notes to financial statements

31 December 2004

1. CORPORATE INFORMATION

During the year, the Group was involved in the manufacture and sale of telecom products and accessories.

In September 2004, the Group disposed of its entire interest in First Precision Holdings Limited ("First Precision") and its subsidiaries (collectively referred to as the "First Precision Group") and CCT Investment Limited ("CCT Investment") to CCT Telecom Holdings Limited ("CCT Telecom"), details of which are set out in notes 32(c) and 37(1) to the financial statements. The principal activities of First Precision Group are the design, manufacture and sale of power supply components including linear and switching transformers and adaptors. The principal activity of CCT Investment is property holding.

In the opinion of the directors, the ultimate holding company of the Company is CCT Telecom, which is incorporated in the Cayman Islands with limited liability and is listed on The Stock Exchange of Hong Kong Limited (the "Stock Exchange").

2. IMPACT OF RECENTLY ISSUED HONG KONG FINANCIAL REPORTING STANDARDS ("HKFRSs")

The Hong Kong Institute of Certified Public Accountants has issued a number of new Hong Kong Financial Reporting Standards and Hong Kong Accounting Standards, herein collectively referred to as the new HKFRSs, which are generally effective for accounting periods beginning on or after 1 January 2005. The Group has not early adopted these new HKFRS in the financial statements for the year ended 31 December 2004. The Group has already commenced an assessment of the impact of these new HKFRSs but is not yet in a position to state whether these new HKFRSs would have a significant impact on its results of operations and financial position.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of preparation

These financial statements have been prepared in accordance with Hong Kong Financial Reporting Standards (which also include Statements of Standard Accounting Practice and Interpretations) issued by the Hong Kong Institute of Certified Public Accountants, accounting principles generally accepted in Hong Kong and the disclosure requirements of the Hong Kong Companies Ordinance. They have been prepared under the historical cost convention.

Basis of consolidation

The consolidated financial statements include the financial statements of the Company and its subsidiaries for the year ended 31 December 2004. The results of subsidiaries acquired or disposed of during the year are consolidated from or to their effective dates of acquisition or disposal, respectively. All significant intercompany transactions and balances within the Group are eliminated on consolidation.

Subsidiaries

A subsidiary is a company whose financial and operating policies the Company controls, directly or indirectly, so as to obtain benefits from its activities.

The results of subsidiaries are included in the Company's profit and loss account to the extent of dividends received and receivable. The Company's interests in subsidiaries are stated at cost less any impairment losses.

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3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Cont'd)*

Goodwill

Goodwill arising on the acquisition of subsidiaries represents the excess of the cost of the acquisition over the Group's share of the fair values of the identifiable assets and liabilities acquired as at the date of acquisition.

Goodwill arising on acquisition is recognised in the consolidated balance sheet as an asset and amortised on the straight-line basis over its estimated useful life of 20 years.

On disposal of subsidiaries, the gain or loss on disposal is calculated by reference to the net assets at the date of disposal, including the attributable amount of goodwill which remains unamortised and any relevant reserves, as appropriate.

The carrying amount of goodwill is reviewed annually and written down for impairment when it is considered necessary. A previously recognised impairment loss for goodwill is not reversed unless the impairment loss was caused by a specific external event of an exceptional nature that was not expected to recur, and subsequent external events have occurred which have reversed the effect of that event.

Impairment of assets

An assessment is made at each balance sheet date of whether there is any indication of impairment of any asset, or whether there is any indication that an impairment loss previously recognised for an asset in prior years may no longer exist or may have decreased. If any such indication exists, the asset's recoverable amount is estimated. An asset's recoverable amount is calculated as the higher of the asset's value in use and its net selling price.

An impairment loss is recognised only if the carrying amount of an asset exceeds its recoverable amount. An impairment loss is charged to the profit and loss account in the period in which it arises.

A previously recognised impairment loss is reversed only if there has been a change in the estimates used to determine the recoverable amount of an asset, however not to an amount higher than the carrying amount that would have been determined (net of any depreciation/amortisation), had no impairment loss been recognised for the asset in prior years. A reversal of an impairment loss is credited to the profit and loss account in the period in which it arises.

Fixed assets and depreciation

Fixed assets, other than construction in progress, are stated at cost less accumulated depreciation and any impairment losses. The cost of an asset comprises its purchase price and any directly attributable costs of bringing the asset to its working condition and location for its intended use. Expenditure incurred after fixed assets have been put into operation, such as repairs and maintenance, is normally charged to the profit and loss account in the period in which it is incurred. In situations where it can be clearly demonstrated that the expenditure has resulted in an increase in the future economic benefits expected to be obtained from the use of the fixed assets, the expenditure is capitalised as an additional cost of that asset.

31 December 2004

3. **SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES** *(Cont'd)*

Fixed assets and depreciation *(Cont'd)*

Depreciation is calculated on the straight-line basis to write off the cost of each asset over its estimated useful life. The principal annual rates used for this purpose are as follows:

Leasehold land	2%–6%
Buildings	5%–6%
Plant and machinery	10%–20%
Tools, moulds and equipment	10%–20%
Furniture and office equipment	10%–20%
Motor vehicles	15%–30%

Improvements to leasehold buildings are depreciated over the shorter of the lease terms and the rate of 20% per annum.

The gain or loss on disposal or retirement of a fixed asset recognised in the profit and loss account is the difference between the net sales proceeds and the carrying amount of the relevant asset.

Construction in progress

Construction in progress represents building under construction. It is stated at cost less any impairment losses, and is not depreciated. Cost comprises direct costs of construction and capitalised borrowing costs on related borrowed funds during period of construction. Construction in progress is reclassified to the appropriate category of fixed assets when completed and ready for use.

Intangible assets

Deferred development costs

All research costs are charged to the profit and loss account as incurred.

Expenditure incurred on projects to develop new products is capitalised and deferred only when the projects are clearly defined; the expenditure is separately identifiable and can be measured reliably; there is reasonable certainty that the projects are technically feasible; and the products have commercial value. Product development expenditure which does not meet these criteria is expensed when incurred.

Deferred development costs are stated at cost less any impairment losses and are amortised using the straight-line basis over the commercial lives of the underlying products not exceeding four years, commencing from the date when the products are put into commercial production.

Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is determined on the weighted average basis and, in the case of work in progress and finished goods, comprises direct materials, direct labour and an appropriate proportion of overheads. Net realisable value is based on the estimated selling prices less any estimated costs to be incurred to completion and disposal.

31 December 2004

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Cont'd)*

Income tax

Income tax comprises current and deferred tax. Income tax is recognised in the profit and loss account, or in equity if it relates to items that are recognised in the same or a different period directly in equity.

Deferred tax is provided, using the liability method, on all temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred tax liabilities are recognised for all taxable temporary differences:

- except where the deferred tax liability arises from goodwill or the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and

- in respect of taxable temporary differences associated with investments in subsidiaries, except where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred tax assets are recognised for all deductible temporary differences, carryforward of unused tax assets and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carryforward of unused tax assets and unused tax losses can be utilised:

- except where the deferred tax asset relating to the deductible temporary differences arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and

- in respect of deductible temporary differences associated with investments in subsidiaries, deferred tax assets are only recognised to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised. Conversely, previously unrecognised deferred tax assets are recognised to the extent that it is probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the balance sheet date.

Leased assets

Leases that transfer substantially all the rewards and risks of ownership of assets to the Group, other than legal title, are accounted for as finance leases. At the inception of a finance lease, the cost of the leased assets is capitalised at the present value of the minimum lease payments and recorded together with the obligation, excluding the interest element, to reflect the purchase and financing. Assets held under capitalised finance leases are included in fixed assets and depreciated over the shorter of the lease terms and the estimated useful lives of the assets. The finance costs of such leases are charged to the profit and loss account so as to provide a constant periodic rate of charge over the lease terms.

