

Management Discussion and Analysis

BUSINESS REVIEW

Overview

The consolidated turnover and profit of the Group for 2003 were primarily derived from the following subsidiaries:

Name of subsidiary	Percentage of equity held by the Company	Principal activities
Shenzhen Tian Ma Microelectronics Co., Ltd. ("Tian Ma")	59.85%	Manufacture and sale of liquid crystal displays and modules (LCD & LCM)
Shenzhen Shennan Circuit Ltd. Corp. ("Shennan")	95.00%	Manufacture and sale of printed circuit boards (PCB)
Shenzhen Fiyta Holdings Limited ("Fiyta")	52.24%	Manufacture and sale of mid-to high-end timepieces

In 2003, the Group recorded a consolidated turnover of approximately RMB1,181,009,000, representing an increase of approximately 41.24% over the previous year. The overall gross profit posted approximately RMB283,965,000, an increase of 39.13% over the previous year. The Group's consolidated profit attributable to shareholders (after minority interests) amounted to approximately RMB44,776,000, compared with a loss of approximately RMB60,548,000 in the previous year.

Management Discussion and Analysis

The analysis of the Group's turnover and contributions to profit for 2003 by principal activities with the comparative figures for 2002 are as follows:

Turnover by activities	2003	2002
LCD	53.66%	39.17%
PCB	22.98%	25.85%
Timepieces	17.64%	18.12%
Other activities	5.72%	16.86%
Total	100%	100%

Contributions to profit by activities (before allocation of expenses to respective segments)	2003
LCD	51.89%
PCB	45.50%
Timepieces	5.93%
Other activities	-3.32%
Total	100%

Note: Contributions to profit by activities in 2002 cannot be calculated owing to a loss in the Group's overall results for that year resulting from LCD and Timepieces businesses having made a provision of RMB60,000,000 and RMB78,247,000 respectively.

LCD

Turnover for the Group's LCD & LCM operation was approximately RMB633,780,000 for the year 2003, representing a 93.48% increase over the previous year. Net profit (after minority interests) recorded approximately RMB34,020,000, compared with a loss of RMB26,663,000 in the previous year.

During the year, the Group's mobile phone display module products made a market breakthrough by obtaining batches of orders from domestic mobile phone manufacturers, and sales witnessed rapid growth quarter by quarter, making it the major growth driver for LCD & LCM operations of the Group. Sales revenue for LCM surged 216% over the previous year, with ratio to sales growing to 72%, compared with 53% in the same period of the previous year. Overall sales in the LCD & LCM operations as a whole has nearly doubled over that of the previous year, with substantial improvement in profitability.



Management Discussion and Analysis

The color STN-LCD production line invested by the Group was completely built during the year, and was, in the second half of the year, successfully put into batch production for monochromatic STN-LCD, as well as trial production of color STN-LCD on a small scale. Moreover, the Group has achieved critical progress in respect of research and design of color STN-LCD modules, as demonstrated by launches of several finalized new products. In response to rapid growth in mobile phone display module operations, the Group has also expanded its color STN-LCD module production lines and completed technical tests.

During the year, the Group strengthened R&D for LCD modules, aiming to meet the ever up-climbing product design requirements from customers through exploiting its LCD development potential and opportunities. The Group's mobile phone monochromatic LCD module program was honored with a Science and Technology Progress Award conferred by the Shenzhen Municipal Government during the year.

Gross Profit Margin

	2003 <i>RMB'000</i>	2002 <i>RMB'000</i>	2001 <i>RMB'000</i>
Sales income	633,780	327,574	283,202
Cost of sale	494,385	254,242	232,576
Gross profit	139,395	73,332	50,626
Gross profit margin	21.99%	22.39%	17.88%

Market Structure

	2003	2002	2001
PRC:	60%	30%	33%
Guangdong province	13%	15%	20%
Other regions	47%	15%	13%
Hong Kong	13%	25%	35%
Europe and America	27%	35%	30%
Southeast Asia	—	10%	2%
Total	100%	100%	100%

Management Discussion and Analysis

Product Structure

	2003	2002	2001
Telecommunications equipment	69%	23%	28%
Electrical household appliance	6%	23%	26%
Apparatus and devices	25%	46%	41%
Electronic games machines	—	8%	5%
Total	100%	100%	100%

PCB

Turnover for the PCB operations of the Group for the year was approximately RMB271,449,000, representing a 25.60% increase over last year, and net profit (after minority interests) increased by 9.23% over the previous year to approximately RMB29,835,000.



