CEC
中国电子
CHINA ELECTRONICS

CHINA ELECTRONICS
Corporation Holdings Company Limited
中國電子集團控股有限公司

Annual Report
2004

Contents

Chairman's Statement

Yang Xiaotang
Chairman

"Our core competence is the most important and effective element to win in the future."

Dear Shareholders,

I am pleased to announce the results of China Electronics Corporation Holdings Company Limited (the "Company") and its subsidiaries (collectively the "Group") for the year ended 31 December 2004 and the Group's future prospects.

Achievements in 2004

2004 was a year of major reform for the Company. On 24 September 2004, the Company completed the acquisition of the 65% equity interest in Shenzhen Sang Fei Consumer Communications Company Limited ("Sang Fei"). Upon completion, China Electronics Corporation ("CEC") has become the controlling shareholder of the Company. Leveraged on the new management team and the new business model, the Group has a more solid operating base and a proven steady cash flow. The management also brought major realignment to the Group's investment portfolio which involves the disposal of investment projects continuously recording operating losses or those which fall short of set targets. After the overall strategic reorientation of its business, not only did Sang Fei contribute profits to the Group, the new business also laid a solid foundation for the Group to further develop in consumer electronics and communications businesses – sectors which have promising potential in the coming future.

In light of the keen market competition creating a harsh business environment, the Group has focused in expanding its production capacity of the mid- to high-end handsets for the global market. In addition to the enhanced operation efficiency and cost control management, the Group recorded remarkable results in 2004. During the year under review, the Group sold approximately 8.4 million units of mobile phones, representing more than 57% increase over last year. Notwithstanding the stiff market competition from both local manufacturers and leading multinational industry players, the Group effectively capitalized on its know-how and technology in mobile phone manufacturing to offer products at

competitive prices. In addition to its reliable network of suppliers from different parts of the world and the well-implemented inventory control policies, the Group successfully achieved robust growth in sales volume as well as in its overall operating profitability.

I would like to extend my appreciation and attribute our success to you.

Outlook

The global consumer electronics and communication sector is expected to grow steadily, and the evolution in technology will continue at fast pace. 4C convergence (computer, communication, consumer electronics and content) and 3-net integration (communication network, cable television network and internet) will be the trend of future advancement in information technology. These provide the Group with plentiful business opportunities, and will be regarded as the direction of our future development. The management is confident with the prospect of the Group in the coming years.

Our core competence is the most important and effective element to win in the future. In 2004, the Group completed the business realignment and corporate reorganization with great success, and attained remarkable operating results during the year. This is, however, only the first step of our overall corporate strategy. Looking forward, the Group will endeavour to promote Sang Fei as a major mobile phone provider in the industry, and will proactively explore new business opportunities in consumer electronics and communication products and services.

At present, Sang Fei has the capability of producing GSM, CDMA and PHS mobile phones, and possesses the technology and expertise for the manufacture of 3G mobile phones and lead-free handsets. With the extensive experience and know-how it has gained, together with the continuous support from CEC, Sang Fei will continue to diversify its product profile and income source, and to improve the overall profitability as a whole.

Chairman's Statement

To drive quantum growth of its business, the management will implement dynamic development strategies. The Group will devote its resources in research and development, production and sales and distribution functions, and to establish a complete production chain in mobile communication products. In addition, the Group will actively explore and extend its business profile in the upstream and downstream of the consumer electronics and communication product chain, including the design and manufacture of proprietary chipsets, development of system platform and provision of network application and services. The Group will also expedite its business growth by actively pursuing new investment opportunities through strategic acquisitions or partnerships with good potential. Besides, the State Council has approved CEC early this year to set up the China Cable Network ("CCN") joint venture with China Media Group. Being the core operator of the cable television network, CCN will be engaged in the integration and development of the domestic cable television network and related service provision, including the high-definition television broadcasting in China. With the technological advantage of CEC and through maximizing the synergies between CEC and the Group, the management will further integrate, improve and expand the business profiles of the Group and creates a healthy, efficient and transparent corporate structure, and a comprehensive industry value chain and supply chain. Our ultimate objective is to advance the Group as a leading information technology, equipment manufacturing and network application services provider in China.

The management is ambitious towards achieving these goals and objectives. With the support from our shareholders, we are confident that the Group will carry the best performance in the coming years, which in turn maximize the shareholders value and investor return as a whole.

Acknowledgement

Last but not least, I would like to take this opportunity to express the Board's sincere gratitude to all shareholders and business associates for their continuous support and trust, and to all staff for their devoted efforts and contributions to the Group.