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3. **SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES** *(Cont'd)*

Leased assets *(Cont'd)*

Leases where substantially all the rewards and risks of ownership of assets remain with the lessor are accounted for as operating leases. Rentals payable under operating leases are charged to the profit and loss account on the straight-line basis over the lease terms.

Employee benefits

Paid leave carried forward

The Group provides paid annual leave to its employees under their employment contracts on a calendar year basis. Under certain circumstances, such leave which remains untaken as at the balance sheet date is permitted to be carried forward and utilised by the respective employees in the following year. An accrual is made at the balance sheet date for the expected future cost of such paid leave earned during the year by the employees and carried forward.

Employment Ordinance long service payments

Certain of the Group's employees have completed the required number of years of service to the Group in order to be eligible for long service payments under the Hong Kong Employment Ordinance in the event of the termination of their employment. The Group is liable to make such payments in the event that such a termination of employment meets the circumstances specified in the Employment Ordinance.

A contingent liability is disclosed in respect of possible future long service payments to employees, as a number of current employees have achieved the required number of years of service to the Group, to the balance sheet date, in order to be eligible for long service payments under the Employment Ordinance if their employment is terminated in the circumstances specified. A provision has not been recognised in respect of such possible payments, as it is not considered probable that the situation will result in a material future outflow of resources from the Group.

Share option scheme

The Company operates a share option scheme for the purpose of providing incentives and rewards to eligible participants who contribute to the success of the Group's operations. The financial impact of the share options granted under the share option scheme is not recorded in the Company's or the Group's balance sheet until such time as the options are exercised, and no charge is recorded in the profit and loss account or balance sheet for their cost. Upon the exercise of the share options, the resulting shares issued are recorded by the Company as additional share capital at the nominal value of the shares, and the excess of the exercise price per share over the nominal value of the shares is recorded by the Company in the share premium account. Options which are cancelled prior to their exercise date, or which lapse, are deleted from the register of outstanding shares.

31 December 2004

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Cont'd)*

Employee benefits *(Cont'd)*

Pension schemes

The Group operates a defined contribution Mandatory Provident Fund retirement benefits scheme (the "MPF Scheme") under the Mandatory Provident Fund Schemes Ordinance, for those employees who are eligible to participate in the MPF Scheme. Contributions are made based on a percentage of the employees' relevant income and are charged to the profit and loss account as they become payable in accordance with the rules of the MPF Scheme. The assets of the MPF Scheme are held separately from those of the Group in an independently administered fund. The Group's employer contributions vest fully with the employees when contributed into the MPF Scheme, except for the Group's employer voluntary contributions accumulated in the previous retirement scheme before 1 December 2000, which are refunded to the Group when the employee leaves employment prior to the contributions vesting fully, in accordance with the rules of the MPF Scheme.

In addition to the MPF Scheme, the Group operates a separate defined contribution retirement benefits scheme for those employees who are eligible to participate in this scheme. This scheme operates in a similar way to the MPF Scheme, except that the contributions are made based on a percentage of the employees' basic salary and when an employee leaves this scheme before his/her interest in the Group's employer contributions has vested fully, the ongoing contributions payable by the Group are reduced by the relevant amount of the forfeited employer contributions.

Foreign currencies

Foreign currency transactions are recorded at the applicable exchange rates ruling at the transaction dates. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated at the applicable exchange rates ruling at that date. Exchange differences are dealt with in the profit and loss account.

On consolidation, the financial statements of overseas subsidiaries are translated into Hong Kong dollars using the net investment method. The profit and loss accounts of overseas subsidiaries are translated into Hong Kong dollars at the weighted average exchange rates for the year, and their balance sheets are translated into Hong Kong dollars at the exchange rates at the balance sheet date. The resulting translation differences are included in the exchange fluctuation reserve.

For the purpose of the consolidated cash flow statement, the cash flows of overseas subsidiaries are translated into Hong Kong dollars at the exchange rates ruling at the dates of the cash flows. Frequently recurring cash flows of overseas subsidiaries which arise throughout the year are translated into Hong Kong dollars at the weighted average exchange rates for the year.

Cash and cash equivalents

For the purpose of the consolidated cash flow statement, cash and cash equivalents comprise cash on hand and demand deposits, and short term highly liquid investments which are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value, and have a short maturity of generally within three months when acquired, less bank overdrafts which are repayable on demand and form an integral part of the Group's cash management.

For the purpose of the balance sheet, cash and cash equivalents comprise cash on hand and at banks, including term deposits, which are not restricted as to use.

31 December 2004

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Cont'd)*

Revenue recognition

Revenue is recognised when it is probable that the economic benefits will flow to the Group and when the revenue can be measured reliably, on the following bases:

(a) from the sale of goods, when the significant risks and rewards of ownership have been transferred to the buyer, provided that the Group maintains neither managerial involvement to the degree usually associated with ownership, nor effective control over the goods sold;

(b) rental income, on a time proportion basis over the lease terms; and

(c) interest income, on a time proportion basis taking into account the principal outstanding and the effective interest rate applicable.

Related parties

Parties are considered to be related if one party has the ability, directly or indirectly, to control the other party or exercise significant influence over the other party in making financial and operating decisions. Parties are also considered to be related if they are subject to common control or common significant influence. Related parties may be individuals or corporate entities.

4. SEGMENT INFORMATION

Segment information is presented by way of two segment formats: (i) on a primary segment reporting basis, by business segment; and (ii) on a secondary segment reporting basis, by geographical segment.

The Group's operating businesses are structured and managed separately according to the nature of their operations and the products and services they provide. Each of the Group's business segments represents a strategic business unit that offers products and services which are subject to risks and returns that are different from those of the other business segments. Summary details of the business segments are as follows:

(a) the telecom products segment engages in the manufacture and sale of telecom products and accessories; and

(b) the corporate segment includes corporate income and expense items.

31 December 2004

4. SEGMENT INFORMATION *(Cont'd)*

In determining the Group's geographical segments, revenues are attributed to the segments based on the location of the customers, and assets are attributed to the segments based on the location of the assets.

(a) Business segments

The following table presents revenue and profit/(loss) for the Group's business segments.

Group

	Telecom products		Corporate		Total	
HK$ million	**2004**	2003	**2004**	2003	**2004**	2003
Segment revenue:						
Sales to external customers	**3,846**	1,925	**—**	—	**3,846**	1,925
Other revenue and gains	**37**	12	**20**	—	**57**	12
Total revenue	**3,883**	1,937	**20**	—	**3,903**	1,937
Segment results	**197**	119	**(4)**	(9)	**193**	110
Interest income					**1**	1
Finance costs					**(53)**	(29)
Profit before tax					**141**	82
Tax					**(16)**	(9)
Net profit from ordinary activities attributable to shareholders					**125**	73

No analysis of the assets and liabilities and other segment information regarding the Group's business segments for the two years ended 31 December 2004 has been presented as over 90% of the Group's revenue is derived from the telecom products segment.

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4. SEGMENT INFORMATION *(Cont'd)*

(b) Geographical segments

The following table presents revenue information for the Group's geographical segments.

Group

HK$ million	United States of America		PRC, including Hong Kong		European Union		Others		Consolidated	
	2004	2003	**2004**	2003	**2004**	2003	**2004**	2003	**2004**	2003
Segment revenue:										
Sales to external customers	**2,377**	1,244	**640**	343	**139**	65	**690**	273	**3,846**	1,925
Other revenue and gains	**—**	—	**57**	12	**—**	—	**—**	—	**57**	12
Total revenue	**2,377**	1,244	**697**	355	**139**	65	**690**	273	**3,903**	1,937

Over 90% of the Group's assets are located in the People's Republic of China (the "PRC") including Hong Kong. Accordingly, no analysis of the assets and capital expenditures by geographical segments is presented.

