Management Discussion and Analysis on Financial Conditions and Operating Results

The Group's production base is located at Changzhou, Jiangsu, the PRC. Its major operating subsidiaries include Galaxy Electrical, Galaxy Semiconductor, Galaxy Technology, Galaxy Micro-Electronics and Galaxy Hi-New.

Operating results for the year ended 31st December 2006 were as follows:

	Year ended 31st December			
	2006	2005	Increase/ (Decrease)	% of Change
	RMB'000	RMB'000	RMB'000	%
Turnover	336,562	252,826	83,736	33.12
Gross profit	73,408	66,058	7,350	11.13
Operating profit	44,312	43,025	1,287	2.99
Listing expenses	9,690	—	9,690	100.00
Profit before taxation	34,622	43,025	(8,403)	(19.53)
Profit for the year	29,055	39,063	(10,008)	(25.62)
Items attributable to:				
Equity holders of the Company *(Note)*	30,202	39,414	(9,212)	(23.37)
Minority interests	1,147	351	796	226.78

Note:

For illustration purposes, profit attributable to equity holders of the Company increased approximately 1.22% to approximately RMB39,890,000 excluding once off listing expenses which has been charged to the profit and loss account (31st December 2005: approximately RMB39,410,000).

	Note	Year ended 31st December 2006	2005
Net cash	1	(31,955)	(25,921)
Net assets	2	221,813	112,367
Liquidity ratio	3	164.17%	137.06%
Inventory turnover (number of days)	4	128 days	107 days
Accounts receivable turnover (number of days)	5	119 days	123 days
Accounts payable turnover (number of days)	6	106 days	137 days
Earning interest multiple	7	12.96 times	24.57 times
Capital liabilities ratio	8	39.35%	47.99%

Note:

1. Cash at bank and cash in hand – bank loans
2. Total Assets – Total Liabilities
3. Current Assets / Current Liabilities x 100%
4. Inventories / Cost of Sales x 365 days
5. Accounts Receivable and Bills Receivable / Turnover x 365 days
6. Accounts Payable and Bills Payable / Cost of Sales x 365 days
7. Profit before interest and tax / net interest expense
8. Interest bearing loans and other borrowings / Equity x 100%

Turnover

Turnover for the year ended 31st December 2006 amounted to approximately RMB336,560,000 as compared with the turnover amounted to approximately RMB252,830,000 of the previous year, representing an increase of approximately 33.12%.

Analysis of the Group's turnover by geographical and product types were as follow:

By geographical region

	Year ended 31st December					
					Increase/(Decrease)	
	2006		2005		% of Change	
	RMB'million	%	RMB'million	%	RMB'million	%
China *(Note 1)*	287.20	85.33	214.02	84.65	73.18	34.19
Hong Kong and Korea *(Note 2)*	27.47	8.16	27.44	10.85	0.03	0.11
Other countries and regions *(Note 3)*	21.89	6.51	11.37	4.50	10.52	92.52
Total	336.56	100.00	252.83	100.00	83.73	33.12

Note:

1. The PRC is the major market for the Group's products. The Group leverages on the advantages of its own brand name and product quality. As at 31st December 2006, the Group had over 1,200 customers in the PRC.

2. Korea and Hong Kong are the major overseas markets for the Group's products. Sales in the Korean and Hong Kong markets continued to grow due to the Group's participation in exhibitions in overseas regions such as Korea and Hong Kong and our efforts in the exploration of commercial opportunities. During the year, the Group has succeeded in winning international brand name customers in Korea.

3. Other countries and regions include Thailand, Taiwan, US, Italy, Canada, Germany, Spain and France. Sales in these countries and regions continued to grow due to the Group's efforts in exploring other overseas markets through commercial advertisements and participations in exhibitions.

Turnover by product type

	Year ended 31st December					
	2006		2005		Increase/(Decrease) % of Change	
	RMB'million	%	RMB'million	%	RMB'million	%
Plastic packaged diodes *(Note 1)*	270.95	80.51	204.47	80.87	66.48	32.51
Glass packaged diodes *(Note 2)*	14.97	4.45	18.12	7.17	(3.15)	(17.38)
Bridge rectifiers *(Note 3)*	10.45	3.10	9.33	3.69	1.12	12.00
Surface mount device packaged diodes *(Note 4)*	40.05	11.90	20.39	8.06	19.66	96.42
Others *(Note 5)*	0.14	0.04	0.52	0.21	(0.38)	(73.08)
Total	336.56	100.00	252.83	100.00	83.73	33.12

Note:

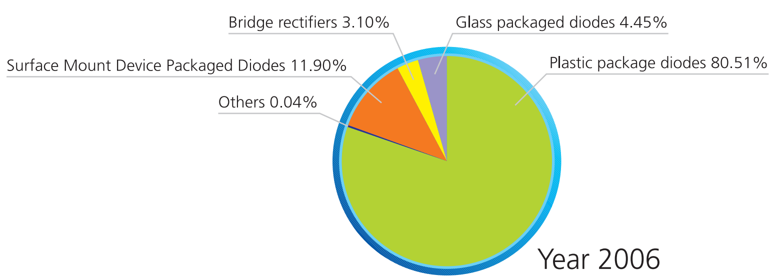
1. Plastic packaged diodes are the Group's major products. For the year ended 31st December 2006, the Group continued to expand its production capacity, adjust its product mix and increase its product range to satisfy increasing customers' demands. As a result, sales of plastic package diodes grew more than 30% while its proportion to total turnover declined.

