

# Management Discussion and Analysis

## MANAGEMENT DISCUSSION AND ANALYSIS

### Results

The Group's financial performance for the year ended 30 June 2005 recorded a steady upward growth with a double-digit increase in turnover. During the year under review, turnover of the Group amounted to RMB369,787,000 (2004: RMB301,255,000), representing an increase of approximately 22.7% as compared to the corresponding period last year. The Group managed to achieve satisfactory results during the year primarily due to the global economic recovery, and the incessant growth in market demand for consumer electronic products which stimulated the overall strong demand for electronic products parts and accessories. This greatly benefited the Group as a PCB manufacturer. In addition, the Group installed technologically-advanced production facilities and leased a new manufacturing plant during the year, so as to expand its scope of operations and attain even greater economies of scale.

The gross profit for the year under review reached approximately RMB147,004,000 as compared to approximately RMB136,349,000 for previous year. The gross profit margin was decreased due to the increase in raw material prices and the incurrence of pre-operation expenses resulting from the commencement of trial production of the two subsidiaries. Operating profit and profit attributable to shareholders were RMB112,289,000 (2004: RMB107,716,000) and RMB80,427,000 (2004: RMB81,214,000) respectively, representing an increase and a decrease of approximately 4.2% and 1.0% respectively as compared to the corresponding period last year. The decrease in profit attributable to shareholders was mainly due to the expiry of tax holiday of a subsidiary. Earnings per share was RMB17 cents (2004: RMB19 cents).

### Business Review

Financial year 2005 was an important milestone for the Group. Apart from the conventional PCB production operations, the Group successfully moved downstream into PCB Assembly (PCBA) services when it set up a new manufacturing plant in Fuzhou Mawei Economic and Technical Development Zone. In addition, the Group acquired a new manufacturing plant specializing in the production of flexible PCBs in Huizhou City, Guangdong Province, and this manufacturing plant commenced full-scale operation in early 2005. These new products not only contributed to the Group's income, but also further fortified the Group's market position as a one-stop EMS solution provider, allowing the Group to provide an even more comprehensive scope of EMS solution to its clients and further strengthening the Group's competitive edge in the market.

### Segmental Information

Segment information is presented in respect of the Group's business and geographical segments. Business segment information is chosen as the primary reporting format because this is more relevant to the Group in making operating and financial decisions.

Throughout the years ended 30 June 2005 and 2004, the Group has been primarily operating in the manufacturing and sale of printed circuit boards.

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Geographically, sales within the PRC (excluding Hong Kong and Taiwan) remained the largest segment in which approximately 83.0% (2004: 83.2%) of the Group's turnover was generated, while approximately 10.6% (2004: 10.5%) was attributable to the sales to Australia for the year under review. The balance of approximately 6.4% of the Group's turnover (2004: 6.3%) was taken up by the US, Germany, Hong Kong, Taiwan and other countries.

Key products manufactured by the Group during the year under review were single and double-sided PCBs, multilayer PCBs as well as flexible PCBs, and the Group also provided PCBA services. Details of the individual products are as follows:

### *Single and Double-sided PCBs*

During the year under review, the sales of single and double-sided PCBs amounted to approximately RMB159,684,000 (2004: RMB120,984,000), representing approximately 43.2% of the Group's total turnover. Operating profit contributed by this business segment was approximately RMB48,447,000 (2004: RMB43,259,000), up approximately 12.0% as compared with that of the preceding year.

### *Multilayer PCBs*

Total sales of multilayer PCBs was approximately RMB198,030,000 (2004: RMB180,271,000), which made up approximately 53.6% of the Group's total turnover during the year under review. Operating profit reached approximately RMB82,909,000 (2004: RMB64,457,000), an approximate increase of 28.6% as compared to the preceding year.

### *Flexible PCBs and PCBA*

To maintain an advantageous position in the competitive PCB industry, the Group has always been dedicated to the development of new innovative PCB products, including flexible PCBs for which full-scale manufacturing commenced operation in January 2005. Given that flexible PCBs yield higher profits as compared to conventional PCBs, this business segment will boost the overall profit level significantly. The Group kick started the PCBA services in September 2004 as it aimed to provide an even more comprehensive scope of EMS solution to its clients and fortify its market position as a one-stop EMS solution provider. Turnover contributed by flexible PCBs and PCBA amounted to approximately RMB12,073,000 (2004: Nil), accounting for approximately 3.2% of the Group's total sales, and associated operating loss was approximately RMB19,067,000 (2004: Nil).

## Manufacturing Facilities

Well-equipped manufacturing facilities and sizeable production capacity are key factors to success for an EMS solution provider. The Group therefore devoted resources to constructing new manufacturing plants and installing technologically-advanced production facilities and system, so as to cater to the rapidly increasing demands of the PCB industry.