5. TURNOVER

Turnover represents the net invoiced value of goods sold, after allowances for returns and trade discounts.

Revenue from the following activities has been included in turnover:

HK$ million	**2004**	2003
Manufacture and sale of telecom products and accessories	**3,846**	1,925
Interest income	**1**	1
	3,847	1,926

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6. PROFIT FROM OPERATING ACTIVITIES

The Group's profit from operating activities is arrived at after charging:

HK$ million	Notes	2004	2003
Cost of inventories sold		3,480	1,693
Depreciation	14	85	43
Less: Amount capitalised in deferred development costs		—	(2)
		85	41
Minimum lease payments under operating leases in respect of land and buildings		5	6
Research and development costs:			
Deferred expenditure amortised*	15	30	20
Current year expenditure	15	50	19
Goodwill:	16		
Amortisation for the year**		2	2
Impairment arising during the year**		1	—
		3	2
Staff costs (excluding directors' remuneration — note 8)***		266	129
Pension scheme contributions		3	2
Less: Amount capitalised in deferred development costs		(29)	(11)
		240	120
Auditors' remuneration		3	3
Bad and doubtful debt provisions on trade receivables		3	—
Bad and doubtful debt provisions on other receivables		3	—
Write off of fixed assets		—	18
Write off of deferred development costs**	15	15	7
Provision for slow-moving and obsolete inventories*		33	8
and after crediting:			
Net rental income		6	3
Exchange gains, net		6	—
Gain on disposals of fixed assets, net		1	—
Gain on disposal of subsidiaries	32(c)	20	—

* The amortisation of deferred development costs and provision for slow-moving and obsolete inventories are included in "Cost of sales" on the face of the consolidated profit and loss account.

** The amortisation and impairment of goodwill for the year and write off of deferred development costs for the year are included in "Other operating expenses" on the face of the consolidated profit and loss account.

*** The effect of forfeited contributions on the Group's contributions to the pension schemes for the year, and the amounts of forfeited contributions available to reduce contributions in future years, were not material.

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7. FINANCE COSTS

	Group	
HK$ million	**2004**	2003
Interest on bank loans wholly repayable within five years	**2**	1
Interest on convertible notes	**51**	28
	53	29

8. DIRECTORS' REMUNERATION

Directors' remuneration for the year, disclosed pursuant to the Rules Governing the Listing of Securities on the Stock Exchange (the "Listing Rules") and Section 161 of the Hong Kong Companies Ordinance, is as follows:

	Group	
HK$ million	**2004**	2003
Fees:		
Executive directors	**—**	—
Independent non-executive directors	**—**	—
	—	—
Executive directors' other emoluments:		
Salaries, allowances and benefits in kind	**13**	6
Performance related bonuses	**5**	—
Pension scheme contributions	**1**	—
	19	6
	19	6

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8. DIRECTORS' REMUNERATION *(Cont'd)*

The number of directors whose remuneration fell within the following bands is as follows:

	Number of directors	
	2004	2003
Nil–HK$1,000,000	**4**	4
HK$1,000,001–HK$1,500,000	**—**	1
HK$1,500,001–HK$2,000,000	**—**	1
HK$2,000,001–HK$2,500,000	**—**	1
HK$4,000,001–HK$4,500,000	**2**	—
HK$4,500,001–HK$5,000,000	**1**	—
HK$5,000,001–HK$5,500,000	**1**	—
	8	7

There was no arrangement under which a director waived or agreed to waive any remuneration during the year.

In 2003, certain directors were granted share options in respect of their services to the Group under the share option scheme of the Company, and further details of which are set out in note 30 to the financial statements. No value in respect of the share options granted has been charged to the profit and loss account, or is otherwise included in the above directors' remuneration disclosures.

9. FIVE HIGHEST PAID EMPLOYEES

The five highest paid employees during the year included four (2003: three) directors, details of whose remuneration are set out in note 8 above. Details of the remuneration of the remaining one (2003: two) non-director, highest paid employee for the year are as follows:

	Group	
HK$ million	**2004**	2003
Salaries, allowances and benefits in kind	**2**	1

The number of the non-director, highest paid employees fell within the following bands is as follows:

	Number of employees	
	2004	2003
Nil–HK$1,000,000	**—**	2
HK$2,000,001–HK$2,500,000	**1**	—

In 2003, a non-director, highest paid employee was granted share options in respect of his service to the Group, future details of which are included in the disclosures in note 30 to the financial statements. No value in respect of the share options granted has been charged to the profit and loss account, or is otherwise included in the above non-director, highest paid employees' remuneration disclosures.

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10. TAX

Hong Kong profits tax has been provided at the rate of 17.5% (2003: 17.5%) on the estimated assessable profits arising in Hong Kong during the year. Taxes on profits assessable elsewhere have been calculated at the rates of tax prevailing in the countries in which the Group operates, based on existing legislation, interpretations and practices in respect thereof.

Certain PRC subsidiaries of the Group, which are categorised as wholly foreign-owned enterprises, are entitled to preferential tax treatments including full exemption from the PRC income tax for two years starting from the first profit-making year, followed by a 50% reduction for the next consecutive three years.

HK$ million	**2004**	2003
Group:		
Current — Hong Kong		
Charge for the year	**10**	8
Overprovision in prior years	**(3)**	(1)
Current — Elsewhere		
Charge for the year	**4**	2
Underprovision in prior years	**1**	—
Deferred — note 28	**4**	—
Total tax charge for the year	**16**	9

A reconciliation of the tax expense applicable to profit before tax using the statutory rates for the countries in which the Company and its subsidiaries are domiciled to the tax expense at the effective tax rates, and a reconciliation of the applicable rates (i.e., the statutory tax rates) to the effective tax rates, are as follows:

Group — 2004

	Hong Kong HK$ million	**%**	**PRC, excluding Hong Kong HK$ million**	**%**	**Total HK$ million**	**%**
Profit before tax	**1**		**140**		**141**	
Tax at the statutory or applicable tax rate	**0.2**	**17.5**	**33.6**	**24.0**	**33.8**	**24.0**
Lower tax rate for specific provinces or local authority	**—**	**—**	**(19.3)**	**(13.8)**	**(19.3)**	**(13.7)**
Tax exemption	**—**	**—**	**(29.6)**	**(21.1)**	**(29.6)**	**(21.0)**
Adjustments in respect of current tax of previous periods	**(2.3)**	**(230)**	**1.2**	**0.9**	**(1.1)**	**(0.8)**
Income not subject to tax	**(8.0)**	**(800)**	**(4.9)**	**(3.5)**	**(12.9)**	**(9.1)**
Expenses not deductible for tax	**19.6**	**1,962.5**	**19.1**	**13.6**	**38.7**	**27.4**
Tax losses not recognised	**1.5**	**150**	**4.9**	**3.5**	**6.4**	**4.5**
Tax charge at the Group's effective rate	**11.0**	**1,100**	**5.0**	**3.6**	**16.0**	**11.3**

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10. TAX *(Cont'd)*

Group — 2003

	Hong Kong		PRC, excluding Hong Kong		Total	
	HK$ million	%	HK$ million	%	HK$ million	%
Profit before tax	8		74		82	
Tax at the statutory or applicable tax rate	1	17.5	18	24	19	23.3
Higher tax rate for specific provinces or local authority	—	—	0.4	0.6	0.4	0.6
Effect on opening deferred tax of increase in rates	0.1	1.1	—	—	0.1	0.1
Tax exemption	—	—	(2.1)	(2.8)	(2.1)	(2.6)
Income not subject to tax	(0.1)	(1.8)	(17.1)	(22.8)	(17.2)	(20.6)
Expenses not deductible for tax	6	71.6	2.8	3.9	8.8	10.9
Tax charge at the Group's effective rate	7	88.4	2	2.9	9	11.7

11. NET LOSS FROM ORDINARY ACTIVITIES ATTRIBUTABLE TO SHAREHOLDERS

The net loss from ordinary activities attributable to shareholders for the year ended 31 December 2004 dealt with in the financial statements of the Company, was approximately HK$34 million (2003: net profit of HK$1 million) (note 31(b)).

