current net asset value was RMB333,385,000, liquidity ratio was 1.10, quick ratio was 0.86, bank deposits and cash were approximately RMB365,000,000 and total loan amount was approximately RMB1,346,000,000 with an annual interest rate of 5.04%.

(3) **Investments in the Reporting Period**

1. **The Company did not utilise any proceeds raised in the Reporting Period or continue any use thereof commencing from the previous periods.**
2. **The Company did not have any principal investment financed by non-raised funds.**

(4) **Business plans for the second half of the year**

The Company will continue to dedicate its effort in the work of new product development, market exploration, Sino-foreign joint venture and internal reform management in the second half of the year in order to further accelerate the pace of development. Joint ventures such as ENC and BMC will further expand their productions in order to materialise the pre-set target in the year as a way to maintain a relatively larger growth. Panda mobile phones will proactively respond to the changes in the market in the second half of the year by quickening the speed of the introduction of new products into the market and improving internal management and after-sales services in order to strive for a relatively greater growth as compared with the first half of the year. Satellite communications, electromechanical and information products also aspire for speedy growth to ensure that the annual operational results of the Company will step further ahead.

(5) **Employees of the Company**

As at 30 June 2004, there were 1,977 employees in the Company, 1,055 of which were engaged in production, 505 of which were engaged in technology, 118 of which were engaged in sales, 68 of which were engaged in finance, 231 of which were engaged in administration. There were 438 retirees, for whom the Company undertook to pay retirement pension.

(6) **Purchase, sale and redemption of shares of the Company**

During the Reporting Period, the Company and its subsidiaries did not purchase, sell or redeem any listed shares of the Company.

(7) **Pre-emptive right**

In accordance with the relevant laws of the People's Republic of China and the Articles of Association of the Company, there was no provision for pre-emptive right.

VI. SIGNIFICANT EVENTS

(1) **General Corporate Governance**

The Company continues to improve its corporate governance and to regulate its operation in accordance with the spirit of the relevant documents issued by China Securities Regulatory Commission ("CSRC") and requirements under the Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong Limited. In compliance with the requirements of the reform report reviewed during the official inspection at the end of last year, the Company amended part of its Articles of Association. Resolutions in relation to the amendment were passed at the annual general meeting held on 12 May 2004. At the meeting, the Fifth Board of Directors of the Company was also formed by means of poll. One-third of the members of the newly formed Board of Directors are independent directors, among which one is a certified accountant, as required by the relevant rules of CSRC.

Issue in relation to the General Manager of the Company acting concurrently as General Manager of controlling shareholder, the Company has been proactively discussing the matter with Party Committee of Jiangsu Province. The relevant matter will soon be resolved properly.

- (2) During the Reporting Period, the Company did not make any profit appropriation which was recommended previously for distribution in the Reporting Period. No reserves were transferred to increase the share capital and no new shares were issued. The Company will not distribute interim profits, nor will it increase its share capital by converting from surplus reserve in the half year of 2004.
- (3) There was no litigation and arbitration which was material to the Company that occurred during the Reporting Period or occurred in the previous period and subsisting during the Reporting Period.

- (4) On 12 May 2004, the Company entered into agreements with Nanjing Jiangning Economic and Technological Development Corporation and Nanjing Xincheng Company Limited respectively on transfers of a total of 35% equity interests held by the Company in Jiangsu Provincial Software Industry Company Limited at an aggregate consideration of RMB80,339,490. The resolution concerning the matter was passed at the 1st meeting of the Fifth Board of Directors of the Company (Relevant announcement was published in Shanghai Securities News and China Securities Journal on 13 May 2004, and Takung Pao (Hong Kong) and The Standard on 14 May 2004).

Following the issue of the announcement in relation to the disposal of assets, the Company received the transfer consideration in full from the two parties before 11 June 2004 as stipulated by the terms of the abovementioned agreements. As a result of the transfer of 35% equity interests in Jiangsu Software Park, the Company recovered investments of RMB80,339,490 and recorded a total gain of RMB13,351,960. The proceeds will be used for the development of the Company's principal operations.

