

STRENGTHENING CORE ADVANTAGES



BYD continued to be the world's largest manufacturer of nickel-based batteries, and second-largest manufacturer of Lithium-ion batteries for mobile phone handsets in 2004. With the same customer base as its battery business, the Group further extended its product range to include handset components and achieved satisfactory results during the Year.

Industry Overview

Rechargeable Battery Industry

There was continuous growth in demand for rechargeable batteries within the global market, attributable mainly to their wide use in portable devices, such as mobile handsets, notebook PCs, digital cameras, MP3 players, etc. Among all these devices, mobile handsets accounted for over half of the demand for rechargeable batteries. New emerging markets also propelled demand for handsets, especially more affordable handsets, which led to increased pricing pressure on the global handset industry.

In the People's Republic of China (the "PRC"), the improved living standards have created strong purchasing power for advanced portable/digital devices like mobile handsets, handheld devices, etc. The growth in the demand for handsets, in particular global mobile handset brands, has remained strong in the PRC. On the other hand, due to the loss of market share to global handset manufacturers and change in sales strategy, the demand for domestic handsets was lower than expected. It also affected the demand for battery products from domestic handset manufacturers in 2004. Together with the fluctuations in raw material prices and fierce competition within the battery industry during 2004, some industry players were affected by higher production costs during the Year.

Handset Component Industry

The global handset component industry has expanded rapidly in the past few years due to advances in technology. New applications of mobile handset, such as multimedia messaging services, cameras, colour screens and intelligent functions, have resulted in rapidly changing consumer preferences and shorter product life cycles, which have also contributed to increased demand for handsets with precise plastic parts. With the emergence of 2.5G and 3G mobile phones, it is expected that there will be a new wave of handset upgrades by consumers.

The increasingly fierce competition within the handset industry has resulted in price wars and demanded quick responses to market needs. Outsourced manufacturing, flexible pricing strategies, quality/cost controls and quick lead times, have all become crucial criteria for handset manufacturers in selecting contractors and maintaining market share. In addition, handset

manufacturers now prefer comprehensive handset component providers to provide services to them.

Automobile Industry in the PRC

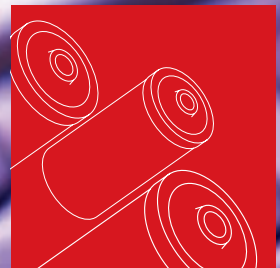
Due to weak consumer sentiment brought forth by the PRC government's credit-tightening measures, contraction in auto financing services and numerous price cuts by industry players, growth in the PRC's automobile sales decreased from 35.0% in 2003 to 23.4% in 2004. However, automobile penetration in the PRC remains low, at around only 2%, as compared to 50%-60% in developed countries, such as the US, Japan and certain European countries. In view of the existing low automobile penetration, there is market potential for PRC's automobile industry, especially with the expected growing affluence and consumption power of Chinese people in the long run.

Business Overview

Rechargeable Battery Business

BYD achieved significant growth in its rechargeable battery business and sustained its leading market position within the rechargeable battery sector for all three of its core products, namely NiCd, NiMH and Lithium-ion batteries. It continued to be the world's largest manufacturer of nickel-based batteries, and second-largest manufacturer of Lithium-ion batteries for mobile phone handsets in 2004. With the accelerating demand for mobile handsets in 2004, the Group recorded historical high sales for Lithium-ion battery products of over RMB3,501 million in 2004 as compared with RMB2,113 million in 2003, an increase in sales of 65.7%. The Group's nickel battery products achieved stable growth in demand in 2004 with sales of over RMB1,547 million, representing a year-on-year increase in sales of 23.8%.

During the Year, orders from domestic handset manufacturers decreased due to loss of market share to global handset manufacturers and change in sales strategy by domestic customers, especially in the second half of 2004. However, the Group received substantial increase in the number of orders from existing global handset manufacturers, which have increased their respective market shares in the PRC. To meet the growing demand from its customers, BYD enhanced its production capacity of rechargeable battery products during the Year.



