MANAGEMENT DISCUSSION AND ANALYSIS

BUSINESS REVIEW

The Group experienced an extremely difficult period with a widened operating loss in the first half of 2006. Global TV market competition was as keen as ever and the operating environment remained tough, especially for the European market. Due to unfavourable macro market conditions and company-specific issues such as slow product rollout, the performance in the European market was far below expectation. The Group as a consequence recorded an operating loss of HK$504 million for the first half of 2006 (as compared to an operating loss of HK$25 million for the same period last year). However, the operating performance of other non-Europe businesses remained healthy, with the PRC, North America, Emerging Markets and Strategic OEM recording an operating profit of over HK$325 million during the period under review.

The Group is of the view that the challenges met in Europe will continue to prevail in the coming quarters. As such, it performed a critical assessment of its investment in Europe and recognised an impairment loss of HK$865 million with respect to certain assets of its European business arm, which significantly affected the Group's first half-yearly results. As a result, a net loss of HK$1,600 million was reported for the six months ended 30 June 2006.

Facing tremendous challenges in respect of business operation and financial performance, the Group has implemented a series of strategies to counterbalance the negative impacts and to enhance its competitiveness in the core markets. The Group maintained its dominant position in the PRC with an increased market share despite market contraction. In North America, the Group's business performance was in line with management's expectations related to sales growth and improvement in operating results. Encouraging sales volume growth was seen in Emerging markets as well as the Strategic OEM business.

TV Business

For the six months ended 30 June 2006, TV sales revenue amounted to HK$13,195 million, representing a decrease of 1.9% as compared with that of the same period last year. This segment, being the Group's core business, took up 84% of the Group's total turnover (1H2005: 86%). During the period, a total of 10.88 million sets of TVs were sold, posting a year-on-year increase of 11%.

In line with the global industry trend, the Group continued to enhance its product mix by rolling out new high-end models. Strong focus was placed on flat panel TV, as the Group recognized the huge growth potential in the global market. In order to cater for different market needs, more than 100 models were launched during the first half of 2006, approximately half of which were high-end models (flat panel TVs and projection TVs).

According to the latest iSuppli data for the first quarter of 2006, the Group was ranked number one in the global market by volume, with 11% market share.

In thousand sets	**1H2006 *('000)***	1H2005 *('000)*	**Change**
TV Unit Sales	**10,880**	9,775	+11%
The PRC	**3,735**	4,144	–10%
Europe and North America	**2,700**	2,698	Nil
Emerging Markets and Strategic OEM	**4,445**	2,933	+52%
PC Unit Sales	**382**	331	+15%

The PRC Market

According to the Ministry of Information Industry (MII), the PRC TV market recorded a year-on-year decline of 12% in the first six months of 2006, which was due to the contraction of CRT TV market. Our overall TV unit sales also saw a milder-than-market decrease of 10% to 3.74 million sets, of which TCL brand and Rowa brand TVs accounted for 3.19 million sets and 0.55 million sets respectively. Sales revenue from the PRC market amounted to HK$4,631 million and accounted for 35% of total TV sales. Despite the shipment decline of the industry, the Group continued to maintain its leading position with a market share of 21% in terms of sales volume, ranking the first in the PRC market, according to MII (Jan-Jun 2006).

During the period under review, market competition was no less severe than before. Domestic and foreign players competed on pricing and the pace in introducing new products. To maintain our leadership and to prepare for further growth in the market, we implemented a number of measures, which include constantly reviewing and adjusting our supply chain management, strengthening our relationship with distributors of all levels, and improving product planning (launching fewer new models but concentrating on superior models with more new features).

Benefiting from our efforts, we successfully upgraded our product mix. The sales of LCD TVs, slim CRT TVs and 16:9 CRT TVs grew significantly. Our LCD TV products demonstrated a growth of over 200% year-on-year, outperforming the market growth rate, and accounted for 23% of total sales revenue (1H2005: 6%). Our market share in LCD segment, according to China Market Monitor report of May 2006, was 9% among the top notch.

Not only did The Group maintain its leading position in the market, but also its solid operating results. The PRC market recorded an operating profit of HK$175 million in the first half of 2006.

MANAGEMENT DISCUSSION AND ANALYSIS

European and North American Markets

Amidst keen market competition, the Group sold a total of 2.70 million sets of TVs in the European and North American markets, with aggregate sales revenue of HK$6,187 million and accounting for 47% of total turnover of TV business.