2. Glass packaged diodes are products which contribute lower gross profit margins. As the Group mainly focuses on the production and sale of higher gross profit margin products, its sales and the proportion in total sales for the year ended 31st December 2006 decreased compared with that of the year ended 31st December 2005.

3. With the expansion in the production of bridge rectifiers which met customers' requirements, there was a slight growth in such sales.

4. Surface mount device packaged diodes are miniaturized diodes which the Group focused on developing. By achieving expansions in our customer base, sales of the Group's products grew rapidly during the year ended 31st December 2006.

5. Others refer to processing fees received from other factories for the processing of mono-crystal silicon into wafers.



Cost of sales

Cost of sales include raw materials, wages, water, electricity, gas and other ancillary materials. Cost of sales for the year ended 31st December 2006 represented 78.19% of the turnover, compared with approximately 73.87% for the year ended 31st December 2005, representing an increase of approximately 4.32%. This was mainly due to an increase in the cost of the Group's major raw materials (copper wire and silicon). Copper wire and silicon accounted for approximately 27.88% (2005: approximately 23.90%) and approximately 20.80% (2005: approximately 18.75%) respectively for the year ended 31st December 2006. In 2006, average purchase prices of copper wire and silicon increased by approximately 46.89% and 55.27% respectively as compared with 2005.

The turnover of the Group inceased by 33.12% while the cost of sales increased by 40.90% for the year ended 31 December 2006 as a result of the cost of raw material increased as discussed above.

Gross profit

The Group's gross profit margin for the year ended 31st December 2006 was approximately 21.81%, representing a decrease from 26.13% for the year ended 31st December 2005. This was due to increase in the cost of sales. The Group strives to produce and sell products with high gross profit margin by adjusting the product portfolio of the Group in order to reduce the impact from cost increases in major raw materials.

Other operating income

Other operating income mainly comprised of income generated by the sale of sub-products (2006: approximately RMB3,110,000; 2005: approximately RMB2,480,000), interest income from bank deposits (2006: approximately RMB570,000; 2005: approximately RMB47,000), dividend received from available-for-sale investment (2006: approximately RMB384,000; 2005: approximately RMB382,000) and income recognized on write back of trade and other payables (2006: approximately RMB1,990,000; 2005: approximately Nil). Other operating income increased mainly due to increase in sales of scrap material, the recognition of the write back of trade and other payables and increase in interest income from bank deposits.

During the year, the Group's turnover increased by 33.12% as compared with the previous year. The sale of sub-products increased as a result of the increased in production capacity and the increase in price of sub-products as a result of the increase in price of copper.

Distribution costs

Distribution costs mainly included commission expenses for sales and distribution activities (2006: approximately RMB3,640,000; 2005: approximately RMB3,460,000), wages and salaries of sales personnel (2006: approximately RMB1,260,000; 2005: approximately RMB1,100,000) and transportation costs (2006: approximately RMB1,350,000; 2005: approximately RMB1,620,000).

Distribution costs for the year ended 31st December 2006 represented approximately 2.25% of the total turnover, showing a decrease when compared with 2.91% for the year ended 31st December 2005. The Group's turnover increased by 33.12% as compared with the previous year while distribution costs increased by only 2.77% as compared with the previous year. The main reason for the decrease was due to strengthened cost control by the Group and the decrease in the relative proportion of fixed cost following increase in turnover.

Administration expenses

Administration expenses mainly included wages, salaries and welfare expenses, bad debt provisions, depreciation of office equipment and entertainment expenses.

Administration expenses for the year ended 31st December 2006 amounted to RMB27,100,000, showing an increase when compared with RMB17,270,000 for the year ended 31st December 2005, which was mainly due to increase in the salaries and benefits of management staff, increase in provision for bad debt and other increases in general administrative expenses.

Salaries and benefits of management staff increased by approximately RMB2,100,000 (2006: approximately RMB9,690,000; 2005: approximately RMB7,590,000). The number of management staff and the amounts of salaries and benefits increased as a result of our efforts to strengthen corporate governance. With the growth in sales, the Group's entertainment expenses also increased by RMB240,000 (2006: approximately RMB2,080,000; 2005: approximately RMB1,840,000) and the corresponding increase in provision of bad debt of RMB1,140,000 (2006: approximately RMB2,030,000; 2005: approximately RMB890,000). Also, audit fee for the year amounted to RMB1,200,000 was charged to general and administrative expenses in current year while such amount was included in the caption of listing expenses in 2005. After the Company listed on the Stock Exchange, relevant listing expenses (including legal and other professional fees) increased by approximately RMB680,000. Due to the Group's expansion, other administration expenses increased correspondingly by approximately RMB4,470,000 (2006: approximately RMB11,420,000; 2005: approximately RMB6,950,000).

