

Chairmen's Statement



Dr Chang Chu Cheng
Chairman

Mr Ko Chun Shun, Johnson
Chairman

Results Highlights:

- Underlying business in 2005 performed better than that of 2004
- The Group made strategic decisions to pave the way for future development, which led to certain non-cash, non-recurring impairment losses and provisions
- Net cash from operating activities: HK\$243 million (2004: HK\$133 million)
- Full-year dividend per share: 38 HK cents (2004: 38 HK cents)

Results

On behalf of Varitronix International Limited and its subsidiaries ("Varitronix" or the "Group"), we are pleased to present the Group's annual audited results for the year ended 31 December 2005.

Varitronix made solid progress in 2005. The Group introduced new management with the vision of ensuring long-term sustainable success. During the year under review, management reviewed the structure of the organisation and initiated certain reorganisation measures, aiming to enhance the Group's overall competitiveness in the coming years.

The management team has made a number of strategic decisions, such as moving operations from Hong Kong and Malaysia to the PRC, which has led to certain non-recurring impairment provisions. During the year under review, the Group relocated the production facilities in Tseung Kwan O ("TKO"), Hong Kong to the PRC. The Group also moved its principal place of business in Hong Kong from the TKO property to the Kwun Tong property. In order to reflect the fair value of the TKO property, the Group appointed an independent property valuer to value the TKO property. The revaluation led to an impairment loss of HK\$46 million.

After reviewing the operational efficiency and productivity of its Malaysian plant, which had recorded losses for years, the Group concluded that the plant lacked the economies of scale needed to stay competitive in the current market environment and that it was in the interest of the Group to move the Malaysian production to the PRC. The relocation resulted in, among others, impairment losses of fixed assets and goodwill amounting to HK\$32 million and HK\$28 million, respectively.

In addition, management has critically reviewed investments held and where impairment indications are evident has made additional non-recurring provisions to reduce the carrying amounts to the recoverable values.

The intangible asset value of HK\$25 million relating to a technology licensing agreement was written off, as mentioned in an announcement dated 14 March 2006.

As mentioned in an announcement dated 9 June 2005, the Group has explored different alternatives to enter the Organic Light Emitting Diode ("OLED") market. Management was of the view that Ness Display's experience and production capability for OLED offered the Group a quick entrance to the market and decided to invest into Ness Display, a Korean-based OLED producer. As at today, management's view remains unchanged.

Nevertheless, market conditions for OLED have become uncertain, despite the advantages over other display technologies. That lengthened the expected payback period of the Group's investment in the OLED business. As a result, the Group has taken a more prudent accounting approach.

The Group also addressed long-standing taxation issues. It had received from the Inland Revenue Department of Hong Kong additional assessments relating to a dispute over the deductibility of certain subcontracting fees for tax assessment purposes. In this regard, the Group made additional provisions as advised by its tax advisers.

These measures have cleared the way for future development. Looking forward, we expect the Group to grow on a more solid foundation.

The underlying business performance in 2005 surpassed that in the previous year. The Group recorded strong net cash from operating activities of HK\$243 million (2004: HK\$133 million) although the Group's turnover of HK\$1,980 million was similar to last year's HK\$2,006 million. However, impairment losses, write-offs and provisions, resulted in substantial charges to the Consolidated Income Statement. Loss attributable to equity shareholders of the Company was \$179 million for 2005 (2004: Profit of HK\$193 million). As the majority of the aforesaid charges were non-cash in nature, the Group maintained strong balances of liquid assets. Liquid funds, net of bank loans and overdrafts, amounted to HK\$696 million (2004: HK\$722 million).

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Review

Business Development

Varitronix recorded satisfactory development in the European automotive market in 2005, with its LCD products achieving greater market penetration. The Group also successfully gained market share in the United States and Korea during the year under review.

The Group's products are now widely used in industrial, medical and military equipment and facilities, home electrical appliances and portable entertainment products. The Group continues to broaden its geographical presence with encouraging business growth in the Asian region. Moreover, the Group has strengthened its market position in automotive products in Korea, and is developing business in other Korean electrical and electronic goods sectors.

As a result of rampant illegal activities of "black handset" manufacturers, our customers in the PRC who are licensed mobile phone manufacturers suffered a decline in sales. Since late 2005, the Chinese government has taken decisive measures to constrain the prevalence of these illegal activities in the market. Sales for licensed mobile phones manufacturers are expected to recover in 2006.

Varitronix is confident of capitalising on the opportunities presented by colour LCD applications in the mobile phone sector in the PRC. Apart from fostering a good relationship with handset design companies, the Group announced an acquisition of interest in Varitronix Pengyuan Limited, a joint venture between Varitronix and Tsing Hua University, resulting in an increase of Varitronix's interest in the joint venture to 90% from the previous 51%. This move will not only enable the Group to enjoy a bigger share of future profit contributions from Varitronix Pengyuan Limited, but will also allow the Group to actively pursue business opportunities in the Chinese telecommunications sector.

