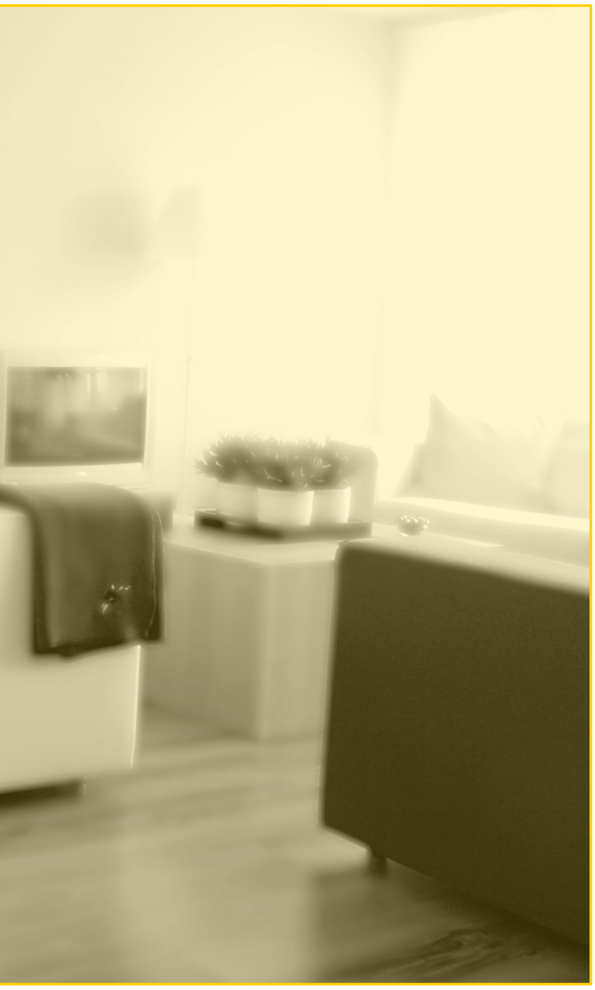
Business Review

The Group has been operating under a challenging business environment throughout 2006. Faced with fierce competition, the Group has been successful in sustaining its sales volume through diversification of its products and services provided to our customers. During the year under review, the Group's original design manufacturer ("ODM") product line continued to perform well. Sales of owned branded and other ODM products in 2006 grew by 19% to 3.1 million units, largely attributable to the new series of *Philips* branded products introduced since the second half of 2005 whereby 1.2 million units were supplied this year. The Group had also been successful in broadening its customer base in other branded original equipment manufacturer ("OEM") products in which sales grew by nearly 2 times to 1.8 million units. However, sales of *Philips* branded OEM products have been reduced as more products are supplied on an ODM basis this year. The overall sales of *Philips* branded products had been dropped by 10% to 5.4 million units. Offset by the overall reduction in sales of *Philips* branded products, the Group recorded an aggregate sale of 8.4 million units of mobile handsets and portable multimedia players in 2006, a mild decrease of 2% as compared to 8.6 million units last year.

During the year under review, turnover of the Group declined by 26% to HK$3,549.3 million from the corresponding period last year, primarily due to a greater proportion of the products being shifted to low to mid-end products this year. To counter the unfavourable operating environment, the Group implemented various measures including stringent cost control and inventory control policies to minimise the overall impact. In addition to the encouraging development in the provision of ODM solution and after sales product maintenance services which brings in good improvement to the overall profit margin, the gross profit for the year was HK$232.3 million, representing a mild increase of 1% over last year.

The profit attributable to equity holders for the year dropped by 13% to HK$43.3 million (2005: HK$49.9 million). Earnings per share for the year was HK3.99 cents (2005: HK4.61 cents).

The directors proposed a 2006 final dividend of HK$0.016 per share (2005: HK$0.02 per share) amounting to a total dividend of HK$17.3 million in cash, which is subject to the approval by the shareholders of the Company at the forthcoming annual general meeting.



Capital Resources and Liquidity

The Group finances its operations primarily by internal resources and short-term bank borrowings. As at 31 December 2006, the Group had cash and cash equivalents amounted to HK$419.8 million (2005: HK$306.4 million) which were primarily denominated in Hong Kong dollars, Renminbi and United States dollars.