Sincerely yours,

Yang Xiaotang
Chairman

Hong Kong, 18 March 2005

Management Discussion and Analysis

Operational and Financial Review

Driven by the strong growth in the global economy, the worldwide mobile phone subscribers reached a total of 1.7 billion in 2004. According to the market researcher Strategy Analytics, the global sales of mobile phones in 2004 reached 684 million units. This represented a growth of 32% over 2003. Driving the growth was the surging market demand arising from handset replacements and trendy upgrades in the more matured markets, and the strong net subscriber growth in the developing regions like Brazil, Russia, India and China. China, in particular, has more than 330 million mobile users, representing 25% of the country's total population, out of which 64.87 million users are new subscribers in 2004. With the ongoing boom and widespread popularisation of 3G communication in 2005, the mobile phone market will continue to grow. Strategy Analytics forecasts 735 million units of mobile phones will be shipped in 2005.

Turnover

The results of the Group were encouraging. During the year under review, the Group sold approximately 8.4 million units of mobile phones, representing an increase of more than 3 million units over 2003. In terms of sales revenue, the Group achieved a turnover of HK$4,590.1 million; a remarkable increase of 60.4% as compared to the same period last year. The increase was contributed primarily from the strong market demand and the expansion of the production capacity of Sang Fei. Moreover, with the installation of the sixth and seventh SMA production lines in 2004, currently the Group has an annual production capacity of over 10 million units of mobile phones. The Group is well prepared towards the continuous growth in market demand in the future.

Philips branded

Sang Fei is the exclusive mobile phone manufacturer for the Philips group. The well-recognised *Philips* branded mobile phones in both China and overseas markets, together with the long-established relationship with the Philips Group, offer the Group a significant and sustainable source of revenue. During the year under review, the Group produced a total of 22 models of *Philips* branded mobile phones. The turnover from the *Philips* branded mobile phones increased by 59.9% to HK$4,149.4 million.

Management Discussion and Analysis

Own-branded and other OEM branded

Sang Fei actively sought to develop an independent customer base on an OEM/ODM basis as well as its own-branded mobile phones. During the year under review, the Group produced a total of 70 models of own-branded and other OEM branded mobile phones. The turnover from own-branded and other OEM branded mobile phones was HK$440.7 million, representing a growth of 65.1% over last year.

Cost of sales

The cost of sales increased by 60.8% to HK$4,352.6 million. The primary component of the cost of sales was raw material cost, which represented approximately 94.7% of the total cost. The increase in cost of sales was primarily attributable to the growth in turnover, and was because more expensive components were being utilized when additional functions and more advanced features, like high resolution camera modules, were built into the new mobile phones, which resulted in higher average production costs of the new products. Despite the general increase in the average cost of materials, the Group was successful in implementing global material sourcing channels which effectively minimize the impact on the overall production costs of the Group.

Profitability

The Group achieved a gross profit of HK$237.5 million, which was 53.3% over the gross profit earned in 2003. The gross margin of 2004 was 5.2%. As compared to 5.4% in last year, the decrease in gross profit margin was primarily due to the general increase in material cost and the stiff market competition which imposed margin pressure on the overall handset industry.

The operating profit of the Group in 2004 was HK$97.6 million, representing an increase of 37.7% over the same period last year. The operating profit margin was 2.1%. The increase in operating profit was largely attributable to the remarkable growth in the Group's sales turnover, effective cost controls and the strengthening of overall management control. With the effective implementation of these policies, the Group had laid a solid foundation for sustained profitability in the future.

The Company completed the acquisition of the 65% equity interest in Sang Fei on 24 September 2004. For accounting purpose, the acquisition has been accounted for as a reverse acquisition. Provision for impairment on the carrying amount of the goodwill at year ended of HK$61.5 million was fully made in the year under review. As a result, the Group recorded a net loss of HK$19.3 million and the loss per share was HK cents 0.27.

In a business' perspective and if the extraordinary loss from the impairment of goodwill is not taken into consideration, the Group would have earned a profit attributable to shareholders of HK$42.2 million during the year under review, which was 9.7% over that of 2003. The corresponding earnings per share was HK cents 0.6.

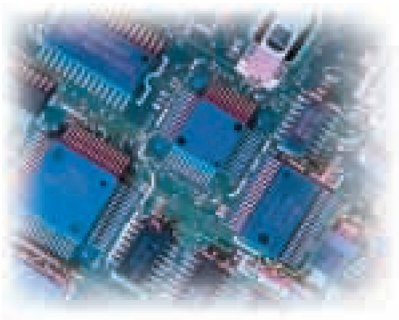
Capital Resources and Liquidity

The capital resources for the Group's operations were primarily generated from its operations and short term bank borrowings. As at 31 December 2004, the Group had net current assets of HK$371.2 million, representing an increase of 93.8% over those of the previous year. The overall gearing ratio, which is calculated as the total liabilities over total assets of the Group, was approximately 70.2% (2003: 79.5%).