WIDENING PRODUCT AND SERVICE RANGE

Handset Component Business

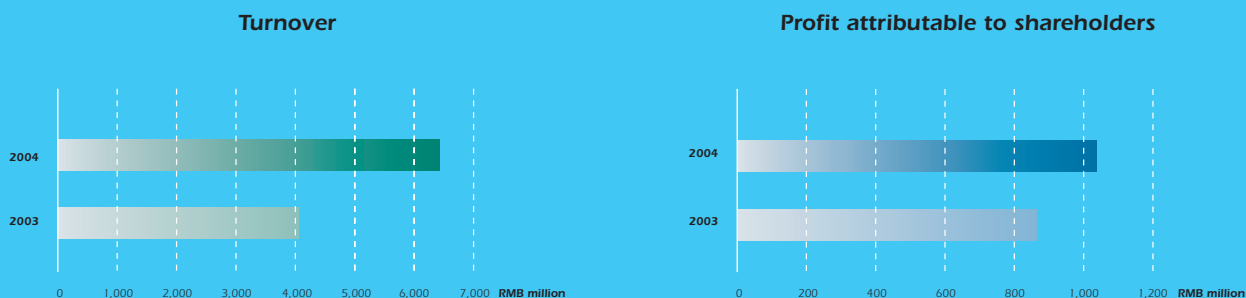
With the same customer base as its battery business, the Group further extended its product range to handset components and achieved satisfactory results during the Year, becoming a fully comprehensive handset component provider. The move was seen as positive and was well received by existing customers. By leveraging on its plastic and mould making capabilities, BYD can provide customers with a total solution from design engineering, moulding, injection moulding and spray painting to final assembly. During the Year, the Group developed several handset components, including plastic housings, key pads, camera lenses, vibration motors and FPCs (flexible printed circuits). BYD also started producing LCDs for handsets and developed monochrome and colour STN-LCDs during the Year for various handset models. The aggregate turnover of handset components was over RMB939 million, in which the turnover of LCD and precise plastic parts for mobile phones were RMB666 million and RMB273 million respectively.

Automobile Business

The Group's automobile sales were affected by the unfavourable operating environment and recorded RMB389 million in turnover, representing a 23.6% decrease when compared with 2003. Turnover and gross profit reached RMB389 million and RMB38 million respectively, representing 6% and 2% of the Group's total contribution. Total sales volume reached 14,818 units. The Group established and launched the first private vehicle inspection centre in Shanghai during the Year with a site area of 3,100 sq. m.. BYD also acquired an additional 15% equity interest in BYD Automobile Company Limited in early 2004, which increased its equity interest in BYD Automobile Company Limited to 92%. In view of the unfavorable operating environment, BYD has already adjusted its development strategy and applied stringent cost control measures.

Financial Review

Turnover and Profit Attributable to Shareholders

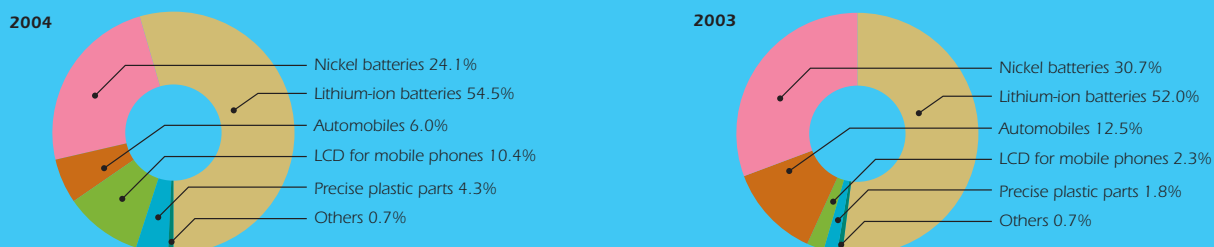


The increase in turnover and profit attributable to shareholders was mainly resulted from the tremendous increase in sales of lithium-ion battery products by 65.7% during the year. Sales of handset components surged significantly due to increase in sales of LCDs for handsets by 6.2 times and significant increase in sales of precise plastic parts for mobile phones.

Segmental Information

Set out below is a comparison of the Group's turnover in terms of product categories and their proportion in 2004 and 2003:

A breakdown of turnover in terms of product categories and their proportion



During 2004, lithium-ion battery products proved to be the largest income source for the Group, recording increase in sales of 65.7% as compared with 2003. This in turn led to a decrease in total contribution to turnover from the automobile business. During the Year, sales of handset components, including LCDs and precise plastic parts for mobile handsets surged significantly and contributed to 14.7% of the Group's total turnover.