In the year, investment in domestic telecommunication facilities was in recovery. According to the statistics published by Chinese Ministry of Information Industry, investment in domestic telecommunication infrastructure increased 8.6% in 2003 (compared to a decrease of 20.0% in 2002). Investment in the mobile telecommunication facilities such as CDMA and PAS (Personal Access Phone System) grew even faster. The Group made a market hit in a timely manner as was evidenced by an increase of more than 30% in PCB orders for the year. The Group also endeavored to improve the customer structure of its PCB operations, and has achieved a more rationalized customer structure, though its major customers were still concentrated within domestic telecommunication equipment manufacturers.

The Group's PCB output for the year was approximately 194,000 sq. m., jumping by 32% over the previous year. The proportion of sales revenue for higher value-added Multi-layered PCB in this period has been further enhanced to 87% (compared to 82% in the previous year). Thanks to the Group's efforts with respect to optimization of the operating process and cost control, the gross profit margin of PCB operations remained 21% for the year, nearly unchanged from that of the previous year, despite of an average 8% decrease in price of multi-layered boards of PCB operations in the year. However, due to the rescission of the VAT incentive policy in Shenzhen with effect from 1st January, 2003, the Group has recorded an increase of merely 9.23% in the overall profit over the previous year (The Group's PCB operations received a VAT refund of RMB12,002,000 in the year 2002).

Management Discussion and Analysis

Within this period, with the expansion of PCB production capacity, the Group was committed to achieving an internal balance of crucial operating process and the optimization of the business process, so as to further increase productivity and shorten the product delivery cycle. The Group's research and development on PCB operations have also accomplished achievements, such as high-frequency multi-layered PCB made from blended and pressed materials, which was awarded the achievement appraisal by Shenzhen Municipal Science & Technology Bureau.

Gross Profit Margin

	2003	2002	2001
	RMB'000	<i>RMB'000</i>	<i>RMB'000</i>
Sales income	271,449	216,129	237,252
Cost of sale	212,513	170,355	169,051
Gross profit	58,936	45,744	68,201
Gross profit margin	21.71%	21.18%	28.75%

Market Structure

	2003	2002	2001
PRC	91.81%	88.04%	89.82%
Europe and America	7.33%	7.18%	1.38%
Southeast Asia	0.86%	4.83%	8.80%
Total	100%	100%	100%

Product Structure

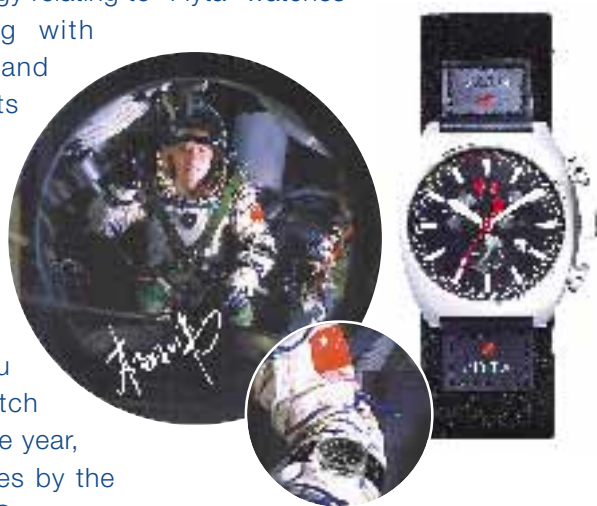
	2003	2002	2001
Telecommunications equipment	84.72%	86.48%	79.46%
Electronic devices	7.67%	3.59%	15.17%
Others	7.61%	9.93%	5.37%
Total	100%	100%	100%

Management Discussion and Analysis

TIMEPIECES

Turnover for the Group's timepieces operation was approximately RMB208,303,000, representing an increase of approximately 37.47% over the previous year. Net profit (after minority interests) was approximately RMB3,889,000, compared with a loss of RMB30,988,000 in last year.