As at 31 December 2006, the Group did not have any outstanding short-term bank borrowings (2005: HK$230.8 million). The total bank facilities available to the Group were RMB 1 billion. The Group did not have any pledged assets or guarantee as at the end of 2006 (2005: nil).

As at 31 December 2006, the Group had net current assets of HK$516.3 million (2005: HK$470.7 million). The overall gearing ratio, which is calculated as the total liabilities over total assets of the Group, was 54.8% (2005: 70.6%).

The Group's exports sales are predominantly invoiced in United States dollars and its domestic sales are invoiced in Renminbi. The Group imports some of its raw materials and production and testing equipment from overseas suppliers which are paid in United States dollars, Japanese Yen and Euro. The Group will make use of hedging contracts, when appropriate, to leverage the risk of foreign exchange fluctuation arising from its operations.

Contingent Liabilities and Capital Commitment

As at 31 December 2006, the Group had contracted but not provided for capital commitment of HK$1.3 million (2005: HK$3.2 million) for the acquisition of fixed assets and intangible assets. The Group did not have any material contingent liabilities outstanding as at 31 December 2006 (2005: nil).

Employee and Remuneration Policies

As at 31 December 2006, the Group had 2,850 (2005: 3,500 employees) employees, the majority of whom were based in China. Personnel expenses during the year were HK$149.1 million (2005: HK$139.5 million).

The Group recognises the importance of high calibre and competent staff and has a strict recruitment policy and performance appraisal scheme. Remuneration packages are largely in line with industry practices, and are formulated on the basis of performance and experience and will be reviewed regularly. Bonus and other merit payments are linked with the performance of the Group and of the individuals as incentive to optimise performance. The Company has in place a share option scheme, pursuant to which share options may be granted to selected personnel of the Group, with a view to encouraging employees to work towards enhancing the value of the Group.

Continuing Connected Transactions

On 21 January 2006, the Group's principal operating subsidiary, Shenzhen Sang Fei Consumer Communications Company Limited ("Sang Fei"), entered into a maintenance services agreement ("Maintenance Services Agreement") with Philips (China) Investment Company Limited ("Philips China"), whereby Sang Fei will provide mobile handsets maintenance services to Philips China. The term of the Maintenance Services Agreement is for one year commencing 1 January 2006. Upon expiry of the one-year term, the Maintenance Services Agreement may be extended for one year unless either party objects. The price of the maintenance services will be determined after arm's length negotiations between the parties with reference to the estimated costs to be incurred by Sang Fei for the provision of the maintenance services plus a service charge which is determined in accordance with market rates. The annual cap as set for the aggregate consideration to be received by Sang Fei from Philips China in relation to the provision of maintenance services was RMB60 million.

As the Philips Group owns 25% interest in Sang Fei, the transactions contemplated under the Maintenance Services Agreement constitutes the continuing connected transactions of the Company. China Electronics Corporation ("CEC"), as the controlling shareholder holding 74.98% interest in the Company, has approved the Maintenance Services Agreement and the continuing connected transactions contemplated thereunder by way of written approval.

The Maintenance Services Agreement has been renewed automatically in accordance with its terms in 2007 and Sang Fei will continue to provide mobile handsets maintenance services to Philips China under the renewed Maintenance Services Agreement. The pricing terms will be the same as those previously adopted by the parties. The expected consideration receivable by Sang Fei from Philips China in 2007 under the renewed Maintenance Services Agreement was RMB25 million. Details of the renewed Maintenance Services Agreement were included in the announcement of the Company dated 5 March 2007.

On 3 March 2006, Sang Fei entered into a plastic supply agreement ("Plastic Supply Agreement") with Shenzhen Sang Da Baili Electronics Co., Ltd. ("Baili"), whereby Sang Fei will purchase from Baili the plastic parts used for the manufacture of mobile handsets. The Plastic Supply Agreement is for a term of 3 years commencing from 1 April 2006. The price of the plastic parts supplied by Baili to Sang Fei under the Plastic Supply Agreement is determined after arm's length negotiation with reference to market rates. The pricing terms will be no less favourable than those offered to Sang Fei by other third party suppliers. The Company estimated that the aggregate amount of consideration to be paid by Sang Fei to Baili for the purchase of plastic parts for the nine months ended 31 December 2006, for the two financial years ending 31 December 2007 and 2008 and for the three months ending 31 March 2009 to be RMB43.5 million, RMB104.5 million, RMB120 million and RMB30 million respectively.