12. DIVIDEND

No dividends have been paid or declared by the Company for the year ended 31 December 2004 (2003: Nil).

13. EARNINGS PER SHARE

The calculation of basic earnings per share is based on the net profit attributable to shareholders for the year of HK$125 million (2003: HK$73 million), and the weighted average number of 14,426,127,480 (2003: 12,066,769,981) ordinary shares in issue during the year.

The calculation of diluted earnings per share is based on the net profit attributable to shareholders for the year of HK$176 million (2003: HK$101 million), after adjustment for interest saved upon deemed exercise of all convertible notes during the year. The weighted average number of ordinary shares used in the calculation of diluted earnings per share is 71,487,171,676 (2003: 46,453,485,820) which includes the weighted average number of 14,426,127,480 (2003: 12,066,769,981) ordinary shares in issue during the year, as used in the basic earnings per share calculation; the weighted average of 56,891,451,991 (2003: 34,263,463,796) ordinary shares assumed to have been issued at no consideration on the deemed exercise of all convertible notes during the year and the weighted average of 169,592,205 (2003: 123,252,043) ordinary shares assumed to have been issued at no consideration on the deemed exercise of all share options during the year.

31 December 2004

14. FIXED ASSETS

Group

HK$ million	Construction in progress	Leasehold land and buildings	Plant and machinery	Tools, moulds and equipment	Furniture and office equipment	Motor vehicles	Total
Cost:							
At 1 January 2004	—	531	213	104	71	15	934
Additions	39	8	49	26	6	4	132
Disposal of subsidiaries — note 32(c)	—	(27)	(19)	(7)	(6)	(2)	(61)
Disposals	—	—	—	(1)	—	(1)	(2)
At 31 December 2004	39	512	243	122	71	16	1,003
Accumulated depreciation:							
At 1 January 2004	—	50	103	51	40	9	253
Depreciation provided during the year	—	26	29	19	9	2	85
Disposal of subsidiaries — note 32(c)	—	(3)	(13)	(4)	(4)	(2)	(26)
Disposals	—	—	—	(1)	—	—	(1)
At 31 December 2004	—	73	119	65	45	9	311
Net book value:							
At 31 December 2004	39	439	124	57	26	7	692
At 31 December 2003	—	481	110	53	31	6	681

The net book value of the Group's fixed assets held under finance leases included in the total amounts of motor vehicles at 31 December 2004, amounted to HK$2 million (2003: HK$2 million).

The Group's leasehold land and buildings included above are situated in the PRC and are held under medium term leases.

31 December 2004

15. INTANGIBLE ASSETS

Group

HK$ million	Deferred development costs
Cost:	
At 1 January 2004	85
Additions	50
Write off	(36)
At 31 December 2004	99
Accumulated amortisation:	
At 1 January 2004	62
Amortisation provided during the year	30
Write back	(21)
At 31 December 2004	71
Net book value:	
At 31 December 2004	28
At 31 December 2003	23

31 December 2004

16. GOODWILL

The amounts of the goodwill capitalised as an asset in the consolidated balance sheet, arising from the acquisition of subsidiaries, are as follows:

Group

	HK$ million
Cost:	
At 1 January 2004	58
Disposal of subsidiaries — note 32(c)	(33)
At 31 December 2004	25
Accumulated amortisation and impairment:	
At beginning of year	3
Amortisation provided during the year	2
Impairment provided during the year	1
Disposal of subsidiaries — note 32(c)	(3)
At 31 December 2004	3
Net book value:	
At 31 December 2004	22
At 31 December 2003	55

17. INTERESTS IN SUBSIDIARIES

	Company	
HK$ million	**2004**	2003
Unlisted shares, at cost	**308**	308
Due from subsidiaries	**425**	595
Due to subsidiaries	**(2)**	(7)
	731	896
Provision for impairment	**(53)**	(10)
	678	886

The balances with the subsidiaries are unsecured, interest-free and are repayable on demand.

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17. INTERESTS IN SUBSIDIARIES *(Cont'd)*

Particulars of the principal subsidiaries are as follows:

Name	Place of incorporation/ registration and operations	Nominal value of issued ordinary/ registered share capital	Percentage of equity attributable to the Company Direct	Indirect	Principal activities
Empire Success Holdings Limited	British Virgin Islands	US$16,501 Ordinary	100	—	Investment holding
CCT Marketing Limited	British Virgin Islands/ Hong Kong	US$1 Ordinary	—	100	Trading of telecom products
CCT Telecom (HK) Limited	Hong Kong	HK$2,600,000 Ordinary	—	100	Sourcing of telecom products
Huiyang CCT Telecommunications Products Limited	People's Republic of China/ Mainland China	HK$80,000,000 Registered*	—	100	Manufacture of telecom products

* Registered as a wholly-foreign owned enterprise under the PRC law.

During the year, the Group disposed of its entire interest in First Precision Group, including Electronic Sales Limited ("ESL") and 東莞易訊電子製品有限公司, and CCT Investment to CCT Telecom. Further details of the disposal are included in note 32(c) and 37(1) to the financial statements.

The above table lists the subsidiaries of the Company which, in the opinion of the directors, principally affected the results for the year or formed a substantial portion of the net assets of the Group. To give details of other subsidiaries would, in the opinion of the directors, result in particulars of excessive length.

18. INVENTORIES

	Group	
HK$ million	**2004**	2003
Raw materials	**41**	33
Work in progress	**42**	44
Finished goods	**85**	78
	168	155

The carrying amount of inventories carried at net realisable value included in the above balance was HK$18 million (2003: Nil) as at the balance sheet date.

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19. TRADE AND BILLS RECEIVABLES

An aged analysis of the trade and bills receivables as at the balance sheet date, based on invoice date, and net of provisions, is as follows:

Group

	2004		2003	
	HK$ million	Percentage	HK$ million	Percentage
Current to 30 days	283	39	252	42
31 to 60 days	242	33	184	31
61 to 90 days	202	27	154	26
Over 90 days	9	1	4	1
	736	100	594	100

The Group offers an average credit period of 30–90 days to its trade customers.

20. PREPAYMENTS, DEPOSITS AND OTHER RECEIVABLES

	Group		Company	
HK$ million	2004	2003	2004	2003
Prepayments	2	—	1	—
Deposits and other receivables	9	7	—	—
	11	7	1	—

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21. CASH AND CASH EQUIVALENTS AND PLEDGED TIME DEPOSITS

	Group		Company	
HK$ million	**2004**	**2003**	**2004**	**2003**
Cash and bank balances	**347**	317	**22**	1
Time deposits	**170**	233	**26**	10
	517	550	**48**	11
Less: Time deposits pledged for bank borrowings — note 34	**(95)**	(100)	**—**	—
Cash and cash equivalents	**422**	450	**48**	11

At the balance sheet date, the cash and bank balances of the Group denominated in Renminbi ("RMB") amounted to HK$5 million (2003: HK$12 million). The RMB is not freely convertible into other currencies, however, under Mainland China's Foreign Exchange Control Regulations and Administration of Settlement, Sale and Payment of Foreign Exchange Regulations, the Group is permitted to exchange RMB for other currencies through banks authorised to conduct foreign exchange business.