The Group persisted with its brand building strategy relating to "Fiyta" watches and "Harmony" chain stores. Cooperating with professional branding consulting companies and advertising companies, the Group adjusted its marketing strategy and enhanced the promotion of these brands. Despite of the severe impact brought on by the SARS in 2003, sales income from timepieces operations in the year still recorded an impressive growth. On 15th December, 2003, the first space watch in China made by the Group, accompanying the Shenzhou 5 on its space launch, becomes the third watch brand used by astronauts in the world. During the year, the Group's "Fiyta" watches were awarded prizes by the Guangdong Provincial and Shenzhen Municipal Governments as "China Famous Brand Products".



In the year the gross profit margin of the Group's timepieces operation basically remained healthy due to endeavors to adjust business structure and sales strategy. However, the profitability of the Group's timepieces operations was affected by the termination of the VAT incentive policy with effect from 1st January, 2003. (The Group's timepieces operations gained a VAT refund of approximately RMB4,947,000 in the year 2002).

During the year, the number of the Group's "Harmony" timepiece chain stores reached a total number of 18.

Management Discussion and Analysis

Gross Profit Margin

	2003 RMB'000	2002 RMB'000	2001 RMB'000
Sales income	208,303	151,524	161,593
Cost of sale	133,928	96,180	102,304
Gross profit	74,375	55,344	59,289
Gross profit margin	35.71%	36.52%	36.69%

	2003	2002	2001
The gross profit margin of high-end timepieces	50.70%	59.66%	52.18%
The gross profit margin of low-to middle-end timepieces	15.14%	16.74%	29.75%

PROSPECT FOR 2004

The Group is optimistic about the prospects for its main businesses in 2004.

Although overshadowed by the outbreak of SARS during the first half of 2003, China's GDP still managed to increase 9.1% over the previous year, and CPI also got out of the deflation trap, indicating that there will be a new round of robust economic growth. In 2004, China's economy is expected to maintain a relatively high growth. Driven by the rapid growth of the domestic economy, as well as global electronic manufacturers shifting their production bases to the Chinese mainland, new business opportunities continue to be brought to China. It is very likely that the Group will continue to maintain rapid growth in its core electronic businesses.

Management Discussion and Analysis

LCD

In 2004, the Group will continue to focus on the high-demand mobile phone LCD module market. According to statistics from Chinese Ministry of Information Industry, Chinese domestic production of mobile phones exceeded 170 million in 2003, representing a 30% increase over the previous year. The market share for local manufacturers further rose. Based on the advantages of price, quality and services, it is expected that the LCD business of the Group will further expand its market share. The domestic production of color-screen mobile phones is expected to become the mainstream in 2004, and color STN-LCD and its module production lines will be fully put into batch production, and are likely to contribute to the sales income and profit growth for the Group.

In 2004, the Group will enhance the design capability of LCM products, in order to successfully meet LCM product orders and deliver finished products on time. Meanwhile, it will also strengthen quality control and cost control during the whole production process and further expand into new markets to achieve a sustained growth. The Group believes that its LCD & LCM operations will have positive development prospects should there be no dramatic changes in the business environment.

PCB

According to statistics from China PCB Association, the Chinese mainland has become the second largest region following Japan for PCB production in 2003, with production value exceeding US\$6 billion.

Domestic PCB industry is expected to maintain rapid growth in 2004, which will benefit the development of the Group's PCB business. However, it has to face many challenges as price competition becomes more keen, product update accelerates and delivery cycle shortens. The PCB business of the Group has established a good customer base within the field of communication facilities in the domestic market, based on our quality, technology and industrial R&D experience accumulated over the years. If 3G mobile business is launched in China during the year, it will be a positive driver for the PCB business of the Group.

In 2004, the Group will further reinforce the technology and quality advantages of its high-end PCB products, optimize customer structure and product structure and keep on optimizing operating process and balance production capability of the key production procedure and shorten response time to customers so as to enhance the Group's competitiveness. Moreover, the Group will pay close attention to the development of the PCB industry and look for new growth opportunities.

Management Discussion and Analysis

TIMEPIECES

No significant change is expected in the domestic timepieces industry in 2004. However, the zero tariff arrangement of CEPA has taken effect on 1st January, 2004, and Hong Kong timepieces brands will be taking the opportunity to enter the domestic market, which may affect the timepieces business of the Group.

In 2004, the Group is going to persist on its brand strategy, continue to enhance R&D and market operation capability, and strengthen its leading position as the first brand in domestic timepieces industry through maintaining and enforcing the brand image of “Fiyta”. Meanwhile, the Group will speed up the process of establishing “Harmony” chain stores and set up new shops in major large and medium cities and expand its scopes throughout the country, and try to develop brand name agents.