In the European market, the Group implemented a number of business strategies to address the needs of its target market segments. It focused on key countries, key product lines and key customers that offered development potential. Nevertheless, the benefits of these efforts were not shown due to the rapidly changing market environment, and improvements were yet to be made with respect to supply chain management and new product pipelines. The European business therefore recorded a widened loss. As for the North American market, the Group exceeded its sales growth objectives in the DLP and LCD product segments and improved its working capital utilization.

Operating loss in the European market amounted to HK$758 million, as compared with a loss of HK$133 million for the same period in the previous year, while the operating results of the North American market improved substantially and made a step further in approaching breakeven during the period under review.

European Market

In the first half of 2006, the Group experienced a difficult period during which it had to reduce product prices drastically, partly to boost sales and partly to clear old inventories to make room for future developments.

The market trend of switching from CRT TV to flat panel display TV (LCD and Plasma TV) continued to prevail. According to the GfK's report for March to April 2006, flat display TVs accounted for 79% of market value in the European market. This trend was not favourable to the Group because notwithstanding its strength in the CRT TV segment, improvements in supply chain management and new product pipelines were required with respect to the flat panel display TV segment. As sales of flat panel display to total TV sales increased from 42% in the same period last year to 46% in the period under review, and as flat panel display TVs generally commands a lower gross margin as compared to CRT TVs, the Group's gross margin was adversely impacted.

During the period under review, the Group continued to address the needs of major market segments and key consumers' expectations with the offering of precise and structured products. This strategy also meant that more resources would be placed on countries where the Group had a strong presence. However, the implementation of this strategy was far from satisfactory as we encountered delay in introducing certain product series. At the same time, our efforts in selling the inventory of old models also had a negative impact on the overall sales revenue and profitability.

The Group enjoyed a market share of 6% in Europe. (Source: GfK report, January to April 2006, Europe 4 (France, Germany, Italy, Spain), TTE Group value share)

North American Market

Market competition was keen in North America. Price continued to be the focus of market competition in the mature segments like analogue CRT TV and CRT-based PTV. In the DLP segment, although pricing was a crucial factor, the brand image formed another realm of competition. As for the flat panel segment, both price and brand recognition were of equal importance.

The Group's sales and operational performances in the North American market remained on track with improved operating results during the period under review. In the first six months of 2006, both sales volume and value exceeded expectations as growth in the LCD and DLP product segments outpaced the industry average. The Group's sales also benefited from the ongoing analog to digital transition in the U.S. market. According to Synovate data on consumer purchases of TV's for January to May, the RCA brand ranked the third in the U.S. market with a share of 9%.

The Group's efforts are very focused on satisfying the needs of its customers, including mass merchants, national and regional chains and rental customers. Meanwhile, it also embarked on marketing programmes to strengthen its product positioning as "Affordable Digital Television for Every Room and Budget". Continued improvements in profitability were seen as a result of effective cost controls, reduced inventory, better supply chain management and product mix enhancement. High-end TVs accounted for 58% of the sales revenue in North American market.

Emerging Markets and Strategic OEM

The Emerging Markets and the Strategic OEM business continued to record encouraging performance in the first half of 2006. TV unit sales in these two markets reached 4.44 million sets, representing a surge of 52% over the corresponding period last year. The two segments achieved a combined revenue of HK$2,376 million, accounting for 18% of total TV sales revenue. During the period under review, the two operations remained profitable and posted an operating profit of HK$130 million.

For Emerging markets, the average selling price declined slightly due to inventory clearance. However, riding on the market development trend, the Group attained impressive growth in countries including Mexico, Thailand, Australia and India.

Regarding the Strategic OEM business, the Group successfully tapped into the Russian and the Turkish markets which attributed to a substantial increase in sales revenue. During the period, the Group launched a number of tailor-made products which received overwhelming market response and helped the Group to secure orders from clients.

MANAGEMENT DISCUSSION AND ANALYSIS

PC Business

Facing intensified market competition, the Group allocated more resources on promoting and selling its product. Results were encouraging. The Group's PC unit shipment recorded a growth of 15% over that of the same period last year, of which notebook PC posted a notable increase of 316% in sales volume. Despite the rise in sales volume, its weight in the Group's overall business performance gradually declined with the globalization of our TV business.