22. TRADE AND BILLS PAYABLES

An aged analysis of the trade and bills payables as at the balance sheet date based on invoice date, is as follows:

Group

	2004		2003	
	HK$ million	**Percentage**	HK$ million	Percentage
Current to 30 days	**249**	**26**	209	24
31 to 60 days	**181**	**19**	230	27
61 to 90 days	**204**	**21**	175	20
Over 90 days	**329**	**34**	245	29
	963	**100**	859	100

Included in trade and bills payables are trade payables of HK$194 million (2003: HK$95 million) due to Neptune Holding Limited ("Neptune") and ESL, being wholly-owned subsidiaries of CCT Telecom, which are repayable within 120 days from invoice date.

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23. OTHER PAYABLES AND ACCRUALS

	Group		Company	
HK$ million	**2004**	2003	**2004**	2003
Other payables	**15**	30	**—**	—
Accruals	**90**	83	**4**	1
	105	113	**4**	1

24. INTEREST-BEARING BANK AND OTHER BORROWINGS

		Group	
HK$ million	Notes	**2004**	2003
Current portion of bank loans, secured	25	**115**	111
Current portion of finance lease payables	26	**1**	1
		116	112

25. INTEREST-BEARING BANK LOANS, SECURED

	Group	
HK$ million	**2004**	2003
Bank loans, repayable:		
Within one year or on demand	**115**	111
In the second year	**22**	—
	137	111
Portion classified as current liabilities — note 24	**(115)**	(111)
	22	—

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26. FINANCE LEASE PAYABLES

The Group leases certain of its furniture and office equipment and motor vehicles for business use. These leases are classified as finance leases and have remaining lease terms ranging from one to two years.

At 31 December 2004, the total future minimum lease payments under financial leases and their present value were as follows:

Group

HK$ million	**Minimum lease payments 2004**	Minimum lease payments 2003	**Present value of minimum lease payments 2004**	Present value of minimum lease payments 2003
Amounts payable:				
Within one year	**1**	1	**1**	1
In the second year	**1**	1	**1**	1
Total minimum finance lease payments	**2**	2	**2**	2
Future finance charges	**—**	—		
Total net finance lease payables	**2**	2		
Portion classified as current liabilities — note 24	**(1)**	(1)		
Non-current portion	**1**	1		

27. CONVERTIBLE NOTES

	Group		Company	
HK$ million	**2004**	2003	**2004**	2003
2004 Convertible notes — note (a)	**—**	8	**—**	8
2005 Convertible notes — note (b)	**45**	45	**45**	45
2005 Convertible notes — note (c)	**—**	10	**—**	10
2008 Convertible notes — note (d)	**615**	768	**615**	768
	660	831	**660**	831
Portion classified as current liabilities	**(45)**	(8)	**(45)**	(8)
Non-current portion	**615**	823	**615**	823

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27. CONVERTIBLE NOTES *(Cont'd)*

Notes:

(a) On 19 July 2002, CCT Technology Holdings Limited ("CCT Technology"), a direct wholly-owned subsidiary of the Company, issued convertible notes with an aggregate principal amount of HK$20 million through a placing agent to an independent third party and which were subsequently replaced by the convertible notes issued by the Company on 4 November 2002. The convertible notes provide the holder the option right to convert the principal amount into ordinary shares of HK$0.01 each of the Company on any business day until five business days prior to the maturity of the convertible notes at a conversion price of HK$0.01 per share.

The principal amount of the convertible notes bears interest at a rate of 5% per annum and the convertible notes will mature on the second anniversary of the date of their issue.

On 24 June 2003, part of the principal amount of the convertible notes of HK$12 million was converted into 1,200,000,000 shares of the Company of HK$0.01 each at a conversion price of HK$0.01 per share.

On 8 July 2004, the remaining principal amount of HK$8 million was converted into 800,000,000 shares of the Company of HK$0.01 each at a conversion price of HK$0.01 per share. There was no outstanding principal amount of the convertible notes as at 31 December 2004.

(b) On 17 May 2002, CCT Technology issued convertible note with principal amount of HK$45 million (the "2005 Convertible Note") to Emporium International Limited, an indirect wholly-owned subsidiary of CCT Telecom, which were subsequently replaced by the convertible note issued by the Company on 4 November 2002. The convertible notes provide the holder the option right to convert the principal amount into ordinary shares of HK$0.01 each of the Company on any business day until five business days prior to the maturity of the convertible notes at a conversion price of HK$0.01 per share.

The principal amount of the convertible note is interest-free and the convertible notes will mature on the third anniversary of the date of its issue.

During the year, the convertible note was disposed of in full by Emporium International Limited to New Capital Industrial Limited, a company controlled by Mr. Mak Shiu Tong, Clement, the Chairman and a director of the Company, and his family members for a cash consideration of HK$45 million.

(c) On 14 May 2003, the Company issued convertible notes with an aggregate principal amount of HK$21 million through a placing agent to several independent third parties. The convertible notes provide the holders the option right to convert the principal amount into the Company's ordinary shares of HK$0.01 each on any business day until five business days prior to the maturity of the convertible notes at a conversion price of HK$0.01 per share.

The principal amount of the convertible notes bears interest at a rate of 2% per annum and the convertible notes will mature on the second anniversary of the date of their issue.

In June 2003, part of the principal amount of the convertible notes of HK$11 million was converted into 1,100,000,000 shares of the Company of HK$0.01 each at a conversion price of HK$0.01 per share.

During the year, the remaining convertible notes with an aggregate principal amount of HK$10 million were converted into 1,000,000,000 shares of the Company of HK$0.01 each at a conversion price of HK$0.01 per share. There was no outstanding principal amount of the convertible notes as at 31 December 2004.

(d) On 30 June 2003, the Company issued convertible note with principal amount of HK$768 million to Noble Team Investments Limited, an indirect wholly-owned subsidiary of CCT Telecom, as the consideration for the acquisition of the entire interest in Empire Success Holdings Limited ("ESH") from an indirect wholly-owned subsidiary of CCT Telecom, details of which are set out in note 32(b) to the financial statements. The convertible note provides the holder the option right to convert the principal amount into the Company's ordinary shares of HK$0.01 each on any business day until five business days prior to the maturity of the convertible notes at a conversion price of HK$0.014 per share. The convertible note bears interest at the prime or best lending rate as quoted by The Hongkong and Shanghai Banking Corporation Limited for Hong Kong dollar loans plus 2% per annum and will mature on the fifth anniversary of the date of its issue.

During the year, part of the convertible note with principal amount of HK$14 million was converted into 1,000,000,000 shares of the Company of HK$0.01 each at a conversion price of HK$0.014 per share. On 13 September 2004, the convertible note with principal amount of HK$139 million was cancelled for the purpose of satisfying the consideration receivable from CCT Telecom in respect of the disposal of the First Precision Group and CCT Investment.

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28. DEFERRED TAX

The movements in deferred tax liabilities and assets during the year are as follows:

Deferred tax liabilities

Group HK$ million	**2004** **Accelerated tax depreciation**
At 1 January 2004	**3**
Deferred tax credited to the profit and loss account during the year — note 10	**(1)**
Gross deferred tax liabilities At 31 December 2004	**2**

Deferred tax assets

Group **HK$ million**	**2004** **Losses available for offset against future taxable profit**
At 1 January 2004	**9**
Deferred tax charged to the profit and loss account during the year — note 10	**(5)**
Gross deferred tax assets at 31 December 2004	**4**
Net deferred tax assets at 31 December 2004	**2**

Deferred tax liabilities

Group HK$ million	2003 Accelerated tax depreciation
At 1 January 2003	1
Deferred tax credited to the profit and loss account during the year — note 10	(1)
Acquisition of subsidiaries — note 32(b)	3
Gross deferred tax liabilities At 31 December 2003	3

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28. DEFERRED TAX *(Cont'd)*

Deferred tax assets

Group HK$ million	2003 Losses available for offset against future taxable profit
At 1 January 2003	—
Deferred tax charged to the profit and loss account during the year — note 10	(1)
Acquisition of subsidiaries — note 32(b)	10
Gross deferred tax assets at 31 December 2003	9
Net deferred tax assets at 31 December 2003	6

The Group has tax losses arising in Hong Kong of HK$25 million (2003: HK$24 million) and in Mainland China of HK$11 million (2003: HK$8 million) that are available indefinitely for offsetting against future taxable profits of the companies in which the losses arose. Deferred tax assets have not been recognised in respect of these losses as they have arisen in subsidiaries that have been loss-making for some time.

