MANAGEMENT DISCUSSION AND

ANALYSIS

BUSINESS REVIEW

The year under review was a challenging one for the Group as well as for the TV industry globally. The rapid transition from CRT to flat panel TVs and from analogue to digital technology across different markets tested all manufacturers. During the year under review, the Group had developed right strategies to master these market changes and had completed the integration of the international TV business acquired from Thomson in 2004. These efforts put pressure on the Group's operations and greatly impacted its profitability.

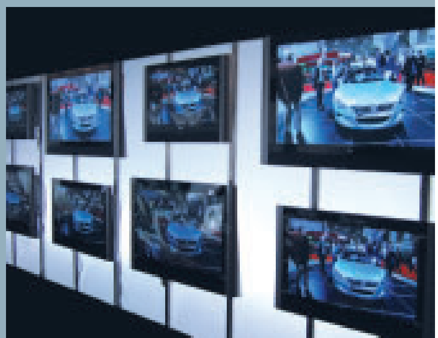
Restoring profitability has been the Group's primary target. Strategies were implemented by the Group to deal with market changes and to strengthen the Group's international competitiveness. However, the management was disappointed to see the operating loss in the European market widen.

Separately, the Group continued to rationalize its operations and resources along its core global TV business. Thus, the Group disposed of its PC business in August 2006 to TCL Corporation, its parent company. In addition, to effectively address the continued poor results in Europe, the Group implemented a wide-ranging restructuring plan beginning in October 2006, and incurred and accrued HK$695 million costs, net of related gains, in connection with the restructuring and winding-down of the EU Business. The operating loss in this market together with the restructuring costs depleted the Group's profits from other markets, leading to a loss of HK$2,500 million for the year ended 31 December 2006.

REVIEW OF OPERATIONS

The Group is a world leading TV manufacturer by sales volume. It is ranked amongst the top three players in the global TV market, according to statistics from iSuppli in December 2006.

Revenue from TV sales decreased by 12% to HK$26,368 million during the year under review. The Group sold a total of approximately 22 million TV sets, representing a decrease of 4% as compared to the previous year. High-end TV models, including Digital Light Processing ("DLP"), flat panel LCD and plasma TVs, accounted for 36% of the Group's TV revenue, as compared to 30% in the previous year. Unit sales of such high-end TVs outpaced overall sales by far, posting a surge of 27% in 2006.



Management Discussion and Analysis

TV Unit Sales	FY2006 ('000)	FY2005 ('000)	Change
The PRC	**7,976**	9,236	(14)%
Europe and North America	**4,775**	6,129	(22)%
Emerging Markets and Strategic OEM	**9,409**	7,639	23%
Total	**22,160**	23,004	(4)%

Seeing enormous potential from flat panel TVs, the Group placed strong focus on, and committed significant resources to, product design and development, supply chain management and sales and marketing in order to capture opportunities in this high-growth market segment. More than 174 models were launched during the reviewing year, of which 84 were high-end models. The Group's market share in the flat panel TV segment rose with its extended product offering.

The PRC Market

Competition in the PRC continued to be fierce as domestic and foreign TV manufacturers flooded the market, quickening the pace of new product introduction and intensifying competition in pricing. This led to rapid price declines in all product categories, in particular for LCD TVs. Seeing this, some consumers delayed their purchases in the hopes of further price reductions.

According to the China Market Monitor report, the PRC TV market experienced a contraction of approximately 7% by volume. This was primarily due to the shrinkage of the CRT TV market, which was larger than the increase in demand for LCD TVs .

Despite the intense competition, the Group maintained its position as the market leader in 2006. Sales revenue from the PRC market amounted to HK$10,459 million, representing a decrease of 5% and accounting for 40% of the total TV revenue. The Group sold a total of 7,976,000 TV sets in the PRC. Although this was a 14% decline compared with 2005, it was within the overall trend of the market. Thus, the Group maintained its leading position in the PRC market, with a share of 18% (source: Ministry of Information Industry (January – December 2006)).

The Group also achieved good performance in terms of the overall product mix, with high-end TV sales accounting for 35% of total TV sales revenue, as compared to 19% for 2005. In terms of unit sales, the Group grew LCD TV sales by 174% year-on-year. Thus, according to the China Market Monitor report of November 2006, the Group achieved a 10% share of the LCD segment in the PRC.

