

## CHAIRMAN'S STATEMENT

On behalf of the board of directors (the "Board") of Artel Solutions Group Holdings Limited (the "Company" or "Artel"), I am pleased to present the annual report of the Company and its subsidiaries (the "Group") for the year ended 31 December 2004.

### THE VISION OF ARTEL GROUP

Artel is committed to serve the genuine need for computing, multimedia, and networking solutions in the high-tech community. We are dedicated to providing cutting edge solutions – complete, concise, and always current with reliable services. We commit to help our customers reach their business goals. With this positive attitude, we invest a great deal of effort in cultivating the new sales channels in 2004. We now have solid personal computer ("PC") do it yourself ("DIY") channel, original equipment manufacturer ("OEM") channel, consumer electronic ("CE") channel, I-Café channel, value added reseller ("VAR") networking channel and online channel to boost our growth for the year 2005.

### THE VALUES OF ARTEL GROUP

Artel's core values are integrity, customer satisfaction, supply chain partnership and dedication to excellence. These values motivate our employees and management team. Also, we incorporate them in evaluating our operations, our planning, our decision making and our vision for the future.

### BUSINESS REVIEW

2004 was a challenging year for the Group to expand our marketing scope from a hardware distributor to a high tech solution provider. At the beginning of the year, we targeted to cultivate new channels for increasing our gross profit margin. The Group's gross profit margin increased from 4% to 5% mainly lifted by the 22% gross profit of our integrated e-enabling solutions as approximately HK\$21.9 million and 12% gross profit of our thin film transistor liquid crystal display ("LCD") group as approximately HK\$28.6 million. After diversifying our product line to fulfill the new channel's needs, the major source of income is composed of 74% Intel Semiconductor Limited ("Intel") central processing unit ("CPU") and chipset products, 6% e-enabling network solutions, 13% LCD products and 7% Intel motherboard. Because we developed new channel, it caused an impact of approximately HK\$488 million drop in revenue for Intel CPU business alone. Further, we discontinued several slow moving networking specialty items from our 2003 product line, which brought about the rest of the approximately HK\$56 million drop in revenue. For the year 2004, the Group achieved a turnover of approximately HK\$1,659 million, against approximately HK\$2,203 million recorded last year. The net profit after tax was approximately HK\$33.2 million, as compared with approximately HK\$50.3 million in 2003. The Group was able to maintain the net profit margin, with only a slight change from 2.3% to 2.0% in 2004. Nevertheless, we had significant revenue increases in certain categories year over year. Motherboard revenue increased 15%, e-enabling solutions was up 22% and LCD products was up 25%. The most exciting accomplishment in 2004 was the revenue of approximately HK\$38 million of design-in LCD panel to our OEM customers and approximately HK\$25 million of design-in television ("TV") panel to Chinese TV factories. These improvements make all the hard work in channel development worthwhile.

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The highlight of 2004 for Artel was winning over 40% market share in the People Republic of China ("PRC") as the No.1 Intel Box motherboard based on our efficient channel management and customer satisfaction. Also, we successfully entered the CE & OEM market by carrying LCD TV and monitor Panel. We have developed over 60 OEM customers in the PRC. Lastly, We have established 14 LCD monitor and service centers in the PRC.

### PROSPECTS

#### **Market trend**

Multimedia Internet through wireless and mobility access is a global trend. According to PC magazine 12.1. 2005 edition, the PRC is about to become a huge player in flat-screen TVs, cell phones, and more. They will continue to steamroll the competition in CE since the country has already taken over the manufacture of digital vasatile disc ("DVD") players and tube TVs. The global demand of LCD monitor in 2004 was approximately 69 million units. The forecast growth for 2005 is approximately 97 million units, 2006 is approximately 117 million units, 2007 is approximately 128 million units, and 2008 is approximately 143 million units. The global demand of LCD TV in 2004 was approximately 9 million units. The forecast growth for 2005 is approximately 16 million units, 2006 is approximately 27 million units, and 2007 is approximately 34 million units. The Group foresees a strong economic growth in the PRC and is keen to identify business opportunities to grow in this market. In the long run, we will benefit from the synergy that will be generated from the combination of the vertical and horizontal segments. Both Digital Home Solution and Digital Enterprise Solution that Intel is promoting are portals for us to penetrate into the huge PRC market. It is expected that these new concepts will be able to fortify our market share in distribution of computer components, and will provide Artel with a new direction to enlarge our solutions business.

#### **Major products development**

##### *Distribution business*

Distribution of Intel products:

- Principal products include CPU, motherboard, wireless and networking products.
- Major market segments include DIY channel and PC retailers.

Distribution of LCD products:

- Principal products include various sizes of monitor and TV.
- Major market segments include PC retailers and CE retailers.

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### *Solution business*

#### Solution for CE & OEM Makers:

- Principal products include chipset, IC (Integrated Circuit) or board level products, monitor panel, and TV panel.
- Major market segments include LCD monitor maker, LCD TV maker, DVD maker, and motherboard maker.

Solution for Digital Home: The concept of 5C value = Control + Convenience + Community + Customization + Content to link digital home appliances and PC with Internet accessibility.

- Principal products include CPU, motherboard, TV tuner, PVR (Personal Digital Video Recorder), DMA (Digital Media Adapter), TV encoder for desktop or notebook to link with TV, media center with remote control features, and digital TV related products.
- Major market segments include VAR and SI (System Integrator).

Solution for Digital Enterprise: e-enabling solution provides mobility to users through wireless device for Internet access anywhere and anytime.

- Principal products include CPU, motherboard, monitor, various networking devices such as PRO/wireless network connection, mobile adapter and other connectivity products.
- Major market segments include institutions such as government, education, healthcare, finance, telecommunication and business enterprise.

#### Solution for customer service:

- Principal products include after sales services such as repair, exchange and technical support for monitors.
- Major geographical market segments include Beijing, Shanghai, Shenzhen, Guangzhou, Chengdu, Chongqing, Xian, Kunming, Wuhan, Nanjing, Guiyang, Fuzhou, Hangzhou, Zhengzhou, Shenyang, Haerbin, and Urumqi. We plan to expand our service centers into a nationwide consumer electronic service system.

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### **Adjusting to the multimedia Internet world**

The Internet is a global web of networks to connect people to business and people. It becomes a common communication channel as telephone and even more sophisticated. The stream line video, MP3 (MPEG Layer 3) music, X-box games, VoIP (Voice Over Internet Protocol), and other forms of visual, audio, text, graphic information reach every corner of the world through the giant Internet highway. The number of Internet users is continuously growing in a rapid speed. This provides a booming opportunity for Artel to expand our business in the high-tech community.

In conclusion, the Group will seize the golden opportunity offer by booming Internet and the PRC economic growth. In the vertical segment of PC channel, we will continue to grow in CPU and LCD monitor products, which account for one-third of the cost of a PC's costing. In the horizontal segment of the high tech industry, we will set foot in the OEM market, multimedia CE market and the e-enabling solutions market. With the products for distribution and solutions, we believe the Group will continue to grow with the PRC market.

### **ACKNOWLEDGEMENT**

On behalf of the Board, I would like to take this opportunity to extend my gratitude to all my fellow directors and staff for their valuable dedication and commitment. I would also like to express my sincere thanks to our business partners and shareholders for their supports in the past years.

**Yu Pen Hung**

*Chairman*

Hong Kong, 22 April 2005