MANAGEMENT DISCUSSION AND ANALYSIS

Business Review

During the first half of this year, the global economic climate varied as geopolitical events continued to distract attention in major markets. The US and European economies did not exhibit consistent signs of full recovery or growth. Sectors that benefited from low interest rates performed well. However, growing consumer debts remained a concern.

In the consumer electronics arena, suppliers faced extreme competition in mainstream audio-video (AV) products as new products and new applications came to the market at a quick tempo while conventional products were phasing out rapidly. As a result, retailers used cut-throat price points to move their goods in short cycles.

The most important issue that had been troubling the electronics industry as a whole was the high oil price that, for the past year, had been driving up the costs of raw materials vital for electronics goods. The PRC also became a major user of the commodity raw materials from plastics to metals and paper.

Business at the In-Car division was solid. Consumers were particularly attracted by the option of video entertainment they could add to their vehicles. The revenue increased due to volume increase while the unit price dropped as expected.

The Home Division experienced some setbacks during the first six months as reflected by their drop in revenues when compared to the same period of the previous year. The higher materials costs and delays in certain new products coming to the market were the primary reasons.

For the PRC market, our goal this year is to build up a network of 400 POS (points of sales) in target cities as retails channels for our home AV products. As of end of June this year, over 400 POS were in place. The central government's endorsement in digital cable TV began to take shape that had led to our supplying small orders of these digital boxes for operators at the provincial and city level for field trials.

Prospects

We expect the global economy will remain soft as the geopolitical situation remains uncertain and no sign of the high oil price to ease. The presidential election in the US will hopefully set a direction for the US economy and therefore the world's as well. Europe's economy is greatly influenced by its dependence on foreign oil supply. The PRC has reached a point that internal demands can drive growth.

For the consumer electronics industry, traditional products are now replaced by new concepts of portability, delivery and storage, all of which are made possible by technologies that have recently become affordable for mass-market products. High definition television sets (HDTV) and digital still cameras are at or near mass market price points; the overall atmosphere for both digital hardware and software is good for consumers.

The super-competitive landscape has also seen certain export-oriented manufacturers taking exit due to losses incurred from failure in materials cost management.

Broadcasting of digital entertainments by service providers to consumers is also taking place. Countries across Europe, for example, have switched on their digital terrestrial transmissions in co-existence with the present analog formats. Retailers have begun carrying digital set-top-boxes as households recognize new programs are available from the air. Similarly, the digital cable box market in the PRC is poised to grow as the central government's commitment to switch from analog to digital appears solid.

We hold guarded optimism that our overall results will improve by end of 2004 through accelerated efforts to regain lost grounds in the early part of the year. We have a strong outlook for growth in 2005 with new products.

We expect the In-Car Division to hold its course with healthy growth in the video sector. As we establish regular relationships with the car manufacturers in the primary market, we expect both the volume and product assortment will increase. We are optimistic that the Home Division will recover from the product delays and produce positive results during the second half of the year. Various new products are coming to the market in fourth quarter this year.

Liquidity and Financial Resources

The Group's objective is to maintain a healthy and liquid financial position. Liquidity, assets and capital structure were all enhanced comparing to the same period in the previous year. As is usual in the consumer electronics industry, the Group experiences a low season during the first half of the year and normally a high season in the second half. The result is a higher use of financial resources at the interim balance sheet date vis-a-vis that at the end of the financial year. Total borrowing rose 21.6% compared to the last year end. Subsequent to the balance sheet date, the Group arranged another HK$300 million syndication loan to refinance the existing loans at a lower interest rate. The Group views its financial resources adequate for its ongoing business activities.

The Group's order book shows continuous shortening of order cycle from customers. The Group remains conservative and expects no substantial amount of investment in capital expenditure in the coming months. The Group had no assets pledged at the balance sheet date.

The gearing ratio, calculated by total borrowings from banks and financial institutions net of cash divided by tangible net worth, was 53.2%. The Group mainly borrows in US Dollars and HK Dollars on floating interest rates. Details on maturity profile of these borrowings and contingent liabilities are set out in note 11, 12 and 13 to the financial statements. At the balance sheet date, the Group mainly held cash and bank deposits in US Dollars, HK Dollars, Renminbi and Australian Dollars. The Group considered its foreign exchange exposure well balanced with some exposure in non-US dollar base currencies.

All other information pertaining to those matters set out in paragraph 32 of Appendix 16 of the Listing Rules has not changed materially from the information disclosed in the most recent published annual report.