Colour STN Line Upgrade

In order to meet the growing demand for colour LCD solutions, the Group upgraded the fully automated production facilities in its Heyuan plant, which increased the production capacity for Colour STN LCD (Colour Supertwisted Nematic Liquid Crystal Display).

Technological Development

In line with its strategy to diversify its scope of technologies, Varitronix invested in Ness Display, which provides the Group with access to the advanced know-how of OLED technology.

In the year under review, the Group also committed to commercialising BCD (Bistable Cholesteric Displays) and ZBD (Zenithal Bistable Displays) technologies. BCD and ZBD consume very low power and have a wide range of potential applications. BCD products have commenced mass production, and have been applied to portable products available at the retail level. ZBD technology has also achieved a breakthrough. The Group is working to apply this technology to shelf labels in supermarket chains in the United Kingdom.

Future Development Strategy

Confident Market Expansion

The Group will strive to increase its market share and has set the following targets for 2006:

- To maintain a strong position in small-volume, high margin business
- To continue to expand in high-volume, short-cycle business
- To strengthen market presence and sales force in growth markets: the PRC, Korea, the United States and Europe
- To reorganise the sales network and direct more resources to the sales network; to continue to improve services and add value to customers

Improvement of Product Mix

Colour displays are setting the trend for the future. We believe that more colour displays will be adapted to a greater variety of end-products to enhance the appeal of those products to customers. The Group will capture this rising demand to further expand its business in the colour display sector.

Apart from expanding the production capacity of Colour STN, the Group will fortify its alliances with TFT (Thin-Film Transistor) suppliers to enrich the Group's technological offerings in colour LCD solutions.

Commercialisation of New Technologies

BCD and ZBD are unique technologies that require low power consumption and display multi-colour, high-resolution, high-contrast images. They are able to retain the images without consuming any power and hence are especially suitable for handheld products or products that operate under environments where electric wiring is inconvenient.

Varitronix is highly confident of these technologies and the initial response from customers has been encouraging. The Group and its technological partner will make every effort to commercialise these technologies for a wide range of applications.

The Group achieved consistent advancement of its LCOS (Liquid Crystal On Silicon) Microdisplay technology and improved the resolution to 1920 x 1280 pixels in panels the size of a postage stamp. The technology is commercialised in various fields including photograph developing.

Expansion of Production Capacity

In order to meet increasing demand, and to ensure that the Group has adequate room for future expansion, the Group is expanding its production plant in Shenzhen. The construction is expected to be completed by the end of 2006. It is expected that a meaningful growth in capacity will be achieved in the following years when production is ramped up.

Cost Control

The Group has set up a dedicated team responsible for coordinating and implementing measures to control costs, increase the competitiveness of our products and add value to our customers.

Prospects

We believe that the demand for LCD products will continue to rise in the automotive, industrial, consumer and telecommunications sectors.

Faced with a wide array of opportunities in the market, the Group will accelerate its quest to increase its market share. We have recently adopted a new company logo, and our head office has returned to the place where Varitronix was

founded. We have returned to our roots, from where we will launch initiatives that maintain our traditional values and at the same time keep abreast of contemporary corporate cultures. At present, our staff is working from top to the bottom. Senior management devises development strategies that lead the market trends. Middle management demonstrates strong organizational abilities and efficient execution skills. The technical, marketing and various support teams ensure that customers are satisfied with our services. The Group as a whole is progressing towards our goals with confidence.

The LCD industry represents great potential. Varitronix has been engaged in the design and manufacture of LCD and related products for 28 years, and the LCD market has ever been expanding. With decades of experience and the development of new technologies, we believe that we will further develop the market, and we will continue to focus on LCD as the core business.

Acknowledgements

We would like to thank our shareholders for their continued support, particularly during such a challenging year as 2005. This is not only gratifying but also strengthens our commitment to strive for greater achievements for the Group. We would also like to express our sincere gratitude to the Board of Directors, for their unfailing support which has sustained the growth of Varitronix throughout the years. Furthermore, we would like to thank Dr Yan Sze Kwan, Mr Chung Shun Ming, Mr Kwok Siu Kwan, Professor Kao Kuen, Charles, and Mr Lui Chi Shing, Anthony who retired from the Board, for their valuable contributions to the Group during their tenure. Varitronix has entered a new phase of development. The aspiration for excellence demonstrated by our staff will continue to drive us towards the realisation of our goals.

Chang Chu Cheng
Chairman

Ko Chun Shun, Johnson
Chairman

Hong Kong, 10 April 2006