The Group's turnover increased by 33.12% as compared with the year 2005 while administrative expenses increased by 56.92% due to the increase in salaries and benefits, bad debt and other administrative expenses as discussed above.

Listing expenses

Listing expenses referred to once off expenses incurred for the listing which amounted to approximately RMB9,690,000, and had been charged to the profit and loss account.

Finance costs

Finance costs refer to interest expenses for short-term bank loans.

Interest expenses for the year ended 31st December 2006 was approximately RMB2,890,000, while those for the year ended 31st December 2005 were approximately RMB1,830,000. The Group's turnover increased by 33.12% compared with the year 2005 while the finance cost increased by 58.58%. The increase in finance costs was due to increased fund raising to finance operations. There was an increase in average bank loans for the year ended 31st December 2006 compared with the year ended 31st December 2005.

Diminution in the value of goodwill

The diminution in the value of goodwill amounted to RMB390,000 for the year ended 31st December 2005, being the diminution in the value of goodwill which arose from the acquisition of all the equity interest in Galaxy Electric (China) Company Limited ("Galaxy China") on 1st August 2005 by the Group. As Galaxy China mainly engages in the provision of administration and supportive services to the Group, and the Board has not formulated detailed business plans for Galaxy China, therefore the Board decided to write off the goodwill in that year.

Taxation

The effective tax rate increased from approximately 9.21% for the year ended 31st December 2005 to approximately 16.08% for the year ended 31st December 2006. The increase in effective tax rate was mainly due to the once off listing expenses of approximately 9,690,000 which was not allowed to be set off for tax purposes.

Net profit for the year

Due to the above reasons, net profit ratio dropped from 15.59% for the year ended 31st December 2005 to 8.97% for the year ended 31st December 2006.

Net current assets

With the improvement in the Group's capital structure and increase in operating cashflow, the net current assets of the Group as at 31st December 2006 amounted to RMB110,990,000 (31st December 2005: approximately RMB48,600,000).

Liquid Assets and Financing

With the net proceeds from the Listing of approximately HK$70,000,000, the balances of deposits at banks as at 31st December 2006 amounted to RMB33,050,000 whereas the balance on 31st December 2005 amounted to RMB7,780,000.

As at 31st December 2006, the total amount of borrowings by the Group was approximately RMB65,000,000, representing an increase of approximately RMB31,300,000 compared with the balance outstanding on the balance sheet date of the year 2005. The borrowings were all short term bank loans due within one year.

The Group mainly depends on the steady recurrent cashflows generated by its operations for the repayment of debts. With the total amount of net proceeds from the Listing, the Group's assets to liabilities ratio decreased to 43.81% as at 31st December 2006, while the assets to liabilities ratio as at 31st December 2005 was approximately 53.85%. That ratio was computed by dividing the Group's total liabilities with total assets.

As at 31st December 2006, all of the Group's borrowings were denominated in Renminbi, while approximately 90% of the Group's income was denominated in Renminbi, with about 10% denominated in Hong Kong dollars and US dollars. Most of the borrowings of the Group are fixed interest loans.

In March 2007, the Group has entered into a facility agreement with a syndicate of banks and financial institution for syndicated bank loans totaling HK$120,000,000. Since Renminbi has experienced an appreciation in 2006, the Board considered that the syndicated bank loans in Hong Kong currency will be favourable to the Group in 2007.

The Group has not exposed to any currency hedging facility for the year ended 31 December 2006 and up to the date of this report as the Board considered that the cost of any hedging facility would be higher than the potential risk of the costs incurred from currency fluctuation.

The overall treasury and funding policies of the Group were designed to control foreign exchange risk and interest risk of individual transactions.

Pledge of Assets

As at 31st December 2006, the Group had pledged assets in land and buildings with net book value of approximately RMB18,225,000 (31st December 2005: approximately RMB16,828,000) to secure bank credits advanced to the Group.

Contingent Liabilities

For the years ended 31st December 2005 and 31st December 2006, the Group did not have any major contingent liabilities.

Employees

As at 31st December 2006, the Group had about 2,400 full time employees (31st December 2005: 2,000 full time employees) in Hong Kong and China, including about 2,000 employees (31st December 2005: 1,700 employees) supplied by labor service companies who are responsible for management, administration and production works. During the year 2006, relevant employee costs (including directors' emoluments) was approximately RMB37,940,000 (2005: approximately RMB28,370,000). The Group ensures that employees' remuneration is competitive, and distribute bonus according to the general rules of our remuneration policy and the performance of employees.