Although the increase in high-end TV sales helped to boost the average product selling price by 10%, the overall profit margin for the PRC market decreased. This was due to the fact that the gross margin for high-end goods such as LCD TVs was and remains lower than that of CRT TVs.

In view of the rapid shift in consumer preference from CRT TVs to flat panel TVs, the Group invested further in the development of high-end TVs and introduced more high-end products, such as its 47" large display LCD TV model, to capture the significant opportunity represented by this growing market.

European and North American Markets

The European and North American markets continue to challenge the Group. Although performance in North American market was in line with expectation, performance in Europe continued to be well below management expectations. Thus, the Company recorded a significant operating loss and provision for the business restructuring.

Sales revenue generated from these two markets in aggregate amounted to HK$10,421 million, representing a year-on-year decrease of 28% and accounting for 39% of the Group's total TV revenue, as compared to 48% in the previous year. A total of 4,775,000 TV sets were sold in these markets during the year under review.

European Market

The European market is one of the world's most dynamic markets in that consumers are migrating at an unprecedented pace towards flat panel LCD TVs. In this highly competitive operating environment, the Group experienced an extremely difficult year. The Group's cost advantages, which had helped it to become a global leader in the CRT market, did not translate into the same market leadership in the high-end flat panel TV market.

Due to the heavy losses in the first part of the year, the Group decided to implement a wide-ranging restructuring plan to close certain loss-making business lines and re-launch the operation under a new, smaller, leaner business model. Going forward, the Group plans to work only with a limited number of key customers, major accounts and markets with the greatest potential, which will enable it to rationalize product lines and its supply chain. The restructuring process began in October 2006 and completion is expected to be in the first half of 2007.

North American Market

In the North American market, price pressure continued to prevail in mature segments, such as CRT TV and CRT-based Panel TV ("PTV"). In the DLP segment, brand image became another crucial competitive factor, though pricing still remained as the primary consideration. In the flat panel segment, product price and brand recognition were of equal importance.

Following the year's reform and hard work in 2005, the Group recorded sales and operating performance were in line with management's expectation for the full year results of 2006. This attests to the Group's capability of managing development efficiently in key aspects such as product development, sales and marketing and cost management.

Both sales volume and sales value exceeded the Group's targets. Remarkable growth was seen in the LCD and CRT PTV segments. According to Synovate data on consumer purchases of TVs in October 2006, the Group's RCA brand ranked the third in the U.S. market with a market share of 9%.

The Group expanded its offering of LCD models in North America and introduced its first model in the plasma segment in 2006. A total of 49 new product models were launched, of which 21 were high-end models. Sales of high-end TVs accounted for 58% of the sales revenue, compared to 47% in 2005.

During the year under review, the Group maintained its focus on key products that are well-received by the market and served key customers that generated higher margin purchases. Meanwhile, the Group continued to communicate and reinforce its product positioning as "Affordable Digital Television for Every Room and Budget", with the aim of offering a compelling combination of good picture quality at an affordable price through its marketing activities.

In addition, the Group put emphasis on enhancing profitability by adopting effective cost control measures, such as reduced inventory, better supply chain management and an enhanced product mix. During the year, the Group enjoyed an overall reduction in R&D expenses on a company-wide basis with better manpower and resources allocation.

Emerging Markets and Strategic OEM Business

The Emerging Market and Strategic OEM business achieved the Group's targets, posting stable and satisfactory sales volume growth in the year under review. Total TV unit sales of these two markets rose by 23% to 9,409,000 sets as compared with last year. Sales revenue of these two segments grew by 24% to HK$5,488 million, accounting for 21% of the Group's total TV sales revenue. However, during the year the Emerging Market business recognized provisions for bad debts and assets write-down of appropriately HK$132 million in total arising from restructuring of operations in certain regions including Russia, India, Thailand and Indonesia. These two divisions, in aggregate, therefore incurred an operating loss of HK$70 million.