At 31 December 2004, there was no significant unrecognised deferred tax liability (2003: Nil) for taxes that would be payable on the unremitted earnings of certain of the Group's subsidiaries as the Group has no liability to additional tax should such amounts be remitted.

There are no income tax consequences attaching to the payment of dividends by the Company to its shareholders.

29. SHARE CAPITAL

Shares

	Company	
HK$ million	**2004**	2003
Authorised:		
120,000,000,000 (2003: 120,000,000,000) ordinary shares of HK$0.01 each	**1,200**	1,200
Issued and fully paid:		
15,938,422,562 (2003: 13,138,422,562) ordinary shares of HK$0.01 each	**159**	131

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29. SHARE CAPITAL *(Cont'd)*

A summary of the transactions involving the Company's issued ordinary share capital during the year is as follows:

	Notes	Number of ordinary shares of HK$0.01 each	Issued share capital HK$ million
At 1 January 2003		10,838,403,562	108
Exercise of share options	(a)	19,000	—
Conversion of convertible notes	(b)	2,300,000,000	23
At 31 December 2003 and 1 January 2004		13,138,422,562	131
Conversion of convertible notes	(c)	2,800,000,000	28
At 31 December 2004		15,938,422,562	159

(a) In 2003, the subscription rights attaching to 19,000 share options were exercised at the subscription price of HK$0.014 per share (note 30), resulting in the issue of 19,000 shares of HK$0.01 each for a total cash consideration, before expenses, of HK$266.

(b) In 2003, HK$23 million worth of convertible notes were converted into 2,300,000,000 shares of the Company of HK$0.01 each. Further details relating to these convertible notes are set out in note 27 to these financial statements.

(c) During the year, HK$32 million worth of convertible notes were converted into 1,800,000,000 shares and 1,000,000,000 shares of the Company of HK$0.01 each at conversion prices of HK$0.01 and HK$0.014 per share, respectively. Further details relating to these convertible notes are set out in note 27 to these financial statements.

Share options

Details of the Company's share option scheme and the share options issued under the scheme are included in note 30 to the financial statements.

30. SHARE OPTION SCHEME

A share option scheme (the "Share Option Scheme") was conditionally adopted by the then shareholder of the Company and the shareholders of CCT Technology Holdings Limited, the then holding company of the Company, on 17 September 2002 and 15 October 2002 respectively to comply with the new amendments to the Listing Rules. The Share Option Scheme became effective on 7 November 2002. Unless otherwise cancelled or amended, the Share Option Scheme will remain in force for 10 years from that date. As at 31 December 2004, there were 1,082,781,000 share options outstanding under the Share Option Scheme. Based on these outstanding share options, the total number of shares available for issue is 1,082,781,000, which represents approximately 6.79% of the existing issued share capital of the Company as at the date of this report. No share option has been granted under the Share Option Scheme during the year.

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30. SHARE OPTION SCHEME *(Cont'd)*

The purpose of the Share Option Scheme is to provide incentives and rewards to the eligible participants who contribute to the success of the operations of the Group. Eligible participants of the Share Option Scheme include any employee, executive or officer of the Group (including executive and non-executive directors of the Group) and any supplier, consultant, agent, adviser, shareholder, customer, partner or business associate who, at the sole discretion of the board of directors of the Company (the "Board"), will contribute or has contributed to the Group.

Pursuant to the Share Option Scheme, the maximum number of shares in respect of which share options may be granted under the Share Option Scheme is such number of shares, when aggregated with shares subject to any other share option scheme(s) of the Company, must not exceed 10% of the issued share capital of the Company upon the listing of the shares of the Company on The Stock Exchange of Hong Kong Limited (the "Stock Exchange") or 30% of the issued share capital of the Company from time to time.

The maximum number of shares issuable upon exercise of the share options granted under the Share Option Scheme and any other share option scheme(s) of the Company (including exercised, cancelled and outstanding share options) to each eligible participant in any 12-month period is limited to 1% of the shares of the Company in issue as at the date of grant. Any further grant of share options in excess of this 1% limit shall be subject to the issue of a circular by the Company (and if required, the holding company) and the shareholders' approval of the Company (and if required, the approval of the shareholders of the holding company) at a general meeting.

Share options granted to a director, chief executive or substantial shareholder of the Company, or to any of their respective associates, are subject to the approval in advance by the independent non-executive directors of the Company, (and if required, the approval of the independent non-executive directors of the holding company) excluding the independent non-executive director(s) of the Company and the holding company who is/are the grantee(s) of the share options. In addition, any share options granted to a substantial shareholder or an independent non-executive director of the Company, or to any of their respective associates, in excess of 0.1% of the shares of the Company in issue as at the date of grant or with an aggregate value (based on the closing price of the shares of the Company as at the date of grant) in excess of HK$5 million, within any 12-month period, are subject to the issue of a circular by the Company (and if required, the holding company) and the shareholders' approval of the Company (and if required, the approval of the shareholders of the holding company) in advance at a general meeting.

The offer of a grant of share options may be accepted within 28 days from the date of the offer, upon payment of a nominal consideration of HK$1 in total by the grantee. The exercise period of the share options granted is determinable by the Board, and commences on a specified date and ends on a date which is not later than 10 years from the date of grant of the share options or the expiry date of the Share Option Scheme, whichever is earlier.

The exercise price of the share options is determinable by the Board, but may not be less than the highest of (i) the closing price of the shares of the Company as stated in the daily quotation sheet of the Stock Exchange on the date of grant, which must be a trading day; (ii) the average closing price of the shares of the Company as stated in the daily quotation sheets of the Stock Exchange for the five trading days immediately preceding the date of grant; and (iii) the nominal value of the shares of the Company.

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30. SHARE OPTION SCHEME *(Cont'd)*

Details of the movements of share options under the Share Option Scheme during the year were as follows:

Name or category of participant	Number of share options Outstanding as at 1 January 2004	Granted during the year	Exercised during the year	Lapsed/ Cancelled during the year	Outstanding as at 31 December 2004	Date of grant of share options	Exercise period of share options	Exercise price per share (Note) HK$
Executive directors								
Mak Shiu Tong, Clement	100,000,000	—	—	—	100,000,000	30/4/2003	30/4/2003–29/4/2008	0.014
Cheng Yuk Ching, Flora	100,000,000	—	—	—	100,000,000	30/4/2003	30/4/2003–29/4/2008	0.014
Tam Ngai Hung, Terry	100,000,000	—	—	—	100,000,000	30/4/2003	30/4/2003–29/4/2008	0.014
Tong Chi Hoi	50,000,000	—	—	—	50,000,000	30/4/2003	30/4/2003–29/4/2008	0.014
	350,000,000	—	—	—	350,000,000			
Independent non-executive directors								
Chow Siu Ngor	8,000,000	—	—	—	8,000,000	30/4/2003	30/4/2003–29/4/2008	0.014
Lau Ho Kit, Ivan	8,000,000	—	—	—	8,000,000	30/4/2003	30/4/2003–29/4/2008	0.014
	16,000,000	—	—	—	16,000,000			
Other employees								
In aggregate	716,781,000	—	—	—	716,781,000	30/4/2003	30/4/2003–29/4/2008	0.014
	716,781,000	—	—	—	716,781,000			
	1,082,781,000	—	—	—	1,082,781,000*			

Note: The exercise price of the share options is subject to adjustment(s) in the case of rights or bonus share issues, or other similar changes in the share capital of the Company.

