MANAGEMENT DISCUSSION AND ANALYSIS

OPERATIONS REVIEW

Working against the challenging year of 2005, the Group was adversely affected by the fierce price competition in the computer component and information technology products market and the allowances for its doubtful debts. The Group recorded a loss of approximately HK$596 million for the year 2005.

During the year, the Group's turnover was approximately HK$1,198 million (2004: approximately HK$1,659 million), representing a decrease of approximately 28%. The Group recorded an increase in the quantity of products sold by approximately 27% compared with 2004. However, the average selling prices were lower than previous years because of the price-cutting strategies commonly adopted in the market. Revenue generated from the PRC market in 2005 accounted for about 81% (2004: 62%) of total turnover. The increase was mainly due to the Group continuous expansion of its distribution and logistic networks in the PRC.

Gross profit of approximately HK$27 million was recorded for the year 2005. It represented a 68% decrease of gross profit compared with 2004, which was mainly due to the decreasing selling price of the computer components and information technology products.

The Group had made a significant amount of allowance and write-down during the year 2005. Details were set out below:

- **Trade Receivables**

  Amongst the gross value of approximately HK$500 million at 31 December 2005, the Group had made an aggregate allowance of doubtful debts of approximately HK$403 million. The trade receivables were regarded as doubtful because they had exceeded the Group's credit period. There was also no subsequent settlement since year end. However, the Group is in discussion with our major customers in relation to the repayment arrangement by them. The Group expects that such repayment arrangement may improve the Group's liquidity in the future.

- **Rebates Receivables**

  An allowance for rebates receivables amounting approximately HK$93 million was made in 2005. The rebates receivables were resulted from the purchase of inventories from the Group's major supplier, in which a material amount was regarded as long-aged receivables. Because of the Group's liquidity problem, the amounts owed to the major supplier had not been settled for a considerable time. As such, the Directors consider it is unlikely that the rebates receivables can be utilised in the future. Accordingly, the Group adopted a prudent strategy of making an allowance for the rebates receivables to reflect the current situation with the major supplier.

- **Inventories**

  The Group had made a write-down of inventories of approximately HK$66 million during the year. The write-down was mainly attributable to the aging analysis and the market situation of the inventories. The Group is now paying great deal of effort to market these aged stocks in various channels. It is expected that the possible sales of these inventories may relax the Group's liquidity and financial position.

Finance costs for 2005 was approximately HK$19 million which represented an increase by approximately 20% compared with 2004. The increase in finance costs was mainly resulted from the steady rise of interest rates in 2005. The administrative expenses were approximately HK$29 million which was close to 2004. The Group managed to tighten the distribution costs, which led to a decrease of about 31% to approximately HK$6 million compared with HK$9 million in 2004.

BUSINESS RELATIONSHIP WITH MAJOR PARTNERS

Due to the Group's default in settling the purchase of inventories, one of our major suppliers had taken legal action to recover the amount due to them. The Group is in negotiation with the supplier in settling the dispute. The business partnership remains unchanged as at the date of this report and the Group is still possible to place orders with the supplier.

LIQUIDITY, FINANCIAL RESOURCES AND GEARING

The Group had total cash and bank balances (including pledged bank deposits) of approximately HK$51 million as at 31 December 2005 (2004: approximately HK$118 million). Balance of bank overdrafts and short-term bank borrowings was approximately HK$230 million as at 31 December 2005 (2004: approximately HK$387 million). The short-term bank borrowings were applied to finance the purchase of inventory of the Group. The gearing ratio of the Group as at 31 December 2005 calculated as a ratio of total bank loans to total assets was 102% (2004: 38%). Net liabilities were approximately HK$143 million (2004: net assets of approximately HK$483 million).

The Group recorded total current asset value of approximately HK$217 million as at 31 December 2005 (2004: approximately HK$1,062 million) and total current liability value of approximately HK$370 million (2004: approximately HK$605 million). The current ratio of the Group, calculated by dividing the total current asset value by the total current liability value, was about 0.6 as at 31 December 2005(2004: approximately 1.8).

MANAGEMENT DISCUSSION AND ANALYSIS

The Group had inventories of approximately HK$55 million as at 31 December 2005 (2004: approximately HK$361 million) representing a decrease of 85% from last year. The substantial decrease was mainly due to the written-down for aged stocks of approximately HK$66 million according to our prudent strategy.

The Group recorded a loss in 2005 and this attributed to a decrease in shareholders' funds to a negative value of approximately HK$145 million as at 31 December 2005 (2004: a positive value of approximately HK$452 million).

TREASURY POLICIES

The Group's major borrowings are in US dollars and HK dollars. All borrowings are based on LIBOR or Hong Kong best lending rates. As the Group's revenues are mainly in US dollars, and major borrowings and payments are in either US dollars or HK dollars, there is a natural hedge mechanism in place and currency risk exposure is relatively low. However, the Group has strengthened its treasury management functions and will continue to manage its currency and interest rate exposures.

PLEDGE OF ASSETS

In accordance with the terms of the distribution agreements entered into between the Group and a major supplier, the Group has granted the major supplier a security interest in the inventories supplied and in any proceeds (including accounts receivables) as security for any outstanding amount due by the Group. In addition, certain bank deposits of the Group were pledged to its bankers to secure certain banking facilities granted to the Group.

INVESTMENTS

The Group acquired 30% issued share capital of a company engaged in logistics and warehouse management business for a cash consideration of HK$15 million in 2004. As the logistics business became more competitive, the associated company recorded a loss for the year 2005. The Group had taken the best estimate to revise its cash flow forecasts for the associates. Accordingly, the goodwill arising from the acquistion was written off. In December 2005, the Group established a Joint Venture. The company is to engage in the DTV business in the PRC and expected to bring substantial benefits to the Group in the future.

MANAGEMENT DISCUSSION AND ANALYSIS

CONTINGENT LIABILITIES

The Group had no significant contingent liabilities at the balance sheet date.

EMPLOYEES

As at 31 December 2005, the Group had 35 full time employees.

The Group remunerated its employees mainly based on the industry practice, individual's performance and experience. Apart from the basic remuneration, discretionary bonus and share option may be granted to eligible employees by reference to the Group's performance as well as individual's performance. Other benefits include medical and retirement schemes.

AUDIT COMMITTEE

The principal activities of the Audit Committee include the review and supervision of the Group's financial reporting process and internal controls. The Audit Committee has reviewed the financial statements of the Group for the year ended 31 December 2005.

The Audit Committee comprises three independent non-executive directors, namely Dr. Liu James Juh, Ms. Hu Gin Ing and Mr. Yim Hing Wah.