For the six months ended 30 June 2006, the Group's PC sales revenue amounted to HK$1,207 million and accounted for 8% of the Group's total turnover.

The Group enhanced its marketing and promotional efforts in notebook PC series while introducing the second generation of "SHE" series desktop PC to capture more young female clients. Besides, the Group and Intel jointly launched the world's first-ever notebook PC with core duo CPUs, "Verone", in the first half of 2006.

An operating profit of only HK$1 million approximately was reported for the period under review, mainly due to a bad debt provision of HK$14 million.

In order to concentrate on its TV business, the Group, on 21 June 2006, announced the plan to dispose of its PC and web education businesses as well as the other non-TV assets to its ultimate controlling shareholder, TCL Corporation, at an initial aggregate cash consideration of HK$377 million. Upon the disposal, the Group would be capable of allocating more resources on strengthening its global TV operations and TCL Corporation would be able to deploy more resources in expanding the PC business in the PRC market. It is believed that such initiative will bring forth meaningful benefits to the Group in the long run.

Outlook

The global TV industry is now undergoing dynamic changes. The Group expects market competition will continue to intensify. Market players compete for survival by offering low priced products, which will further undermine profit margin and brand image. In addition, the ever-changing consumer demand and pursuit in advanced technology also increased its operating cost and research and development ("R&D") expenses.

With flat panel TV becoming the global growth engine, the Group will further strengthen its product development and promotion of flat panel TV and enhance its brand image to reinforce its market competitiveness. The Group will strive to capture more market share in flat panel TV while consolidating its foothold in CRT TV business. Nevertheless, the profit margin of flat panel TVs is currently still lower than that of CRT TVs. The increase in sales mix of flat panel TV may harm the overall profit margin of the Group. To maintain profitability, the Group will further strengthen its supply chain management and perfect its sales and distribution channels, so as to reduce its operating expenses.

The Group will continue to launch new and innovative TV products in the market. It plans to launch over 70 models in the second half of the year to accommodate the change of market demand and product trend. 40% of the new models would be conventional CRT models and 60% of them would be high-end models, in which LCD models would be the dominant one. Looking ahead, the Group will further improve its time-to-market and will accelerate the speed of product rollout.

All of the above strategies will be carried out with the ultimate goal of achieving turnaround in its business within the shortest period and recording profitable results in the foreseeable future.

FINANCIAL REVIEW

The Group recorded substantial loss for the period under review. Although performance of the Group's businesses in major markets including the PRC and the North America was in line with the management's expectation, with even better-than-expected sales revenue generating from the Emerging and Strategic OEM markets, results of the Group was materially adversely affected by deteriorating performance of the European operations. The Group is currently taking measures to drastically restructure its European operations in order to minimize incurring further losses, and to reschedule its debts so as to improve its solvency position. The Company has decided that it will not invest any further capital in the European business until the European management present to the Company a convincing new business plan.

Impairment of European Assets

In view of the above, the Group has carefully re-assessed its investment in Europe and estimated the recoverable amounts of all major categories of assets in relation to the European business according to the latest reorganisation plans in Europe. Losses on assets impairment and write-down of HK$865 million in aggregate were incurred as a result.

The impairment and write-down made for the Group's European assets in the first half of 2006 are summarized as follows:

	HK$ million
Angers factory assets receivable	79
Trademark fee reinvestment	62
Property, plant and equipment	225
Inventories	499
Total	865

MANAGEMENT DISCUSSION AND ANALYSIS

Significant Investments and Acquisitions

On 9 March 2006, TCL King Electrical Appliances (Huhehaote) Company Limited ("TCL King Huhehaote"), an indirect wholly-owned subsidiary of the Company, entered into an investment agreement (the "Investment Agreement") with TCL Corporation in relation to the setting up of a finance company in the PRC (the "Finance Company"). Pursuant to the Investment Agreement, TCL King Huhehaote contributed RMB70 million as capital contribution to the Finance Company, representing 14% of the registered capital of the Finance Company.

The establishment of the Finance Company is subject to the obtaining of the approval from the relevant PRC authorities, including but not limited to the China Banking Regulatory Commission. Further details of this transaction were set out in the Company's announcement dated 9 March 2006.