As at 31 December 2004, the Group had cash and cash equivalents amounted to HK$217.4 million (2003: HK$23.4 million), and were primarily denominated in Hong Kong dollar, Renminbi and United States dollar.

The Group's exports sales are predominantly invoiced in United States dollar and its domestic sales are invoiced in Renminbi. The Group imports some of its raw materials and SMA and testing equipments from overseas suppliers, which are paid in United States dollar, 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.

Management Discussion and Analysis



Bank Borrowings

As at 31 December 2004, the Group had unsecured short term bank borrowings of HK$392.2 million (2003: HK$309.3 million). The bank borrowings were all denominated in Renminbi, and were borrowed at contracted fixed interest rate. As at 31 December 2004, the Group had available bank facilities of approximately RMB800 million.

As at 31 December 2003 and 2004, the Group did not have any pledged assets or guarantee.

Capital Commitment and Contingent Liabilities

As at 31 December 2004, the Group had contracted but not provided for capital commitment of HK$8.7 million (2003: HK$13.3 million) for the purchase of fixed assets and computer software.

The Group did not have any material contingent liabilities outstanding as at 31 December 2003 and 2004.

Employee and Remuneration Policies

As at 31 December 2004, the Group had approximately 2,650 employees (2003: 1,580), majority of them were based in China.

The Group recognizes 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 optimize 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.

Major Acquisition and Disposal

On 10 December 2003, the Company, CEC and Winsan International Holdings Limited, the then controlling shareholder of the Company, entered into a sale and purchase agreement to acquire CEC's 65% equity interest in Sang Fei, a Sino-foreign joint venture company established in the People's Republic of China (the "PRC") principally engaged in the manufacturing and sale of mobile phones, at a consideration of HK$260 million. The consideration was satisfied by the issuance of 6,500,000,000 shares of the Company at HK$0.04 per share.

The acquisition was completed on 24 September 2004. Upon completion of the acquisition and the placing of shares referred below, CEC was interested to 74.98% of the issued share capital of the Company, and became the controlling shareholder of the Company. The Company also changed its name from Winsan (China) Investment Group Company Limited to China Electronics Corporation Holdings Company Limited with effect from 28 September 2004.

As part of the business reorientation, the Company entered into agreements to sell the entire interests in the Transonline Group and DICO Group on 29 September 2004 and 11 October 2004 respectively to an independent third party for HK$1 each. As both groups of companies had been recording losses and were at net liabilities position, the dispose of the two groups of companies were at the interests of the Company as a whole.

Placing of Shares

On 17 September 2004, the Company entered into the placing agreements to place 420,000,000 shares and 190,000,000 shares of the Company to Wellful Holdings Limited and Ready Finance Limited respectively at HK$0.233 per share, raising a net proceed of HK$142.1 million. The placing of shares was completed on 24 September 2004. As at 31 December 2004, the unused proceed was HK$137.3 million and were reserved as the working capital of the Group and for future opportunistic investments by the Group.

Corporate Information

Board of Directors

Non-executive Directors

Mr. Yang Xiaotang *(Chairman)*

Mr. Tong Baoan *(Vice Chairman)*

Executive Directors

Mr. Fan Qingwu *(Managing Director)*

Mr. Hua Longxing

Independent Non-executive Directors

Mr. Chan Kay Cheung

Mr. Wong Po Yan

Mr. Yin Yongli

Company Secretary

Mr. Yam Pui Hung, Robert

Principal Bankers

Bank of China (HK) Limited

The Bank of East Asia, Limited

The Hongkong and Shanghai Banking Corporation Limited

Auditors

PricewaterhouseCoopers

Legal Advisors

As to Hong Kong Law:

Linklaters

As to Bermuda Law:

Conyers Dill & Pearman

Registered Office

Clarendon House
2 Church Street
Hamilton HM 11
Bermuda

Head Office and Principal Place of Business in Hong Kong

Room 908, 9th Floor
Sun Hung Kai Centre
30 Harbour Road
Wanchai
Hong Kong

Principal Share Registrar and Transfer Office

Butterfield Fund Services (Bermuda) Limited
Rosebank Centre
65 Front Street
Hamilton
Bermuda