* According to the composite offer and response document dated 31 March 2005 jointly issued by the Company and CCT Telecom, Jade Assets Company Limited (the "Offeror"), a wholly-owned subsidiary of CCT Telecom, made the voluntary conditional cash offers to acquire all the issued shares from the independent shareholders of the Company and the 2005 Convertible Note, and to cancel all the outstanding share options of the Company (collectively the "Offers"). All optionholders have accepted the Offers in respect of their entire holding of the share options at the consideration of HK$0.009 per share option. The Offers have become unconditional in all respects as to acceptances on 21 April 2005 and all such outstanding 1,082,781,000 share options under the Share Option Scheme will be cancelled in accordance with the terms of the Offers.

The financial impact of the share options granted is not recorded in the balance sheet of the Company or the Group until such time as the share options are exercised, and no charge is recorded in the profit and loss account or balance sheet for their cost. Upon exercise of the share options, the resulting shares issued are recorded by the Company as additional share capital at the nominal value of the shares, and the excess of the exercise price per share over the nominal value of the shares is recorded by the Company in the share premium account. Share options which are lapsed or are cancelled prior to their exercise date are deleted from the register of outstanding share options.

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31. RESERVES

(a) Group

The amounts of the Group's reserves and the movements therein for the current and prior years are presented in the consolidated statement of changes in equity on page 45 of the financial statements.

(b) Company

HK$ million	Special reserve	Share premium account	Accumulated losses	Total
At 1 January 2003	(56)	—	(11)	(67)
Profit for the year	—	—	1	1
At 31 December 2003 and beginning of year	(56)	—	(10)	(66)
Conversion of convertible notes	—	4	—	4
Loss for the year	—	—	(34)	(34)
At 31 December 2004	(56)	4	(44)	(96)

The special reserve of the Company represents the difference between the fair values of the shares of the subsidiaries acquired in prior years and the nominal value of the Company's shares issued in exchange therefor.

32. NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT

(a) Major non-cash transactions

(i) In 2003, the Company issued convertible notes with a principal amount of HK$768 million to an indirect wholly-owned subsidiary of CCT Telecom as consideration for the acquisition of the entire interest in ESH.

(ii) During the year, the Group entered into finance lease arrangements in respect of fixed assets with a total capital value at the inception of lease of HK$1 million (2003: Nil).

(iii) During the year, the convertible notes with an aggregate principal amount of HK$139 million were cancelled for satisfying the consideration receivable from CCT Telecom for the disposal of First Precision Group and CCT Investment.

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32. NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT *(Cont'd)*

(b) Acquisition of subsidiaries

HK$ million	Note	2004	2003
Net assets acquired:			
Fixed assets		—	700
Intangible assets		—	31
Deferred tax assets	28	—	10
Cash and bank balances		—	138
Pledged time deposits		—	59
Inventories		—	189
Trade and bills receivables		—	500
Prepayments, deposits and other receivables		—	26
Trade and bills payables		—	(619)
Tax payable		—	(8)
Other payables and accruals		—	(75)
Interest being bank borrowings		—	(200)
Finance lease payables		—	(2)
Deferred tax liabilities	28	—	(3)
		—	746
Goodwill on acquisition		—	25
		—	771
Satisfied by:			
Issue of convertible notes — note 27(d)		—	768
Cash paid for incidental acquisition costs		—	3
		—	771

An analysis of the net inflow of cash and cash equivalents in respect of the acquisition of subsidiaries is as follows:

HK$ million	2004	2003
Cash paid	—	(3)
Cash and bank balances acquired	—	138
Net inflow of cash and cash equivalents in respect of the acquisition of subsidiaries	—	135

The subsidiaries acquired in the prior year contributed approximately HK$1,866 million to the Group's consolidated turnover and approximately HK$97 million to the consolidated profits after tax before minority interests for the year ended 31 December 2003.

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32. NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT *(Cont'd)*

(c) Disposal of subsidiaries

HK$ million	2004	2003
Net assets disposed of:		
Fixed assets	35	—
Inventories	5	—
Trade receivables	50	—
Cash and bank balances	36	—
Trade payables	(29)	—
Other payables and accruals	(7)	—
Tax payables	(1)	—
	89	—
Reversal of goodwill upon disposal of subsidiaries	30	—
Gain on disposal of subsidiaries	20	—
	139	—
Satisfied by:		
Cancellation of convertible notes — note 27(d)	139	—

An analysis of the net outflow of cash and cash equivalents in respect of the disposal of subsidiaries is as follows:

HK$ million	2004	2003
Cash and bank balances disposed of	(36)	—
Net outflow of cash and cash equivalents in respect of the disposal of subsidiaries	(36)	—

The subsidiaries disposed of during the year contributed approximately HK$7 million (2003: HK$60 million) to the Group's consolidated turnover and approximately HK$10 million (2003: HK$12 million) to the consolidated profits after tax before minority interest for the year ended 31 December 2004.

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33. CONTINGENT LIABILITIES

(a) At the balance sheet date, contingent liabilities not provided for in the financial statements were as follows:

	Group		Company	
HK$ million	**2004**	2003	**2004**	2003
Corporate guarantees given to banks in connection with facilities granted to subsidiaries	**—**	—	**426**	346

As at 31 December 2004, the banking facilities granted to the subsidiaries subject to guarantees given to the banks by the Company were utilised to the extent of approximately HK$223 million (2003: HK$183 million).

(b) The Group had a contingent liability in respect of possible future long service payments to employees under the Hong Kong Employment Ordinance, with a maximum possible amount of HK$6 million as at 31 December 2004 (2003: HK$5 million), as further explained under the heading "Employee benefits" in note 3 to the financial statements. The contingent liability has arisen because at the balance sheet date a number of current employees have achieved the required number of years of service to the Group in order to be eligible for long service payments under the Employment Ordinance if their employment is terminated under certain circumstances. A provision has not been recognised in respect of such possible payments, as it is not considered probable that the situation will result in a material future outflow of resources from the Group.

34. PLEDGE OF ASSETS

At 31 December 2004, the Group's bank borrowings were secured by the pledge of the Group's fixed deposits amounting to approximately HK$95 million (2003: HK$100 million).

35. OPERATING LEASE ARRANGEMENTS

The Group leases certain of its office premises under operating lease arrangements, with leases negotiated for terms ranging from one to three years.

At 31 December 2004, the Group had total future minimum lease payments under non-cancellable operating leases in respect of office premises falling due as follows:

HK$ million	**2004**	2003
Within one year	**5**	4
In the second to fifth years, inclusive	**2**	2
	7	6

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36. COMMITMENTS

In addition to the operating lease commitments detailed in note 35 above, the Group had the following capital commitments at the balance sheet date:

	Group	
HK$ million	2004	2003
Contracted, but not provided for		
Construction in progress	15	—
Purchase of plant, machinery and equipment	1	2
Purchase of a motor vehicle	4	—
	20	2

37. RELATED PARTY TRANSACTIONS

(1) On 2 June 2004, the Company and CCT Telecom entered into a conditional agreement pursuant to which the Company agreed (i) to dispose of its entire interest in First Precision and CCT Investment to CCT Telecom; and (ii) to assign the interest-free shareholders' loans owed by First Precision and CCT Investment to CCT Telecom as at the completion date of this transaction, at a total consideration of HK$139 million. The consideration was satisfied by cancellation of the convertible note in the same amount which was issued by the Company to an indirect wholly-owned subsidiary of CCT Telecom on 30 June 2003.

