

TO OUR SHAREHOLDERS

The financial year ended 31 March 2002 was one of the most challenging in the history of AV Concept Group. Unprecedented weakness in the global electronics market and across the board uncertainties in customer demands have affected most segments of the Group's businesses.

For the first time in the history of the Group since its establishment in 1980, the Group reported a loss attributable to shareholders.

During the year under review, turnover rose by 8.6% to HK\$1,194 million. Nonetheless adverse market conditions, in particular in the second half of the financial year, have caused the Group's gross profit for the year ended 31 March 2002 to fall by 36% to HK\$62,335,000.

One-off charges relating to non-operating expenses and impairment of goodwill and fixed assets has rendered a loss attributable to shareholders of HK\$52,340,000. Profit attributable to shareholders for the year ended 31 March 2001 amounted to HK\$16,127,000.

BUSINESS REVIEW

Marketing and Distribution

Cyclical downturn of the semiconductors industry and the slowdown of the US economy have affected the Group's profitability of its semiconductors distribution business.

During the year under review, turnover from the distribution of semiconductors fell 6.4% to HK\$880,897,000 (2001: HK\$ 941,086,000).

Distribution of semiconductors in Hong Kong recorded a steady growth in turnover of 9.2% during the year. Nonetheless, such growth was offset by a 53.7% reduction of turnover of semiconductors distribution in Singapore. Thus resulting in an overall decline in turnover for the business segment.

Semiconductors distributed in Singapore are mainly supplied to multinational customers for applications in mobile telecommunications and computer peripherals. These products were amongst the hardest hit during the financial year.

Management has taken positive steps in re-engineering its Singapore operation through a series of cost cutting measures, re-alignment of sales and marketing efforts and active promotions to industrial and consumer electronics customers.

Chairman's Statement

Management is confident that solid steps being taken now will ensure a speedy return to profitability in the anticipated market turnaround in the forthcoming financial year.

Turnover for semiconductors distribution in Hong Kong market increased by a modest 9.2%. The Group's customers in Hong Kong and China are less affected by the cyclical downturn in the semiconductors and the computer related industries. Nonetheless the slowdown of the worldwide economy has dampened overall demand for semiconductors from Hong Kong manufacturers. Gross profit margin fell in line with prevailing market conditions.

Against a background of falling demand, the Group was able to maintain and grew its market share in Hong Kong. Much tribute went towards our relentless sales team and strong support from our principal suppliers, Samsung Electronics and Fairchild Semiconductors.

Design and Manufacture

For the year ended 31 March 2002, turnover from the Group's design and manufacture operation rose 97.2% to HK\$313,568,000 (2001: HK\$158,994,000). The growth was primarily attributable to the manufacture of the Group's award winning iMP products.

Since the first launch of the iMP product in the last quarter of 2000, the product has continued to rejuvenate itself through continuous firmware upgrades and new models introduction. The many awards and public interest generated by the product has turned into solid revenue for the Group and a substantial market share in the CD/MP3 discman market in the United States, Europe and Korea.

The Group's iMP products are firmly established as the market leaders and demand for the products are strong as ever. The hard facts remain that competition in this market segment has intensified over the past year and the gross profit margin in the manufacture of the iMP products declined. Particularly in the second half of the financial year where the US channel sales customers were postponing delivery of previously ordered products or accepting the products at a discount to the previously agreed prices.

Turnover for the manufacture of other non-iMP OEM products fell during the year as demand for Internet appliances and other electronic products was weak.

While manufacturers are seeking for signs of an imminent and sustained recovery in the US to relieve the current adverse market environment, management of the Group has taken a more practical and pragmatic approach.

The Group recognises the importance of product technology and engineering expertise in maintaining its market leading position in the iMP products. It also recognises the importance of maintaining reasonable profitability and return on investment in the iMP products. While the Group continues to invest in in-house engineering and development of new generation of iMP products. More capital intensive product development projects are being out-sourced. Stringent cost control measures have been implemented in all areas of the design and manufacture operation.

Through advanced engineering and higher level of integration, the new iMP models being rolled out in the financial year 2002/2003 carry lower material costs and improved profit margin. With established product quality and reputation, the management is confident that the new generation of iMP products will be well received by the market.

A renewed emphasis has been placed on the non-iMP OEM business. Pilot production for a number of new OEM projects, including advanced CCD camera systems and commercial IP-telephones, are currently running at the factory. These projects are expected to commence mass production in the third quarter of the financial year 2002/2003. These products require a high standard of manufacturing and engineering skills and carry a higher profit margin. These projects will materially improve the profitability of the overall manufacturing operation from the third quarter onwards.

Associates

On 31 August 2001, the Group's interest in Reigncom Limited ("Reigncom"), an associate of the Group and design house behind the iMP product, was diluted from 20.0% to 19.4%. The dilution was due to the issue of new shares by Reigncom to its employees association, whose beneficiaries are present employees of Reigncom. The issue of shares was an incentive to reward the employees for their dedication and to further promote the sense of ownership amongst Reigncom's employees.

Reigncom ceased to become an associate of the Group and has been reclassified as a long term investment. The Directors believe the issue of shares to the employees association was made for the long term benefit of Reigncom and the reduced equity interest does not change the strategic partnership between the Group and Reigncom in the development and the manufacture of the iMP products in the foreseeable future.

Chairman's Statement

CURRENT PERFORMANCE AND PROSPECTS

Today, as many people continue to search for evidence of a sustained recovery in the US and elsewhere, it would not be prudent to present anything other than the facts that we have on the current business conditions of the Group.

In this respect, the signs are encouraging. For the first quarter in the financial year 2002/2003, the Group's overall profit margin has improved and recorded an encouraging net profit attributable to shareholders for the quarter.

On 3 June 2002, the Group completed a one for two rights issue. The rights issue was 54% oversubscribed and raised HK\$29,400,000, net of expenses, for working capital for the Group.

Overall, we continue to view our business as possessing a strong competitive position in the market place and would expect a recovery in the global economy to result in a significant improvement in AV Concept Group's financial performance.

On behalf of the Board, I would like to thank all our customers, shareholders, financiers, suppliers and employees for their continued support.

On behalf of the Board

So Yuk Kwan

Chairman

Hong Kong

26 July 2002