



MANAGEMENT DISCUSSION AND ANALYSIS

Financial Performance

During the six months ended 30 September 2006 (the "Period"), the Group's consolidated turnover increased to HK\$1,277 million from HK\$1,175 million during the same period last year, representing a growth of approximately 9%. The growth in turnover was mainly attributed to the steady increase in the Group's current markets as well as sales expansion in new markets such as Russia, Eastern Europe and South America.

Gross profit for the Period rose to HK\$235 million from HK\$219 million during the corresponding period in 2005, representing an increase of approximately 7%. The Group managed to maintain a gross profit margin of 18% despite higher raw material prices. During the Period, other operating income decreased to HK\$8 million from HK\$27 million, mainly due to a one-time reversal of allowance for bad and doubtful debt in the previous period. And along with an increase in finance cost that resulted from higher interest rates during the Period, the Group recorded a net profit of HK\$143 million, representing a decrease of 6% from HK\$152 million a year ago.

During the Period, the Group implemented further cost-control measurement. As a result, there was a decrease of 22% in administrative expenses from HK\$60 million to HK\$47 million for the six months ended 30 September 2006.

Business Review

Steady growth in current markets

Over the past six months, the North American, Asian, and European markets remained the cornerstone of the Group's business.

During the Period, the new products such as digital photo frame and global positioning system (GPS) were successfully launched in the market. With the support of these new higher potential growth products, the total sales in the PRC market increased by 33% over the same period of the last year and accounted for approximately one-third of the Group's total sales in the Period.

The Group had established and maintained its strong relationship with top distributors and retail chains in the US to further consolidate its market position. Along with the dedicated efforts by the sales teams in the US, strong demand was being generated. The brand of Matsunichi has established a foothold in the US market, resulting in a growth of 10% in sales from a year ago.

During the Period, the Group focused its efforts in consolidating European markets. It restructured the German office to boost sales turnover. As a result, the sales growth in Europe was gradually and periodically affected. But the Group's future operation in Europe is expected to be enhanced by restructuring, and the management is optimistic on the European market.



Further expansion of new markets

During the Period, the Group continued to expand the global market engagement and the overseas sales networks. As the digital consumer electronics markets in Russia and Eastern Europe are still in initial stage, the Group foresees there will be a large growth in these regions. Under the reviewed period, the Group cooperated with a number of large distributors and retail chains and successfully launched storage products and other digital consumer electronics items. Due to the strong demand, the Group enjoyed a sales boom in Russia and Eastern Europe. The Group also took the initiative to cooperate with well-established retail stores in both Hungary and Argentina for launching the electronic consumer products in those growing markets. the Group enjoys an extensive worldwide coverage sales network currently in resulting from the implement of the above strategies.

Global marketing for brand building

In the Period, the Group continued to enlist the support of its global spokesman, US Olympic gold medal winner Michael Phelps to promote its brand globally. The association with Phelps has strengthened the Group's image while focusing on the manufacturing of personal electronic digital products. Matsunichi is one of the few Asian brands in the industry who enjoys strong exposure in the American and European markets currently. This helps to consolidate the Group's worldwide distribution and sales network.

Prospects

Quick response to industry trends

The Group is always responsive to and catch up with the market trends. The industry analyst, International Data Corporation (IDC), estimated that between 2005 and 2008, the global shipments of Personal Multimedia Players will rise from 1.5 million units to 90 million units, at a CAGR of approximately 290%. The Group is poised to capture a share in this lucrative growth market, with launching new models that contain value-added functions such as GPS and digital broadcast reception capabilities. Contributed from all timely strategic moves, the Group is expected to further boost its competitiveness in the digital consumer electronics sector.

Capture market share by product innovation

In the new product market which is less competitive, it is easier for industry players to gain a large market share and high profit margin. As a result, the Group is always keen on developing the innovative products in order to be a market pioneer. For example, the Group developed the digital photo frame which gained a success in the US market, so the Group will launch the digital photo frame in other markets in the coming year to capture more new product market share. Moreover, the Group is one of the forerunners to launch the digital video broadcast (DVB) and the GPS, under the brand name of Matsunichi, in the US and European markets in the coming years. Other innovative products, such as iPod accessories and photo viewers, will be unveiled shortly. Going forward, the Group will focus on the product innovation and development in order to capture a larger market share and sustain sales growth.



Improve account receivables and reduce working capital needs

The Group plans to enter into agreement with the Bank of China in order to shorten its payment collection period. It is expected that the agreement would enable the Group to obtain payments from the Bank of China immediately after the client confirms receiving the products in the US. As a result, the Group will enjoy a shorter days of account receivables, improve operating cash flows and reduce the working capital needs.

Going forward, management believes that the demand for electronic consumer products would remain robust because of a strong growing economy particularly in the emerging markets. Under this environment, the Group will closely monitor the industry trends and concentrate its efforts in launching the innovative products in a timely fashion. Also the Group will further consolidate its sales and distribution network as well as improve the efficiency of the operation and cost control. By capitalizing on its well-established brand name, the management is confident that the Group will further increase in sales, expand market share and maximize shareholders' returns in the future.

FINANCIAL POSITION AND CAPITAL STRUCTURE

As at 30 September 2006, the Group had approximately HK\$1,152 million of cash on hand compared to approximately HK\$1,305 million as at 31 March 2006. The strong cash position has paved the way to finance the working capital requirements of the Group. On the other hand, the Group had neither committed any substantial capital expenditure nor borrowed long-term loan. This further consolidated our liquidity position in the longer run.

The total short-term bank borrowings had decreased from HK\$891 million as at 31 March 2006 to HK\$824 million as at 30 September 2006. The gearing ratio (defined as total bank borrowings on shareholders' equity) decreased from 0.66 as at 31 March 2006 to 0.57 as at 30 September 2006. The Group's liquidity position remained healthy, with a current ratio of 1.9 times as at 30 September 2006 compared with 1.8 times as at 31 March 2006.

The Group's sales and purchase transactions are primarily denominated in either Hong Kong dollars, Renminbi and US dollars. The Group did not face significant risk from exposure to foreign exchange fluctuations.

There was no significant changes to the capital structure since the date of the annual report for the year ended 31 March 2006.

INTERIM DIVIDEND

The directors have resolved to pay an interim dividend of HK7.5 cents per share (2005: an interim dividend of HK5 cents per share and a special dividend HK7 cents per share) to the shareholders of the Company whose names appear on the register of members of the Company on Monday, 8 January 2007.