Hong Kong Branch Share Registrar and Transfer Office

Abacus Share Registrars Limited
Ground Floor
Bank of East Asia Harbour View Centre
56 Gloucester Road
Wanchai
Hong Kong

Stock Code

0085

Biographies of Directors and Senior Management

Non-executive directors

Mr. Yang Xiaotang, aged 62, is appointed the Chairman of the Company in September 2004. Mr. Yang graduated from Yangzhou University, the PRC, and is also the president and legal representative of China Electronics Corporation ("CEC"), the ultimate holding company of the Company. Prior to joining CEC in 2001, he was the vice governor of the State Development Bank of China for 4 years. During 1992 to 1998, Mr. Yang was the deputy provincial governor of Jiangsu Province, and the general secretary of Suzhou City. Before that, he had been the deputy city mayor and thereafter the mayor of Changzhou City, Jiangsu Province during the period from 1988 to 1992. Before 1988, he was the vice president and subsequently the president of Jin Ling Petrochemical Corporation.

Mr. Tong Baoan, aged 57, is appointed the Vice Chairman of the Company in September 2004. Mr. Tong graduated from Tianjin University, the PRC, and is also the vice president of CEC. Prior to joining CEC in 2001, he was the general manager of Shenzhen Sang Da Electronics Corporation during the period from 1996 to 2001.

Executive directors

Mr. Fan Qingwu, aged 41, is appointed the Managing Director of the Company in September 2004. He is also a director of Shenzhen Sang Fei Consumer Communications Company Limited ("Sang Fei"). Mr. Fan graduated from the Renmin University of China in the PRC. From 1996 to 1999, Mr. Fan was the executive vice president of China Securities Industry Institute. After that, he was the general manager of the Investment Banking Department and the Asset Management Department of CEC until the year 2003. He is also currently the vice president of China Electronics Industry Corporation.

Mr. Hua Longxing, aged 63, is appointed an executive director of the Company in September 2004. He is also the chairman of the board of directors of Sang Fei. Mr. Hua graduated from the Faculty of Wireless Engineering of Southeast University in the PRC. From 1993 to 2000, Mr. Hua was the vice-chairman of the board of directors and the general manager of Shenzhen SED Industry Co., Ltd.. Before that, he was the deputy general manager of Shenzhen Sang Da Electronics Corporation. From 1983 to 1987, he was the director of the Liaison Division of the office of Ministry of Electronics Industry in Shenzhen Economic Zone.

Biographies of Directors and Senior Management

Independent Non-executive directors

Mr. Chan Kay Cheung, aged 58, is an executive director and deputy chief executive of The Bank of East Asia, Limited. He joined the bank in 1965 and possesses extensive knowledge and experience in the banking industry. Mr. Chan is a fellow member of the Hong Kong institute of Bankers and a member of the MPF Industry Schemes Committee. He is also an independent non-executive director of Chu Kong Shipping Development Company Limited and Four Seas Food Holdings Limited. Mr. Chan joined the Company in May 1997.

Mr. Wong Po Yan, aged 81, is the chairman and managing director of United Overseas Enterprises Limited and the chairman of the board of Asia Television Limited. Mr. Wong is the vice-chairman of the Basic Law Committee of Hong Kong Special Administrative Region, and was the chairman of the Airport Authority, a member of the Drafting Committee of Basic Law and a member of the Preparatory Committee of Hong Kong Special Administrative Region. He had been a member of the Legislative Council for 9 years. Mr. Wong joined the Company in May 1997.

Mr. Yin Yongli, aged 65, graduated from Shandong Finance Institute, the PRC. Mr. Yin is the chairman of China Rightson Certified Public Accountants/Huazheng Certified Public Accountants since September 2001. He was the chairman of another firm of auditors in the PRC for the period from 1998 to 2001. Before that, he spent over 35 years in the petrochemical industry in the PRC as an accountant of Sinopec Corporation. From the years 1985 to 1988, he became the chief accountant of the financial planning department. From 1988 to 1998 he was the deputy department head of the finance department. Mr. Yin joined the Company in September 2004.

Senior Management

Mr. Yam Pui Hung, Robert, aged 37, is the qualified accountant and company secretary of the Company. Mr. Yam is a certified public accountant of the Hong Kong Institute of Certified Public Accountants and a fellow member of the Association of Chartered Certified Accountants. Mr. Yam holds a bachelor's degree in accountancy and has extensive experience in accounting, financial management and corporate finance. Mr. Yam joined the Company in September 2004.