The transaction was approved by the independent shareholders of the Company in a special general meeting held on 8 September 2004 and was completed on 13 September 2004. Further details of the transaction are set out in the circular of the Company dated 20 August 2004.

(2) During the two years ended 31 December 2004, the Company and certain of its indirect wholly-owned subsidiaries had the following material transactions with CCT Telecom and certain of its subsidiaries:

2004	Period	Notes	HK$ million
Purchase of plastic casings and	1 January 2004 to 14 June 2004	(i)	147
components	15 June 2004 to 31 December 2004	(i)	166
Purchase of materials	1 January 2004 to 14 June 2004	(ii)	13
Factory rental income	1 January 2004 to 31 December 2004	(iii)	6
Office rental expenses	1 January 2004 to 31 December 2004	(iv)	3
Management information system service fee	1 January 2004 to 31 December 2004	(v)	3

31 December 2004

37. RELATED PARTY TRANSACTIONS *(Cont'd)*

(2) *(Cont'd)*

2003	Notes	Year ended 31 December 2003 HK$ million
Purchase of plastic casings and components	(i)	132
Purchase of materials	(ii)	24
Factory rental income	(iii)	3
Office rental expenses	(iv)	2
Management information system service fee	(v)	1

Notes:

(i) The plastic casings and components were purchased by CCT Telecom (HK) Limited ("CCT HK"), an indirect wholly-owned subsidiary of the Company, from Neptune, in accordance with the terms and conditions set out in a manufacturing agreement (the "First Manufacturing Agreement") entered into between CCT HK and Neptune on 15 May 2003. During the year, CCT HK and Neptune agreed to early terminate the First Manufacturing Agreement and on 4 May 2004, the Company and CCT Telecom entered into a new manufacturing agreement (the "Second Manufacturing Agreement") pursuant to which CCT Telecom Group agreed to manufacture certain plastic casings and components and toolings for telecom products and accessories and other products for the Group. The Second Manufacturing Agreement became effective on 15 June 2004.

The purchase prices under both agreements were determined based on the direct material costs plus a mark-up of no more than 300%.

(ii) The purchase of materials was made by ESL from Neptune. The purchase prices were determined based on the direct costs of the materials plus a mark-up of up to 50% of such direct costs in accordance with the terms and conditions set out in a manufacturing agreement (the "Third Manufacturing Agreement") entered into between Neptune and ESL on 23 July 2002. During the year, both parties agreed to early terminate the Third Manufacturing Agreement and on 4 May 2004, the Company and CCT Telecom entered into the Second Manufacturing Agreement, details are set out in paragraph (i) above.

(iii) The factory rental income was charged to Shine Best Developments Limited ("Shine Best"), an indirect wholly-owned subsidiary of CCT Telecom, by CCT Enterprise Limited ("CCT Ent"), an indirect wholly-owned subsidiary of the Company, for the provision of factory space in Huiyang, the PRC, at a rate determined in accordance with the terms and conditions set out in a tenancy agreement (the "Huiyang Tenancy Agreement") entered into between Shine Best and CCT Ent on 15 May 2003.

(iv) The office rental expenses were charged to CCT HK and CCT Telecom R&D Limited ("CCT R&D"), indirect wholly-owned subsidiaries of the Company, by Goldbay Investments Limited ("Goldbay"), an indirect wholly-owned subsidiary of CCT Telecom, for the provision of office spaces in Hong Kong, at a rate determined in accordance with the terms and conditions set out in three tenancy agreements (the "Hong Kong Tenancy Agreements") entered into between CCT HK and Goldbay on 15 September 2003 and 17 September 2004, and between CCT R&D and Goldbay on 23 December 2003, respectively.

(v) The management information system service fee was charged to CCT Telecom by CCT HK for the provision of general management information system support, network and software consultation and hardware maintenance services. The rate was determined in accordance with the terms and conditions set out in an agreement (the "MIS Agreement") entered into between CCT Telecom and CCT HK on 15 May 2003.

31 December 2004

37. RELATED PARTY TRANSACTIONS *(Cont'd)*

(3) ESL and CCT Investment had been the indirect wholly-owned subsidiaries of the Company throughout the period up to 12 September 2004, the date on which these two subsidiaries were disposed of to CCT Telecom.

Before the completion of the disposal of ESL and CCT Investment on 13 September 2004, ESL and CCT Investment had the following connected transactions with certain subsidiaries of CCT Telecom up to 12 September 2004:

	Notes	Period from 1 January 2004 to 12 September 2004 HK$ million	Year ended 31 December 2003 HK$ million
Factory rental expenses	(i)	4	1
Rental expenses	(ii)	1	2

Notes:

(i) The factory rental expenses were charged to CCT Investment, by CCT Properties (Dongguan) Limited ("CCT Prop"), an indirect wholly-owned subsidiary of CCT Telecom, for the provision of factory space in Dongguan, the PRC, at a rate determined in accordance with the terms and conditions set out in a tenancy agreement (the "First Tenancy Agreement") entered into between CCT Investment and CCT Prop on 15 May 2003. Both parties agreed to have an early termination of the First Tenancy Agreement in accordance with the provisions of the First Tenancy Agreement and entered into a new tenancy agreement with a greater floor area on 14 January 2004.

(ii) The rental expenses were charged to ESL by CCT Prop for the provision of factory space in Dongguan, the PRC, at a rate determined in accordance with the terms and conditions set out in a rental agreement (the "Second Tenancy Agreement") entered into between ESL and CCT Prop on 15 April 2003. Both parties agreed to have an early termination of the Second Tenancy Agreement in accordance the provisions of the Second Tenancy Agreement and enter into a new tenancy agreement with a smaller floor area on 14 January 2004.

(4) The following ongoing connected transactions were conducted between the Company and CCT Telecom for the period from 13 September 2004 to 31 December 2004:

	Notes	Period from 13 September 2004 to 31 December 2004 HK$ million
Factory rental expenses	(i)	2
Purchases of products	(ii)	47

Notes:

(i) The factory rental expenses were charged to the Company by CCT Telecom for the provision of factory space in Dongguan, the PRC, at a rate determined in accordance with the terms and conditions as set out in a tenancy agreement (the "New Tenancy Agreement") entered into between the Company and CCT Telecom on 13 September 2004.

(ii) The purchase prices were determined based on the direct material costs of the products plus a mark-up of up to 100% of such direct material costs pursuant to a power supply components manufacturing agreement entered into between the Company and CCT Telecom on 2 June 2004.

(5) During the year, the Company paid interest expense amounting to approximately HK$51 million (2003: HK$27 million) to CCT Telecom in respect of the convertible notes issued by the Company to CCT Telecom in 2003.

31 December 2004

38. POST BALANCE SHEET EVENT

On 31 January 2005, the Company and CCT Telecom jointly announced that a voluntary conditional cash offer with a securities exchange alternative will be made by the Offeror to the shareholders of the Company and the holder of the 2005 Convertible Note to acquire all the issued shares of the Company and the 2005 Convertible Note, and to make a voluntary conditional cash offer to the option holders of the Company to cancel all outstanding share options of the Company (collectively the "Offers"). The Offers will be made on the basis of HK$1,840 in cash for every 80,000 shares of the Company or for every 2005 Convertible Note with a face value of HK$800 with securities exchange alternative of zero coupon five-year convertible bond with a face value of HK$1,840 to be issued by CCT Telecom, and HK$0.009 for every outstanding share option of the Company. The Offers have become unconditional on 21 April 2005.

Further details of this transaction are set out in the Company's press announcement dated 31 January 2005, a composite offer and response document dated 31 March 2005 and the press announcement dated 21 April 2005.

39. APPROVAL OF THE FINANCIAL STATEMENTS

The financial statements were approved and authorised for issue by the board of directors on 25 April 2005.