An increasing number of new international market entrants made competition in the Emerging Markets keener than in the past. Prices for both CRT TVs and flat panel TVs decreased, thereby leading to declines in the overall average selling price despite the fact that sales of higher-priced LCD grew as a percentage of total sales.

In line with its strategy and market trends, the Group focused on key markets such as India, Russia and Brazil, and was one of the top-tier players in Vietnam, the Philippines and Australia.

In the Strategic OEM business, the Group recorded sustainable growth for the year under review. The Group extended the business scope to its major international clients with a mixed ODM and OEM approach, using TCL-designed chassis. Strong sales growth was seen in the Latin American as well as ASEAN countries. The Group continued to maintain amicable strategic relationships with its existing clients. On top of that, the Group will seek every possible opportunity to develop new accounts and explore the potential to work with internationally renowned customers to produce theme-designed TVs to broaden its product variety.

PC Business

In line with its strategy of focusing resources on its core TV business, the Group disposed of its PC and other non-core businesses to TCL Corporation in early September 2006. As a result, only eight months' results of this business unit were consolidated into the full year results of the Group in 2006 as a discontinued operation. Sales from the PC business amounted to HK$1,568 million, accounting for 5% of the Group's total revenue in 2006.

OUTLOOK

While competition will remain keen in the consumer electronics industry, the outlook of the Group for 2007 is positive. Most regions except Europe are expected to be profitable. Following the restructuring, the new Europe business will be able to reduce significantly the operating losses while strengthening towards an eventual profit in the years to come.

Management Discussion and Analysis

To capture new opportunities arising from the migration to flat panel TV and digital TV, the Group is focusing additional resources on these two areas, in particular on LCD TV. It is determined to improve its product development capability and develop itself into a competitive ODM organization. The creation of an Innovation Centre to lead product development is just one of the initiatives demonstrating the Group's commitment.

The Group is moving towards its goal of establishing global cost advantage in small-size products (products of 26 inches or less), while achieving feature and industrial design differentiation in mid-range and high-end products. Cost reductions in manufacturing have been achieved through component and software standardization, together with a relentless effort to improve overall product and supply chain quality. The Group is also implementing plans to enhance the flexibility and efficiency of its supply chain. Some of the key areas of focus include improving information flow from sales to raw material inventory, thereby increasing organizational transparency, together with re-aligning production workflows, stepping up the accountability of each factory and shortening the overall product turnaround time.

Although the PRC market experienced a contraction in demand in 2006, current signs indicate that it will return to a pattern of growth. It is expected that consumer desire to purchase higher quality TVs, whether higher end CRT TV or flat panel TV, will increase in the lead-up to the 2008 Olympics Games. This grand event is expected to produce a positive consumer sentiment which will largely offset the current slowdown in consumption.

As a result of the restructuring of the Group's Europe business, sales for Europe in 2007 will decrease in terms of both volume and revenue. Despite this, the new business model is expected to drastically reduce the loss attributable to Europe, as operating costs will be significantly reduced after the business restructuring. The Group expects Europe to start to report positive financial results in 2008 as sales are expected to grow considerably versus 2007. The Group's confidence in this operation's future comes from its proven record in its OEM business unit.

The Group expects to see continued improvements in the North American operation. The target in 2007 is to achieve a full year breakeven, and in 2008 a reasonable level of profitability. Currently, projection TVs (including MD RPTVs and CRT-based TVs) account for a large proportion of the sales mix in this market. Sales of LCD TVs are still in early days. The Group will improve its position in the LCD TV segment in the next few years with more marketing campaigns as well as further improvements in cost structure.

Emerging Markets and the Strategic OEM business offer ample room for growth, though they are expected to grow at a relatively slower pace. As competition continues to be mainly on pricing, profit margins will be squeezed further in 2007. That notwithstanding, increased unit shipments and revenue growth will boost earnings in the next few years.

Although there was shrinkage in the market for CRT TVs, it remains a sizable business by volume, as market demand is forecasted to stay at 122 million sets per annum. There has been a trend for global TV manufacturers with sizeable scale to reduce or stop production of CRT TVs. This business has always contributed a stable revenue and profit stream for the Group and, as the demand for CRT TVs still represents a substantial market, the Group is poised for brisk growth in the OEM business at a global level. Its largest manufacturing facilities are in the PRC, where a complete CRT manufacturing industry chain, including key raw materials, components and TV sets, is present.