Directors' Report

The directors would like to present their report together with the audited accounts for the year ended 31 December 2004.

THE ACQUISITION

On 10 December 2003, China Electronics Corporation ("CEC"), the Company and the Company's then holding company, Winsan International Holdings Limited, entered into a sale and purchase agreement to acquire CEC's 65% equity interest in Shenzhen Sang Fei Consumer Communications Company Limited ("Sang Fei"), a Sino-foreign joint venture company established in the People's Republic of China principally engaged in the manufacturing and sale of mobile telephones (the "Acquisition"), at a consideration of HK$260,000,000. The consideration was satisfied by the issuance of 6,500,000,000 shares of the Company to CEC. The Acquisition was completed on 24 September 2004.

CHANGE OF COMPANY NAME

Pursuant to a special resolution passed at a special general meeting held on 14 July 2004, the name of the Company was changed from Winsan (China) Investment Group Company Limited to China Electronics Corporation Holdings Company Limited.

PRINCIPAL ACTIVITIES AND GEOGRAPHICAL ANALYSIS OF OPERATIONS

The Company is an investment holding company. The principal activities of the Group, upon the Acquisition, comprise the manufacturing and sale of mobile telephones. The principal activities of subsidiaries are set out in note 28 to the accounts.

Before the Acquisition, the Group was engaged in the operation of Transonline and DICO Group. The two businesses were disposed of on 29 September 2004 and 11 October 2004 respectively.

An analysis of the Group's performance for the year by business and geographical segments is set out in note 3 to the accounts.

RESULTS AND APPROPRIATIONS

The results of the Group for the year are set out in the consolidated profit and loss account on page 27 of the annual report.

The directors do not recommend the payment of a dividend for the year ended 31 December 2004 (2003: Nil).

FIXED ASSETS

Particulars of the movements in fixed assets of the Group and the Company during the year are set out in note 14 to the accounts.

Directors' Report

SHARE CAPITAL

Particulars of the movements in share capital of the Company are set out in note 21 to the accounts.

RESERVES

Particulars of the movements in reserves of the Group and the Company during the year are set out in note 22 to the accounts.

DISTRIBUTABLE RESERVES

As at 31 December 2004, the Company does not have any revenue reserve available for distribution to the shareholders (2003: Nil).

FINANCIAL SUMMARY

A summary of the results and of the assets and liabilities of the Group for the last five financial years is set out on page 67 of the annual report.

SHORT-TERM LOANS

Particulars of the short-term loans of the Group are set out in note 20 to the accounts.

BORROWING COSTS

No interest was capitalised by the Group during the year (2003: Nil).

DIRECTORS

The directors during the year and up to the date of this report were:

Non-executive directors

Mr. Yang Xiaotang	(appointed on 24 September 2004)
Mr. Tong Baoan	(appointed on 24 September 2004)
Ms. Chiu King Cheung	(resigned on 24 September 2004)

Executive directors

Mr. Fan Qingwu	(appointed on 24 September 2004)
Mr. Hua Longxing	(appointed on 24 September 2004)
Mr. Chan Chak Shing	(resigned on 24 September 2004)
Mr. Chan Hon Ching	(resigned on 24 September 2004)
Ms. Lo Mei Chun	(resigned on 24 September 2004)

DIRECTORS *(CONTINUED)*

Independent non-executive directors

Mr. Chan Kay Cheung
Mr. Wong Po Yan
Mr. Yin Yongli (appointed on 24 September 2004)

In accordance with section 86(2) of the Company's bye-laws, Mr. Yang Xiaotang, Mr. Tong Baoan, Mr. Fan Qingwu, Mr. Hua Longxing and Mr. Yin Yongli will retire at the forthcoming annual general meeting of the Company and, being eligible, offer themselves for re-election.

The Company has received confirmation from each of the independent non-executive directors as regards their independence to the Company, and considers them to be independent.

No director proposed for re-election at the forthcoming annual general meeting has a service contract, which is not determinable by the Group within one year without payment of compensation, other than statutory compensation.

BIOGRAPHICAL DETAILS OF DIRECTORS

Brief biographies of the directors of the Company are set out on page 11 of the annual report.

DIRECTORS' AND CHIEF EXECUTIVE'S INTERESTS AND SHORT POSITIONS IN SHARES, UNDERLYING SHARES AND DEBENTURES

As at 31 December 2004, no interests nor short positions in the shares, underlying shares or debentures of the Company or any associated corporation (within the meaning of Part XV of the Securities and Futures Ordinance (the "SFO")) of the Company were recorded in the register maintained by the Company pursuant to Section 352 of the SFO, or as otherwise notified to the Company and The Stock Exchange of Hong Kong Limited (the "Stock Exchange") pursuant to the Model Code for Securities Transactions by Directors of Listed Companies.