Besides, the Company had no acquisition or disposal of assets nor any corporate merger during the Reporting Period or occurred in the previous period and subsisting during the Reporting Period.

(5) Material connected transactions

1. During the Reporting Period, there were no material connected transactions conducted by the Company. Connected transactions were entered into in the ordinary and usual course of business and had been conducted on normal commercial terms. (For details, please refer to financial statements).
2. Loans and current accounts with connected parties

During the Reporting Period, the Company provided capital funds of RMB259,347,058.04 to the controlling shareholder Panda Electronic Group Limited. At the end of the period, the balance amounted to RMB267,388,540.46. The Company also provided capital funds of RMB1,169,246,697.00 to Jiangsu Tianchuang Communication Industrial Co., Ltd., which is the related party of a subsidiary of the Company. At the end of the period, the balance amounted to RMB688,247,697.00.

(6) Material contracts

1. During the Reporting Period, the Company did not hold any trust, contract and lease of assets of other companies or other companies hold any first, contract and lease of assets of the Company in the previous period and subsisting during the Reporting Period.

2. Significant guarantees:

As of 30 June 2004, the Company provided guarantees in respect of the following facilities: the bank loan amounted to RMB50,000,000 for Nanjing Zhongda Mode (Group) Co., Ltd., an independent third party of the Company; the acceptance bill for bills of RMB1,615,500 for Nanjing Panda Ju Neng Small Home Electronic Appliance Co., Ltd.; the bank loans and acceptance bill for bills totalled RMB 31,666,200 for Nanjing Panda Information Industry Co., Ltd.; the bank loans of RMB18,100,000 for Nanjing Huage Dian Qi Plastic Industrial Co. Ltd.; the bank loans and acceptance bill for bills totalled RMB165,000,000 for Nanjing Panda Mobile Communication Equipment Co. Ltd.; the bank loans and banking facilities for bills totalled RMB109,440,000 for Nanjing Panda Communications Development Co., Ltd. Besides, Nanjing Panda Mobile Communication Equipment Co. Ltd., the controlling subsidiary of the Company, provided a guarantee for bank loans and acceptance bill for bills totalled RMB425,300,000 for Jiangsu Tianchuang Communication Industrial Co., Ltd. The obligations of the above guarantees totalled RMB592,724,700, representing 49.94% of the net asset of the Company, of which the guarantee amount for controlling subsidiaries amounted to RMB325,821,700 in total.

3. There was no material entrustment of another party for the management of cash assets by the Company during the Reporting Period or in the previous period and subsisting during the Reporting Period.

(7) Special statement and independent opinion of Independent Directors on the Company's accumulative and current guarantees provided to external parties, guarantees in violation of regulations and fulfillment of requirements set out in document No. 56 (2003) issued by CSRC

Being the Independent Directors of Nanjing Panda Electronics Co., Ltd., we would like to give the following special statement and independent opinions on the Company's accumulative and current guarantees provided to external parties, guarantees in violation of regulations and fulfillment of requirements set out in document No. 56 (2003) issued by CSRC after performing a prudent inspection on the captioned matters in a practicable manner, in accordance with the spirit of document No. 56 (2003) "Notice to Certain Issues for Standardization of Capital Transactions and Guarantees Provided by Listed Companies to Related Parties" issued by CSRC:

1. Details of guarantees

- (1) As at 30 June 2004, the Company provided guarantees to external parties accounting for 53% of the Company's net assets recorded in the consolidated financial statements of 2003. The gearing ratio of one of the guarantees, Nanjing Zhongda Mode (Group) Co., Ltd., was less than 70%, whereas other guaranteed subsidiaries of the Company were all more than 70%.
- (2) Nanjing Panda Mobile Communication Equipment Co., Ltd., a subsidiary of the Company, provided a guarantee to Jiangsu Tianchuang Communication Industrial Co. Ltd. in 2003 without obtaining prior approval of the Company. This was only brought to the attention of the Company recently, which indicates that there are deficiencies in the Company's internal control system. As such, the Company has made efforts to strengthen its internal control and has reorganized the Board of Directors and senior management of Nanjing Panda Mobile Communication Equipment Co. Ltd. in a bid to improve corporate governance and to minimize exposure to guarantee risks as well as to prevent repeated happenings of similar circumstances.
- (3) We request the Company to strictly control guarantee risks and to beef up management of subsidiaries' guarantee granting policies by setting up a monitoring mechanism for the utilization of capital guaranteed by its controlling subsidiaries and other related parties, apart from taking effective measures to deal with guarantees given in violation of regulations.