Management Discussion and Analysis

Set out below is a comparison of the Group's turnover in terms of geographical segment, as determined by location of its operations in 2004 and 2003:

A breakdown of turnover in terms of the geographical location and their proportion



Gross Profit and Margin

The Group's gross profit increased by approximately 26.4% from RMB1,348 million for the year ended 31st December, 2003 to approximately RMB1,705 million for the year ended 31st December, 2004. Whereas, gross profit margin decreased due to price increase in chemical materials for battery products, growth in sales of packed battery products with lower margin and the tightening of export tax refund policy for battery products in 2004 in the PRC.

Liquidity and Financial Resources

BYD generated net operating cash inflow of approximately RMB652 million for the year ended 31st December, 2004, compared with RMB441 million in 2003. Total borrowings as at 31st December, 2004, including all bank loans were approximately RMB2,697 million, compared with approximately RMB724 million as at 31st December, 2003. The maturity profile spreaded over a period of eight years, with RMB2,460 million repayable within one year, RMB166 million in the second year, RMB39 million within three to five years and RMB32 million after five years. The increase in total borrowings was to fund numerous new battery related projects, R&D investment volume and enhance production capacity. The Group maintains adequate daily liquidity management and capital funding expenditure requirements to regulate internal operating cashflow. In addition, BYD has access to significant short-term borrowing facilities from its principal banks. As at 31st December, 2004, the Group's

gearing ratio, calculated on the basis of total borrowing net of cash and cash equivalents over net assets, was at 49.8%.

Accounts receivable turnover days were maintained at about 97 days for the year ended 31st December, 2004 as compared to 94 days for the year ended 31st December, 2003. Inventory turnover days increased from 87 days for the year ended 31st December, 2003 to 91 days for the year ended 31st December, 2004. The surge in raw material prices and allowance for bulk orders during the Year, resulted in increase in total inventories. Additional new projects, together with enhancement in production capabilities of the Shanghai plant, resulted in the increase in inventory turnover days.

Capital Structure

The Group's treasury function is responsible for the Group's financial risk management which operates according to policies implemented and approved by top management. As at 31st December, 2004, borrowings were primarily denominated in RMB and USD, while cash and cash equivalents were mainly denominated in RMB and USD. The Group's intentions to maintain an appropriate mix of financial equity and debt are to ensure an efficient capital structure during the Year. The loans outstanding as at 31st December, 2004 are set out in Note 22 to the accompanying accounts. The loans remaining outstanding as at 31st December, 2004 were at fixed interest rates for RMB loans and floating interest rates for foreign currency loans.

Details of Assets Pledged

As at 31st December, 2004, the Group's trade receivables of approximately RMB333 million (2003: Nil) were pledged for certain of the Group's short-term loans.

Use of IPO Proceeds

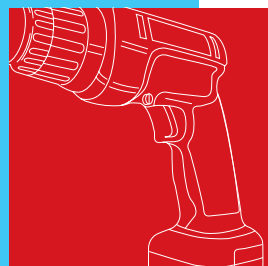
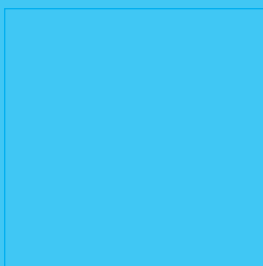
	HK\$ million	
	Planned	Latest allocation
▪ Expansion in production capacity, R&D and manufacturing of Lithium-ion batteries and related new products	189	Fully utilized
▪ Development and manufacture of raw materials for Lithium-ion batteries	94	Fully utilized
▪ Product R&D and manufacture of rechargeable batteries for electric vehicles	85	Fully utilized
▪ Product R&D and manufacture of fuel cells and solar cells	85	0.7
▪ Product R&D and manufacture of monochrome and colour STN-LCDs	142	Fully utilized
▪ Repayment of bank loans	377	Fully utilized
▪ Potential acquisition(s)	189	—
▪ General operating capital	188	Fully utilized

Exposure to Foreign Exchange Risk

Most of the Group's income and expenditure are denominated in RMB and USD. During the Year, the Group did not experience any significant difficulties in its operations or liquidity, due to fluctuations in currency exchange rates. The Directors believe that the Group has sufficient foreign exchange to meet its own foreign exchange requirements.

Employment, Training and Development

As at 31st December, 2004, the Group had over 40,000 employees, representing an increase of 12,000 employees as compared with 31st December, 2003. During the Year, total staff cost accounted for approximately 9.5% of the Group's turnover. Employee remuneration was determined based on performance, experience and prevailing industry practices, with compensation policies being reviewed on a regular basis. Bonuses and commission were also awarded to employees, based on their annual performance evaluation. In addition, incentives and encouragement were offered for personal and career development.