SHARE OPTION SCHEME

On 20 June 2002, the shareholders of the Company approved the termination of the share option scheme adopted by the Company on 5 July 1997 (the "Old Scheme") and the adoption of a new share option scheme (the "Share Option Scheme"). Accordingly, no options can be granted under the Old Scheme. Any outstanding options granted but not exercised under the Old Scheme shall continue to be exercisable.

Directors' Report

SHARE OPTION SCHEME *(CONTINUED)*

Summary of each of the Share Option Scheme and the Old Scheme are as follows:

Term	Share Option Scheme	Old Scheme
Purpose	To provide the participants with the opportunity to acquire proprietary interests in the Company and to encourage participants to work towards enhancing the value of the Company.	Not applicable
Participants	All executive and non-executive directors of the Company, full time employees and part-time employees of the Group, advisors, consultants, distributors, suppliers, agents, customers, partners, joint venture partners, promoters, service providers to the Group.	Any employees (including executive directors) of the Company or any of its subsidiaries.
Total number of ordinary shares available for issue and the percentage of the issued share capital that it represents as at the date of the annual report	111,320,000 ordinary shares and approximately 1.3% of the issued share capital as at the date of the annual report.	Not applicable
Maximum entitlement of each participant	1% of the shares in issue in any 12-month period	Not exceeding 25% of the total maximum number of shares available for subscription
Period within which securities must be taken up under an option	10 years from the business day on which board of directors resolves to make an offer of grant of options	10 years from the offer of the grant of option

SHARE OPTION SCHEME *(CONTINUED)*

Term	Share Option Scheme	Old Scheme
Minimum period for which an option must be held before it can be exercised	The Company must specify the minimum period at the time of grant of options	The Company must specify the minimum period at the time of grant of options
Amount payable on acceptance of the option	HK$1.00	HK$1.00 or its equivalent in RMB at the prevailing exchange rate at the time of offer
Period within which payments/call/ loans must be made/repaid	Not applicable	Not applicable
Basis of determining the exercise price	The higher of (i) the closing price of the shares as stated in the Stock Exchange's daily quotations sheets on the date of grant; (ii) the average closing price of the shares as stated in the Stock Exchange's daily quotations sheets for the 5 business days immediately preceding the date of grant; and (iii) the nominal value of a share on the date of grant	The higher of (i) the average closing price of the shares as stated in the Stock Exchange's daily quotation sheets for the 5 trading days immediately preceding the date of grant; or (ii) the nominal value of a share
Remaining life of the scheme	The scheme remains in force until 19 June 2012	The outstanding options shall remain exercisable up to 29 October 2010

During the year ended 31 December 2004, no options have been granted under the Share Option Scheme. No options have been lapsed nor exercised, but a total of 80,480,000 outstanding options under the Old Scheme have been cancelled due to the resignation of certain directors and employees during the year.

Directors' Report

SHARE OPTION SCHEME *(CONTINUED)*

As at 31 December 2004, there were no share options outstanding under the two share option schemes. Details of the share options outstanding during the year were as follows:

Name	Date of grant	Exercise price	Options as at 1 January 2004	Options cancelled during the year	Options as at 31 December 2004
		HK$	Number	Number	Number
Ex-Directors					
Mr. Chan Chak Shing	1/9/1997	1.530	16,000,000	(16,000,000)	–
	31/3/1998	0.360	11,500,000	(11,500,000)	–
	16/2/2000	0.240	2,300,000	(2,300,000)	–
Mr. Chan Hon Ching	1/9/1997	1.530	1,000,000	(1,000,000)	–
	31/3/1998	0.360	22,000,000	(22,000,000)	–
	16/2/2000	0.240	2,000,000	(2,000,000)	–
Ms. Lo Mei Chun	1/9/1997	1.530	600,000	(600,000)	–
	30/10/2000	0.173	1,000,000	(1,000,000)	–
Ms. Chiu King Cheung	1/9/1997	1.530	1,000,000	(1,000,000)	–
	31/3/1998	0.360	22,000,000	(22,000,000)	–
	16/2/2000	0.240	1,000,000	(1,000,000)	–
Employees					
Total employees	30/10/2000	0.173	80,000	(80,000)	–

As at 31 December 2004, no directors of the Company had any share options outstanding under the two share option schemes.