FINANCIAL REVIEW

Capital Structure

	2003	2002
	RMB'000	RMB'000
Total loans	347,277	377,804
Total liabilities	714,810	646,837
Minority interests	549,964	523,957
Shareholders' equity	1,196,878	1,152,102
Total assets	2,461,652	2,322,896
Loan-to-equity ratio	29.02%	32.79%
Debt-to-equity ratio	59.72%	56.14%

Loan-to-equity ratio – total loans at the year end/shareholders' equity at the year end.

Debt-to-equity ratio – total liabilities at the year end/shareholders' equity at the year end.

Management Discussion and Analysis

Liquidity and Capital Resource

As at 31st December, 2003, the Group had cash and bank deposits approximately totaling RMB230,881,000, which was mainly derived from the following sources:

- Cash and bank deposits at the beginning of the year;
- Revenue from operations.

As at 31st December, 2003, The Group's bank loans, approximately totaling RMB347,277,000, were all short-term borrowings with annual floating interest rates ranging from 1.88% to 5.84% (5.36% to 6.44% in 2002).

Capital expenditure of the Group in 2003 amounted to approximately RMB253,280,000, of which approximately RMB102,744,000 was applied for technical renovation of color STN-LCD production lines and expansion of color LCD module production lines, approximately RMB11,429,000 was applied for the purchase of additional PCB production equipment, approximately RMB66,583,000 was applied for the purchase of CATIC plant and Composite building in South Sha He Industrial Zone and its renovation for PCB operations, approximately RMB71,961,000 was applied for the newly established chain stores of Harmony Worldwide Timepieces Center for timepieces operations and the construction project of Fiyta Technology Mansion in Shenzhen High-tech Zone, and another RMB563,000 was invested in other projects.

The Group's capital expenditure in 2004 is estimated to be approximately RMB221,210,000, of which approximately RMB45,000,000 will be used for the expansion of color LCD module production lines and construction of staff dormitory, approximately RMB27,600,000 will be used for the purchases of additional production equipment for the PCB operations, approximately RMB32,000,000 will be invested in the newly established chain stores of Harmony Worldwide Timepieces Center, approximately RMB100,000,000 will be invested in the construction of Fiyta Technology Mansion in Shenzhen Hi-tech Zone, and approximately RMB16,610,000 will be invested in other projects. The proposed capital expenditure will be financed by bank deposits and the cash generated from the Group's operations.

Management Discussion and Analysis

OTHER SIGNIFICANT EVENTS

Shennan's Acquisition of Property in South Xiao Sha He Industrial Area

On 24th March, 2003, Shennan, a subsidiary owned as to 95% by the Company, and CATIC Shenzhen Company ("Shenzhen CATIC"), the ultimate holding company of the Company entered into an agreement ("the acquisition") regarding the acquisition of the land lot no.T309-30 located at Qiaocheng East Industrial Zone, Xiao Sha He Area, Nanshan District, Shenzhen, Guangdong Province with the structures erected thereon ("Properties in South Xiao Sha He Industrial Area") at the cash consideration of RMB67,080,000. The acquisition constituted a connected transaction under Chapter 14 of the Listing Rules and had obtained the approval by independent Shareholders in the extraordinary general meeting of the Company held on 31st May, 2003. In view of the fact that the tax policy on Shenzhen property transaction has been changed during the transaction period, after mutual negotiation, Shenzhen CATIC has agreed to readjust the cash consideration of Shennan's acquisition to RMB65,408,000. The transaction has been completed within this reporting year.

Follow-up of Provision on Tian Ma's Government Bond Investment

Tian Ma, a subsidiary 59.85% owned by the Company, made provision for the total principal amount of RMB60,000,000 of unredeemed Chinese government bonds, which Tianma had entrusted Dalian Securities Limited ("Dalian Securities") to purchase. On 25th June, 2003, the Dalian Intermediate People's Court ("Dalian Intermediate Court") of Liaoning Province, PRC, handled the case of an application for a bankruptcy declaration with respect to the Clearance Team of Dalian Securities in accordance with related laws, and rules on the procedure for Dalian Securities to enter into the bankruptcy and repayment procedures. Tian Ma has completed an application for creditor registration after the receipt of the Creditor Application Notice issued by Dalian Intermediate Court in 15th July, 2003.