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In early 2004, the Group acquired a new manufacturing plant in Xiangshui River Industrial Area, Daya Bay, Huizhou City, Guangdong Province (廣東省惠州市大亞灣經濟技術開發區(國家級)響河工業園) (“Huizhou Plant”) which specializes in the production of flexible PCBs and thick copper PCBs. Phase one production of flexible PCBs commenced in January 2005, and the currently production capacity is 10,000 square meters per month. The Huizhou Plant has been accredited with US-based UL Corporation’s product certification as well as Switzerland-based SGS Corporation’s ISO9001 quality system certification. Presently, some of the clients include renowned multinational corporations such as Samsung Electro-Mechanics and Sankyo Seiki.

Apart from the Huizhou Plant, the Group also leased a manufacturing plant in Fuzhou Mawei Economic and Technical Development Zone (“Mawei Plant”) to operate the PCBA services. The Mawei Plant has been accredited with ISO9001:2000 quality management system certification and it began full-scale operation in September 2004. Now the plant is outfitted with four automatic Surface-Mount Technology (SMT) production lines and two MI lines to provide a series of ancillary solution including the design of sub-system, production of prototype samples, low-volume production and testing services.

The existing production base in Fuqing City in Fujian Province is equipped with the conventional PCB (including single-sided PCBs, double-sided PCBs and multilayer PCBs) production facilities. This manufacturing plant had been accredited with the ISO/TS16949, ISO9001, ISO14001 and OHSAS 18001 certifications, and its current client portfolio include many multinational corporations such as TPV Technology, Australia-based Telstra and NEC Tokin Electronics. As at 30 June 2005, monthly production capacity was approximately 40,000 square meters and the average monthly utilization rate reached approximately 75% for the year under review.

### Research and Development

The Group is committed to continual research and development to develop competitive and high quality products, which in turn secures the leading market position of the Group in the EMS and PCB industries. The 4 product development engineers and designers employed in Shanghai and Shenzhen work closely with the clients before, during and after the production process, so as to provide the best products and services in accordance to the clients’ requirements.

### Disposal of Floret Industries Limited

Floret Industries Limited (“Floret Industries”) and its subsidiaries are principally engaged in the research, development, manufacture and sales of products as well as the provision of ancillary services in relation to the automation and intellectualization of electric supply systems. In order to further develop and enhance the Group’s production capability, the Group’s strategy has undergone gradual adjustment from high mix production to medium to large volume production of ancillaries for major customers. The development and expansion of its core business of the provision of electronic manufacturing services and the manufacturing and trading of printed circuit board will be the focus of operations for the coming years. Therefore, the major resources of the Group will also be allocated to the expansion and development of its core business.

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## FUTURE PROSPECT

Robust global market demand for electronic products and the rapid development of electronic communication industry combine to fuel the demand for PCB products. BPA Consulting Ltd estimates that the global PCB market will jump from US\$30.1 billion to US\$43.8 billion by year 2007, with China growing at the fastest rate amongst the PCB producing countries, with a compounded annual growth rate of 17.4%.

In addition, the wave of outsourcing of EMS by multinational electronics conglomerates, following China's accession to World Trade Organization, has led to the prediction that total income of EMS solution providers worldwide will grow at a compounded annual rate of 10.2% from US\$89 billion in year 2002 to US\$400 billion in year 2007. According to estimates by International Data Corporation, the market will continue to outsource parts of the production process to low-cost countries especially China. The market predicts that the EMS industry in China will grow at a compounded annual rate of 29.7% from year 2002 to 2007, and it will account for 38% of the global EMS industry by year 2007.

Riding on this positive business environment, the Group will seize the opportunity to reinforce its existing PCB operations, as well as to seek strategic acquisition opportunities to develop upstream and downstream businesses, broaden its scope of services and provide a wide range of value-added services to its clients. This will further fortify the Group's position as a one-stop EMS solution provider.

In the coming two years, the Group plans to install more production lines in the Huizhou Plant and Mawei Plant to cater to the expected growth in market demand. Phase two installation in the Huizhou Plant will begin in mid 2006, with the aim of boosting the monthly production capacity to 15,000 square meters. In addition, the Group will commence production of thick copper PCBs in the Huizhou Plant in early 2007, and the total monthly production capacity is expected to reach 20,000 square meters. As for the Mawei Plant, the Group plans to install 16 SMT production lines, 4 MI lines and 2 finished products assembly lines by the end of 2006.

Leveraging on the current optimism in the EMS and PCB industries, together with the Group's technical expertise and experience, the management strongly believes that the Group will again achieve record financial results in the next financial year, delivering ample returns for its shareholders.

## Liquidity and Financial Resources and Capital Structure

For the year ended 30 June 2005, the Group's working capital requirement was principally financed by its internal resources and banking facilities.

As at 30 June 2005, the Group had cash and cash equivalents, net current assets and total assets less current liabilities of RMB540,915,000 (2004: RMB314,027,000), RMB519,729,000 (2004: RMB348,934,000) and RMB727,939,000 (2004: RMB598,355,000) respectively.