2. Capital transactions between the Company and related parties

- (1) As at 30 June 2004, the outstanding balance of capital transactions receivable by the Company from its controlling shareholder, Panda Electronics Group Limited, was RMB267,390,000. The Group has been offering strong support to its invested companies for their guarantees and reorganization. In the first half of the year, the Group encountered difficulties in cash flow and normal operation because of the macro economic control policies adopted by the State. It therefore had to borrow capital from such companies by paying interest according to the prevailing interest rates of bank loans. The Group also worked out a loan repayment scheme and promised to settle all its borrowings by the end of the year. We are of the view that the Group violated the relevant requirements of document No. 56 (2003) issued by CSRC, although it was in a tough situation. To protect the overall interests of the listed company, the Group must repay its loans as soon as possible and prevent repeated happenings of similar circumstances.
- (2) We consider that although Jiangsu Tianchuang Communication industrial Co. Ltd. is a key distributor of Panda portable phones, the closing balance of capital transactions receivable by the Company from Jiangsu Tianchuang Communication industrial Co. Ltd. is excessive. Accordingly, we request the Company to implement effective measures to reduce the amount.

We request the Company to follow the spirit of the "Notice to Certain Issues for Standardization of Capital Transactions and Guarantees Provided by Listed Companies to Related Parties" issued by CSRC with due care, so as to solve all the existing problems and optimize its operation through the perfection of internal control, with particular emphasis on the utilization of capital and provision of guarantees to external parties.

- (8) During the Reporting Period or in the previous period, and subsisting in the Reporting Period, the Company and its shareholders holding 5% or more of the issued share capital of the Company had no matters of undertaking that might affect the Company's operating results and financial position.
- (9) It was resolved at the Annual General Meeting held on 12 May 2004 that Shine Wing Certified Public Accountants and Horwath Hong Kong CPA Limited were reappointed as domestic and international auditors of the Company for 2004 respectively.
- (10) During the Reporting Period, the Company, the Board of Directors and the Directors were not subject to any inspection, penalty or criticism of CSRC and other administrative departments, and open condemnation by stock exchanges. No party related to the Company's Directors or senior management was subject to mandatory legal actions.
- (11) The Auditor Committee has reviewed together with senior management the accounting principles and accounting standards adopted by the Company, evaluated the matters relating to internal controls and reviewed the unaudited financial statements for the six months ended 30 June 2004.
- (12) **Other matters:**

1. Income tax

The Company is registered in High and New Technology Development Zone in Nanjing which is approved by the State Council as a national high and new technology development zone. The Company has been approved by the Jiangsu Provincial Technological Commission as a high and new technological enterprise, which is entitled to a preferential income tax rate of 15% as per existing policy. The Company is still entitled to the preferential treatment at present.

2. Staff quarters

In respect of purchase of staff quarters by employees of the Company, such staff quarters are owned by Panda Electronic Group Limited and are provided to certain employees of the Company in accordance with the relevant policies issued by the State and Nanjing Municipal Government respectively. The Company was not involved in the selling of staff quarters to its employees during the year ended 30 June 2004, nor rented any staff granter to parent company for employees of the Company

3. The Code of Best Practice and Model Code

During the Reporting Period, the Company has been in compliance with the Code of Best Practice as set out in Appendix 14 of the Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong Limited.

The Company has adopted the Model Code for Securities Transactions by Directors of Listed Issuers set out in Appendix 10 of the Listing Rules as the code of conduct regarding Directors' securities transactions. During the Reporting Period, all Directors and Supervisors of the Company have complied with the said Model Code and the required standard regarding directors' securities transactions set out in the Model Code.

3. **The Company has appointed sufficient Independent Non-executive Directors. Three Independent Non-executive Directors were appointed with effect from 12 May 2004, representing one-third of the members of the Board of Directors.**