DIRECTORS' RIGHTS TO ACQUIRE SHARES OR DEBENTURES

Save as disclosed above, at no time during the year was the Company, its holding company or any of its subsidiaries or fellow subsidiaries a party to any arrangements to enable the directors of the Company or their respective associates (as defined under the Rules Governing the Listing of Securities on the Stock Exchange (the "Listing Rules") to acquire benefits by means of the acquisition of shares in, or debentures of, the Company or any other body corporate.

DIRECTORS' INTEREST IN CONTRACTS

No contracts of significance to which the Company, its holding company or any of its subsidiaries or fellow subsidiaries was a party and in which a director of the Company had a material interest, whether directly or indirectly, subsisted at the end of the year or at any time during the year.

CONNECTED TRANSACTIONS

Details of the connected transactions entered into by the Group during the year are set out below:

Continuing connected transactions

Type of transaction	**Amount**
	HK$'000
Sales of products, samples and materials to the CEC Group [(1)]	44,038
Purchases of raw materials from the CEC Group	8,052
After sales repair and maintenance services by the CEC Group	1,175
Provision of canteen services by the CEC Group	6,459
Fitment and decoration services from the CEC Group	5,065
Rental arrangement with the CEC Group	6,010
Processing arrangements with the CEC Group	6,364
Sales of products, samples and materials to the Philips Group [(2)]	4,162,127
Purchases of raw materials from the Philips Group	1,034,201
Corporate services arrangements with the Philips Group	15,535

Note:

(1) CEC Group, being China Electronics Corporation together with its subsidiaries, is a connected person of the Group by virtue of being the controlling shareholder of the Company.

(2) Philips Group, being Koninklijke Philips Electronics N.V. together with its group companies, is a connected person of the Group by virtue of being a substantial shareholder of Shenzhen Sang Fei Consumer Communications Company Limited, the principal operating subsidiary of the Group.

Directors' Report

CONNECTED TRANSACTIONS *(CONTINUED)*

Pursuant to the resolutions passed in the Company's special general meeting on 14 July 2004, and the written approval by CEC on 20 December 2004 in relation to the revision of the annual cap of the sales of products to the Philips Group, the above connected transactions were approved by the independent shareholders of the Company.

Brief description and particular terms of the continuing connected transactions are set out in note 27 "RELATED PARTY TRANSACTIONS" to the accounts in accordance with the requirements of Chapter 14A of the Listing Rules.

In the opinion of the independent non-executive directors of the Company, the above transactions were carried out in the ordinary and usual course of business, on normal and commercial terms and were in accordance with the relevant agreements governing them on terms that were fair and reasonable and in the interests of the Group and the shareholders as a whole.

The auditors have confirmed that the above transactions:

- had been approved by the board of directors of the Company;
- were in accordance with the pricing policies of the Group;
- were entered into in accordance with the terms of the relevant agreements governing such transactions; and
- had not exceeded the cap approved by the board of directors of the Company as described in the circulars of the Company dated 21 June 2004 and 31 December 2004.

DIRECTORS' INTERESTS IN COMPETING BUSINESS

During the year and up to the date of this report, the following directors of the Company are considered to have interests in businesses which compete or are likely to compete, either directly or indirectly, with the businesses of the Group:

Name of director	Name of entity	Principal business of the entity	Nature of director's interest in the entity
Mr. Yang Xiaotang	China Electronics Corporation *(note a)*	Investment holdings	President and legal representative
Mr. Tong Baoan	China Electronics Corporation *(note a)*	Investment holdings	Vice president
	China Electronics Industry Corporation *(note b)*	Investment holdings	President and legal representative
	Shenzhen SED Industry Co., Ltd. *(note b)*	Investment holdings	Chairman
Mr. Fan Qingwu	China Electronics Industry Corporation *(note b)*	Investment holdings	Vice president
	CEC Wireless R&D Co. Ltd.	Research and development of mobile telephones	Director

Note:

(a) China Electronics Corporation ("CEC") is the controlling shareholder of the Company. CEC is a state-owned nationwide electronics and information technology conglomerate, and has other subsidiaries and associates engaged in mobile telephone related businesses which compete or are likely to compete with the business of the Group.

(b) China Electronics Industry Corporation and Shenzhen SED Industry Co., Ltd. have subsidiaries or associates engaged in the mobile telephone related businesses which compete or are likely to compete with the business of the Group. China Electronics Industry Corporation is wholly owned by CEC. Shenzhen SED Industry Co., Ltd. is a company whose A shares are listed on the Shenzhen Stock Exchange and is indirectly owned as to approximately 55.34% by CEC as at the date of this report.

