

Review of Operations



Europe

Thanks to a close and long-term partnership with its customers, Varitronix continued to maintain a strong market presence in Europe. In 2005, the Group strengthened its niche as a supplier of custom-made LCD products to the automotive and industrial sectors. Several new projects were initiated to bring increased contribution to the group in the coming years. Sales in Europe amounted to HK\$636 million, compared with HK\$633 million in 2004.

Europe is the Group's second largest market segment after the "PRC and Hong Kong" segment, generating sales which accounted for 32% (2004: 32%) of the Group's turnover.

The PRC & Hong Kong

A difficult business environment for our customers in Mainland China adversely affected our business there. The illegal counterfeiting and refurbishment activities of the "black handset" market players were rampant, resulting in a decline in sales for our customers who are licensed mobile phone manufacturers. To reflect the changes in market environment, we wrote off the value of stock inventories by HK\$40 million.

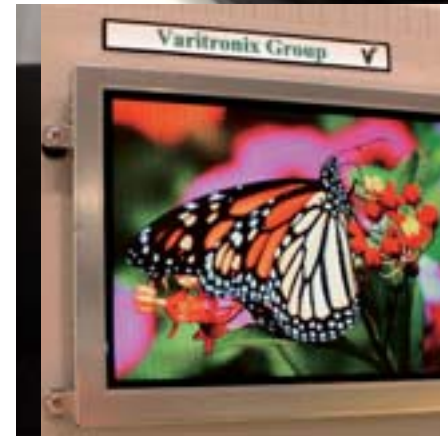
The market environment in the second half of 2005 remained challenging, although we saw early signs of recovery. Sales in the PRC and Hong Kong declined by 12% to HK\$828 million for the full year (2004: HK\$941 million).

We believe that the Group's business in the PRC will resume its growth trend with the recovery of the PRC mobile phone market.

The Rest of Asia

Our business in Asia outside the PRC and Hong Kong (the "Rest of Asia") expanded rapidly in 2005. Sales in the region increased by 25% to HK\$372 million in 2005 from the previous year's HK\$299 million. The growth was driven by robust demand for LCD products embedded in portable entertainment products as well as emerging demand for LCD products used in motor vehicles.





Sales in the Rest of Asia as a percentage of the Group's turnover increased to 19% in 2005 from 15% in the previous year, which followed our development strategy of broadening our geographical footprint.

North America & Others

Sales in North America amounted to HK\$88 million, compared with HK\$89 million in 2004. Sales in regions apart from those mentioned above (the "Others") increased by 25% from the previous year to HK\$55 million (2004: HK\$44 million).

Production

To streamline our production processes and realise economies of scale, Varitronix relocated its production facilities and centralised the production processes into Nanling and Heyuan in the PRC.

In 2005, we moved our production lines in Hong Kong and Shawan, Shenzhen, into these major plants. In addition, we decided to relocate the production capacity in Penang, Malaysia to these major plants. Although the relocations incurred certain non-recurring costs and accounting charges, the improvement in production efficiency which is expected to result from the relocation is in the interest of the Group.

Colour Products

To capitalise on the market opportunities arising from TFT technologies, Varitronix formed alliances with leading TFT panel manufacturers in Asia. Through such alliances, the Group has access to its partners' experience and expertise in TFT technologies, which is helping shorten our learning process in the design and production of TFT modules. At the same time, Varitronix provides its partners with access to its well-established worldwide distribution channels. These alliances enable Varitronix to focus on the high value-added processes without locking up the large amounts of capital needed for upstream manufacturing.

As an important step toward broadening the spectrum of its technology offerings, Varitronix invested in Korean-based Ness Display, one of the world's leading OLED providers. Ness Display commenced mass production in December. The investment in Ness Display secures a stable supply of high-quality full-colour OLED panels.

Final Remarks

Having made solid progress in 2005, the Group is poised to go forward on a solid foundation.