With its competitive cost advantages, strong research and development capability, effective sales and marketing strategies, and strong brand positions, with the right strategies, the Group will be well placed to regain profitability, maintain a steady global market share and enhance its competitiveness.

FINANCIAL REVIEW

The Group recorded a consolidated turnover from continuing operations of HK$29,187 million for the year ended 31 December 2006, representing a decrease of 10% over the previous year. Gross profit dropped by 18% to HK$4,496 million and overall gross profit margin was down from 17% in 2005 to 15% this year. The decline in turnover and gross profit was mainly due to the winding down of the Group's legacy Europe business implemented since October 2006. Although the Group managed to achieve satisfactory performance in other key markets, the profits could not compensate for the substantial operating loss and the costs and impairment provisions for restructuring incurred by the Europe business, resulting in a net loss attributable to equity holders of the parent of HK$2,497 million for the year under review.

Significant Investment and Disposal

Major investment and disposal during the year are listed out as follows:

(1) On 9 March 2006, TCL King Electrical Appliances (Huhehaote) Company Limited ("TCL King Huhehaote"), an indirect wholly-owned subsidiary

Management Discussion and Analysis

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 – TCL Finance Co., Ltd ("TCL Finance"). Pursuant to the Investment Agreement, TCL King Huhehaote contributed RMB70 million as capital contribution to TCL Finance, representing 14% of the registered capital of TCL Finance. TCL Finance was established on 17 October 2006 and further details of this transaction were set out in the Company's announcement dated 9 March 2006 and 27 October 2006.

(2) On 4 July 2005, the Company and TCL International Electronics (BVI) Limited ("TCLIE"), a direct wholly-owned subsidiary of the Company, entered into a conditional sale and purchase agreement with TCL Corporation for the acquisition of the remaining 49% equity interest in the Sales Company owned by TCL Corporation at a consideration of Euro6.5 million (equivalent to approximately HK$63 million). This acquisition was completed on 10 May 2006 and the Sales Company became a wholly-owned subsidiary of the Group. Further details of this acquisition were set out in the Company's announcement dated 5 July 2005.

(3) On 21 June 2006, the Company and T.C.L. Industries Holdings (H.K.) Ltd. (T.C.L. Industries), a controlling shareholder of the Company, entered into a sale and purchase agreement pursuant to which the Company agreed to sell, and to procure its relevant subsidiaries to sell, and T.C.L. Industries agreed to purchase (i) the entire issued share capital of TCL Computer Technology (BVI) Co., Ltd., (ii) the entire issued share capital of TCL Education Web Limited and (iii) the 65% equity interest in Shenzhen TCL Central R&D Co., Ltd. for a consideration of HK$374 million. The resolution for approving the disposal was passed at the extraordinary general meeting of the Company on 7 August 2006 and the disposal was completed on 8 September 2006. Further details of the disposal were set out in the Company's announcements dated 23 June 2006 and 9 November 2006 respectively.

Liquidity and Financial Resources

The Group's principal financial instruments comprise bank loans, factoring, 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 lowest cost possible.

The cash and bank balances as at the year end amounted to HK$1,905 million, of which 20% in US Dollars, 59% in Renminbi, 11% in Euro and 10% 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 year end.

At the year end, the Group's gearing ratio was 64.83% which is calculated based on the Group's net borrowings of HK$1,038 million (calculated as total interest-bearing borrowings less cash and bank balances) and the equity attributable to equity holders of the parent of HK$1,601 million.

Pledge of Assets

At 31 December 2006, certain of the Group's buildings with a net book value of approximately HK$93 million, inventory of HK$53 million and certain time deposits of HK$10 million were pledged to secure general banking facilities granted to the Group.

Capital Commitments and Contingent Liabilities

At 31 December 2006, the Group had capital commitments contracted but not provided for and authorized but not contracted for of approximately HK$0.2 million and HK$2.5 million respectively. Guarantees given in lieu of utility and rental deposits amounted to approximately HK$1.5 million.

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 25,146 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 135,420,000 shares remained outstanding at the year end.