As Baili is a subsidiary of CEC, the transactions contemplated under the Plastic Supply Agreement constitutes the continuing connected transactions of the Company. The transactions have been approved by the shareholders in the special general meeting held on 21 April 2006.

On 3 July 2006, Sang Fei entered into a tenancy agreement ("Tenancy Agreement") with Great Wall Technology Company Limited ("Great Wall Technology") and China Great Wall Computer (Shenzhen) Co., Ltd. ("Shenzhen Great Wall"). Pursuant to the Tenancy Agreement, Great Wall Technology and Shenzhen Great Wall agreed to lease to Sang Fei the factory premises situated in 4th Floor, Factory Building No.1, Great Wall Technology Building, No. 3 Kefa Road, Technology and Industrial Park, Nanshan District, Shenzhen City, PRC for three years commencing from 11 August 2006 and expiring on 10 August 2009 (both days inclusive), at a monthly rental of RMB204,296.75 and management fee of RMB32,103.77. In addition, Shenzhen Great Wall will charge Sang Fei for the electricity and water used by Sang Fei's factory premises on an actual consumption basis at cost.

As Great Wall Technology and Shenzhen Great Wall are subsidiaries of CEC, the transaction contemplated under the Tenancy Agreement constitutes the continuing connected transaction of the Company. The annual cap as set for the aggregate rentals and management fees payable by Sang Fei under the Tenancy Agreement were RMB1.2 million for the five months ended 31 December 2006, RMB2.9 million for the two financial years ending 31 December 2007 and 2008 and RMB1.8 million for the eight months ending 31 August 2009 respectively. Details of the transaction were included in the announcement of the Company dated 15 September 2006.

On 21 December 2006, Sang Fei and CEC entered into a supplemental business services agreement ("Business Services Agreement") whereby Sang Fei will supply products, samples and raw materials to CEC and its group companies ("CEC Group") and CEC Group will supply raw material and provide various support services including canteen services and renovation services to Sang Fei. On the same date, Sang Fei and CEC entered into a supplemental processing agreement ("Processing Agreement") whereby Sang Fei will secure complete SMA production lines (together with operational management rights) from CEC Group.

The products, samples and raw materials supplied under the Business Services Agreement to the CEC Group will be priced in accordance with their models and specifications. The price will be determined after arm's length negotiations between the parties with reference to market rates, and will be no less favorable than those offered to other third party customers of Sang Fei. The price of the raw materials and support services to be provided by the CEC Group to Sang Fei will be determined after arm's length negotiations between the parties with reference to market rates, and the price offered to Sang Fei will be no less favorable than those offered by other third party suppliers of Sang Fei. The processing fee of the SMA production lines charged by the CEC Group shall be determined according to a pre-agreed unit price which is determined with reference to market rates. The price offered to Sang Fei will be no less favorable than those offered by other third party service providers to Sang Fei.

The Company estimated that for the three financial years ending 31 December 2007, 2008 and 2009, the amount of consideration receivable by Sang Fei from the CEC Group for the sales of products, samples and raw materials and the amount of consideration payable by Sang Fei to the CEC Group for the purchase of raw materials, provision of the support services and the processing arrangements are as follows:

Type of transactions	**2007** *(RMB'000)*	**2008** *(RMB'000)*	**2009** *(RMB'000)*
Sales of products, samples and raw materials	9,600	11,520	13,820
Purchase of raw materials	20,400	24,480	29,380
After sales and maintenance services	3,600	4,320	5,180
Canteen services	20,000	25,000	25,000
Renovation services	10,000	10,000	10,000
Processing arrangements	20,000	25,000	30,000

Since CEC is the Company's ultimate controlling shareholder holding 74.98% interest in the Company, the transactions contemplated under the Business Services Agreement and the Processing Agreement constitute continuing connected transactions of the Company. The transactions have been approved by the shareholders in the special general meeting held on 26 January 2007.