Liquidity and Financial Resources

The Group's principal financial instruments comprise bank loans, factorings, cash and short-term deposits. The main objective for the use of these financial instruments is to maintain a continuity of funding and flexibility at the Group's lowest cost.

The cash and bank balance as at the year end amounted to HK$1,771 million, of which 2% was maintained in Hong Kong dollars, 20% in US Dollars, 49% in Renminbi, 13% in Euro and 16% held in other currencies for the overseas operations.

There was no material change in available credit facilities when compared with the year ended 31 December 2005 and there was no asset held under finance lease at the period end.

At the period end, the Group's gearing ratio was 1.2 which is calculated based on the Group's net borrowing of approximately HK$2,897 million (calculated as total interest-bearing borrowings less cash and bank balances) and the equity attributable to equity holders of the Company of approximately HK$2,409 million.

Going Concern Assumption

As a result of the poor financial performance in Europe, for the period under review the Company breached certain financial covenants under (i) the Facility Agreement dated 23 December 2002 (as amended and supplemented) in relation to HK$400 million Term Loan Facility and (ii) the Dual Currency Facilities Agreement dated 16 November 2004 in relation to US$180 million Term and Revolving Loan Facilities (collectively the "Loan Agreements"), both entered into by the Company as borrower. The Group has commenced certain measures to negotiate with its creditors with a view to rescheduling some of its indebtedness in particular for its European operation. Under the Loans Agreements, the aforesaid constituted events of default which would entitle the relevant banks to declare that all the outstanding loans are immediately due and payable.

The aggregate amount outstanding under the Loan Agreements as at 30 June 2006 was HK$1,529.8 million. If the banks are to take action in respect of any of the events of default, there would be fundamental uncertainty as to the Group's ability to continue operation as a going concern. Nevertheless, the directors of the Company are of the view that it is appropriate to adopt the going concern basis in preparing the financial statements based on the followings:

(a) It is expected that on 8 September 2006, the Company will complete the disposal of its computer and non-core business to T.C.L. Industries and the proceeds of around HK$377 million will be used to partially repay the amount outstanding under the Loan Agreements. The amount of current liabilities will thereby be reduced.

(b) As at 30 June 2006, the Group's current liabilities exceeded its current assets by approximately HK$1,030 million. It mainly resulted from (i) classification as current liabilities of the outstanding loans under the Loan Agreements as a consequence of the said events of default, and (ii) the substantial impairment and write-down made by the Company for its investment in Europe. The impairment and write-down though had significant impact on the financial statements of the Group, they did not have adverse impact on cash flows of the Group.

(c) It is considered that the debts rescheduling currently implemented by the Group would be conducive for its European operations to easing its financial pressure and facilitating its turning around. Further, as mentioned above, the Company has decided that no further capital will be invested in the European business. Therefore, the overall position of the Company will be better in future.

(d) The Group is now actively exploring the availability of various options of fund raising to help improve the financial position of the Group and in the process of negotiating with the relevant banks to restructure the loans.

MANAGEMENT DISCUSSION AND ANALYSIS

Having considered the above, the directors of the Company are confident that it is unlikely that the banks will declare all the outstanding loans under the Loan Agreements to become immediately due and payable. As the Group has adequate resources to continue in operational existence for the foreseeable future, the directors consider that it is appropriate to adopt the going concern basis in preparing the financial statements.

The financial statements do not include any adjustments relating to the carrying amount and reclassification of assets and liabilities that might be necessary should the Group be unable to continue as a going concern.

Capital Commitments and Contingent Liabilities

There was no significant change in capital commitments and contingent liabilities of the Group compared to the position outlined in the annual report for 2005.

Foreign Exchange Exposure

Due to its international presence and operations, the Group is facing foreign exchange exposure including transaction exposure and translation exposure.

It is the Group's policy to centralize foreign currency management to monitor the company's total foreign currency exposure, to net off affiliate positions and to consolidate hedging transactions with banks. The Group emphasizes the importance of trading, investing and borrowing in functional currency to achieve natural hedging.

Employee and Remuneration Policy

The Group had a total of 25,000 dynamic and talented employees. They were all dedicated to advancing the quality and reliability of our operations. Remuneration policy was reviewed regularly, making reference to current legislation, market condition and both the individual and company performance. In order to align the interests of staff with those of shareholders, share options were granted to employees under the Company's share option schemes. Options for subscribing a total of 168,817,861 shares remained outstanding at the period end.