Management Discussion and Analysis

Share Capital

As at 31st December, 2004, share capital of the Company is as follows:

	Number of shares issued	Percentage (%)
Domestic shares	390,000,000	72.29
H shares	149,500,000	27.71
	539,500,000	100.00

Capital Commitment

As at 31st December, 2004, the Group's contracted capital commitments for the acquisition of plants and machinery amounted to approximately RMB697 million.

Contingent Liabilities

As at 31st December, 2004, the Group had contingent liabilities of approximately RMB3,531,000 as bank loan guarantees for other companies.

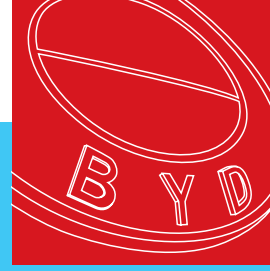
The Group is currently involved in one litigation proceeding in Japan in relation to alleged patent infringements. Due to the fact that there has not been any material development in respect of the proceeding in Japan since commencement of such proceeding, the directors consider that it is impracticable and premature to assess the impact of such proceedings on the Group and its operation. The Directors of the Company believe that the Group has not committed the alleged infringements. The Group would vigorously defend against all claims under the proceeding.

SUBSEQUENT EVENTS

The Group entered into an agreement with Sanyo Energy (USA) Corporation, a Delaware corporation, and Sanyo Electric Co., Ltd. a Japanese company, (collectively referred to as "Sanyo") effective on 24 January, 2005 for settlement of the legal proceeding brought by Sanyo against the Group in 2002 for alleged patent infringements. Pursuant to the settlement agreement, among other things, both the Group and Sanyo have dismissed their respective claims or counter-claims against the other and the parties have agreed not to sue each other for an agreed period regarding patent infringement of lithium-ion batteries. In addition, the Group has paid to Sanyo US\$2,400,000 as part of the terms of the settlement.

Future Prospects and Strategies

With the expected trend of shorter product life-cycles for handsets due to an increase in the frequency of product upgrades by consumers, the Group aims to fully capture the opportunities that will emerge for its handset component business to become one of the world's leading handset-component providers in the coming years, which will balance well with the Group's leading position in its core business, the rechargeable battery business, which it expects to maintain stable growth in the coming years. Regarding the automobile business, the Group will adopt prudent development strategies in its attempt to increase market share.



Rechargeable Battery Business

The rechargeable battery business is the Group's core business and is expected to maintain a stable growth in the future. BYD will further enhance its R&D capabilities, which is in line with the development trend of rechargeable batteries within the global market. To meet the ever-changing market demand, BYD will work closely with existing customers to promptly and efficiently develop new battery models for their products. Other than rechargeable batteries for handsets and notebook PCs, BYD also aims to develop new types of Lithium-ion batteries for other portable devices.

The Group will further enhance its market share and target to become the No. 1 rechargeable battery manufacturer for handset components in 2005 and the No.1 rechargeable battery manufacturer in the world in the near future.

Handset Component Business

The handset component business of BYD is expected to grow tremendously and become another major revenue driver in the future. BYD is optimistic of capturing a greater market share in the handset-component market in the future due to increased sourcing from global handset manufacturers in the PRC and an increasing demand from domestic manufacturers.

The Group will leverage on its plastic and tooling capabilities to further expand its product range for handset components for providing a more comprehensive product range to its customers, including key pads, camera lenses, and Light Emitting Diode ("LED") displays. BYD has successfully supplied handset components to domestic customers. Capitalising on the existing customer base with its rechargeable battery business, BYD will strive to secure orders from global handset manufacturers. The Group expects to receive orders from major global handset manufacturers in 2005. BYD aims to become a comprehensive handset-component provider in the world.

Automobile Business

Amidst the highly competitive automobile market and the government's credit-tightening measures in the PRC, BYD will adopt prudent development strategies for its automobile business. The Group will further strengthen its business foundation in 2005. In order to increase its market share, the Group intends to develop and launch new models of automobiles with varying capacities by mid 2005. Also, the Group will further explore opportunities to produce electric motor vehicles and hybrid vehicles using its rechargeable power battery products. In order to capture the future rebound of the automobile industry in the PRC, the Group will continue to research and develop new models and upgrade its existing automobile engines. BYD targets to become a market leader in the domestic automobile market in the coming years.