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As at 30 June 2005, the Group had total borrowings (excluding obligations under finance leases) of RMB213,019,000 (2004: RMB128,176,000), comparing utilised bank loan facilities of RMB143,791,000 (2004: RMB128,176,000) from several banks and convertible bonds of RMB69,228,000 (2004: Nil), of the total utilised bank loans of RMB110,657,000 (2004: RMB70,300,000) for short term and the remainder of RMB33,134,000 (2004: RMB57,876,000) for long term. Included in these short term loans of RMB81,415,000 and RMB4,500,000 were secured by corporate guarantees given by the Company and pledge bank deposit respectively. The remaining balance of the short term loan of RMB24,742,000 and the long term loan of RMB33,134,000 were unsecured. Besides, the Group had available RMB8,385,000 (2004: Nil) of undrawn committed borrowing facilities in respect of which all conditions precedent had been met and had obligations under finance leases of RMB12,982,000 (2004: Nil) denominated in Hong Kong Dollars. The total borrowings were mainly for business expansion, capital expenditure and working capital purposes. The Group's short term and long term borrowings were mainly denominated in Renminbi and US Dollars. Loan facilities were granted to the Group at the normal market interest rates.

The shareholders' equity of the Group as at 30 June 2005 increased by RMB90,374,000 to RMB596,646,000 (2004: RMB506,272,000). The gearing ratio (calculated as the ratio of current liabilities plus non-current liabilities: shareholders' equity) of the Group as at 30 June 2005 was approximately 0.56 (2004: 0.37).

Saved as disclosed elsewhere on the Management Discussion and Analysis, there is no changes in the Company's share capital.

### Significant Investments

Saved as disclosed elsewhere on the Management Discussion and Analysis, the Group had no other significant investment held.

### Acquisition and disposal of Subsidiaries and Associated Companies

On 27 May 2005, the Group entered into a sale and purchase agreement with an independent third party in relation to the disposal of 49 shares of Floret Industries held by the Group ("the Disposal"), representing 49% of the issued share capital of Floret Industries, at a consideration of RMB52.0 million (equivalent to approximately HK\$49,000,000), which was wholly satisfied in cash at completion.

During the period from 1 July 2004 to 27 May 2005, the associates of the Group made a profit contribution of approximately RMB6,655,000 to the Group. Following the completion of the Disposal, a loss of approximately RMB5,065,000 was recognised by the Group for the year ended 30 June 2005. The loss was calculated based on the difference between the consideration of the Disposal and the unaudited carrying amount of interest in Floret Industries of approximately RMB57,065,000 in the Group's accounts as at 27 May 2005.

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During the year ended 30 June 2005, Fujian Fuqiang Delicate Circuit Plate Co Ltd., the Company's subsidiary, completed the increase in its registered capital by RMB46 million to RMB92 million, the increased registered capital was wholly contributed by the Group.

Saved as disclosed elsewhere on the Management Discussion and Analysis, the Group had no material acquisition and disposals of subsidiaries and affiliated companies.

### Employment Information

As at 30 June 2005, the Group employed a total of 1,200 (2004: 648) employees. It is a policy of the Group to review its employee's pay levels and performance bonus system regularly to ensure that the remuneration policy is competitive within the relevant industry. During the year ended 30 June 2005, the employment cost (including directors' emoluments) amounted to RMB17,823,000. In order to align the interests of staffs, directors and consultants with the Group, share options were granted to staffs, directors and consultants under the Company's 2003 share options schemes ("2003 Scheme"). Shares options granted to staffs, directors and consultants which remained outstanding as at 30 June 2005 aggregated 32,000,000 shares options.

### Charge on Assets

As at 30 June 2005, a fixed deposit of HK\$5,000,000 (equivalent to approximately RMB5,329,000) (2004: RMB5,329,000) was pledged to a bank for bank loan of RMB4,500,000 granted to the Group.

Save as disclosed elsewhere on the Management Discussion and Analysis, the Group had no charge of assets.

### Future Plans for Material Investments and Expected Sources of Funding

Save as disclosed elsewhere on the Management Discussion and Analysis, as at 30 June 2005, the Group had no future plans for material investments.

The management will continue to monitor the industry and review its business expansion plans regularly, so as to take necessary measures in the Group's best interests.

### Exposure to Fluctuations in Exchange Rates

During the year ended 30 June 2005, the Group experiences only immaterial exchange rate fluctuations as most of the Group's monetary assets and liabilities are denominated in Hong Kong Dollars, US Dollars and Renminbi, and the Group conducted its business transactions principally in Hong Kong Dollars, US Dollars and Renminbi, all of which were relatively stable during the year under review. The Group considered that as the exchange rate risks of the Group is considered to be minimal, the Group did not employ any financial instruments for hedging purposes.

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### Capital Commitment

As at 30 June 2005, in respect of acquisition of fixed assets, the Group only had outstanding capital commitment contracted for but not provided in the financial statements amounted to approximately RMB15,638,000.

### Contingent Liabilities

As at 30 June 2005, the Group did not have any material contingent liabilities.

### Use of Share Issue Proceeds

The Group had applied the net proceeds from the top-up placement in January 2004, net of the related expenses, amounted to approximately HK\$77 million as follows:

1. Approximately RMB79.5 million (equivalent to approximately HK\$75.0 million) had been utilised for future developing the Group's printed circuit board fabrication capacity; and
2. Approximately RMB2.1 million (equivalent to approximately HK\$2.0 million) has been utilised for general working capital.