The abovementioned competing businesses are operated and managed by independent management and administration. In addition, the directors of the Company consider that the business model of and markets served by the Group are different from those companies. The board of the Company can exercise independent judgment and is always acting for the interests of the Company and its shareholders as a whole. Accordingly, the Group is capable of carrying on its businesses independently of, and at arm's length from, the competing businesses mentioned above.

Directors' Report

SUBSTANTIAL SHAREHOLDERS

As at 31 December 2004, the register of substantial shareholders maintained by the Company pursuant to Section 336 of the SFO showed that the following shareholders had notified the Company of relevant interests in the issued capital of the Company.

Name of shareholder	Number of shares held	Percentage of shareholding
China Electronics Corporation (BVI) Holdings Company Limited ("CEC BVI")	6,500,000,000	74.98%
CEC (1)	6,500,000,000	74.98%
Bravo New Investments Limited ("Bravo")	500,000,000	5.76%
Mr. Chan Chak Shing (2)	764,372,870	8.81%

(1) CEC holds 100% interest in CEC BVI and is deemed to be interested in the shares held by CEC BVI.

(2) This number of shares represents the aggregate of (i) Mr. Chan Chak Shing's family interest of 33,000,000 shares and (ii) corporate interest of 500,000,000 shares and 231,372,870 shares held by Bravo and Winsan International Holdings Limited ("WIHL") respectively. As Mr. Chan Chak Shing holds 100% interest in both Bravo and WIHL, the shares held by Bravo and WIHL are deemed to be interests of Mr. Chan Chak Shing.

All the interests disclosed above represent long position in the shares of the Company.

Save as disclosed above, as at 31 December 2004, no person or corporation had any interest or short position in the shares or underlying shares of the Company as recorded in the register required to be kept under Section 336 of the SFO.

PRE-EMPTIVE RIGHTS

There is no provision for pre-emptive rights under the Company's bye-laws or the laws in Bermuda.

PURCHASE, SALE OR REDEMPTION OF THE COMPANY'S SHARES

On 17 September 2004, the Company entered into the placing agreements to place in aggregate 610,000,000 shares of the Company to two independent third parties at HK$0.233 per share. The net proceeds of HK$142,130,000 were earmarked as the working capital of the Group and as the reserve for future opportunistic investments by the Group. The placing of shares was completed on 24 September 2004.

Save as disclosed above, neither the Company nor any of its subsidiaries has purchased, sold or redeemed any of the Company's shares during the year ended 31 December 2004.

MAJOR CUSTOMERS AND SUPPLIERS

During the year, the percentages of sales for the year attributable to the Group's major customers are as follows:

Sales

–	the largest customer	38%
–	five largest customers combined	91%

The percentages of purchases for the year attributable to the Group's major suppliers are as follows:

Purchases

–	the largest supplier	23%
–	five largest suppliers combined	44%

Philips Group is the beneficial owner of four of the five largest customers and one of the five largest suppliers of the Group. Details of the transactions are set out in the section headed "CONNECTED TRANSACTIONS" above.

None of the directors, their associates or any shareholder (which to the knowledge of the directors owns more than 5% of the Company's share capital) had an interest in the major suppliers or customers noted above.

DISCLOSURE PURSUANT TO RULE 13.20 OF THE LISTING RULES

As at 31 December 2004, the Group had in aggregate approximately HK$744.7 million (RMB789.8 million) due from members of the Philips Group. The receivables were mainly trade balances which arose from sales of products including goods, samples and materials in the ordinary course of the business of the Group with a small amount which represented reimbursement for taxation and administrative expenses paid during the year by the Group. Such amounts are to be settled in accordance with normal trade credit terms ranging from 30 to 60 days after invoice and are covered then by bank guarantee or by documents against acceptance arrangements.

The Philips Group is a connected person of the Company by virtue of being a substantial shareholder of the Group's principal operating subsidiary. Details of the transactions are set out in the section headed "CONNECTED TRANSACTIONS" above.

Save as disclosed above, there is no other disclosure required to be made by the Company pursuant to Rule 13.20 of the Listing Rules.

Directors' Report

COMPLIANCE WITH THE CODE OF BEST PRACTICE OF THE LISTING RULES

The directors are pleased to confirm that throughout the year ended 31 December 2004, the Company has complied with the Code of Best Practice as set out in Appendix 14 to the Listing Rules which was in force prior to 1 January 2005, except that during the year, the independent non-executive directors of the Company were not appointed for a specific terms but are subject to retirement by rotation in accordance with the Company's bye-laws.

PUBLIC FLOAT

As at the date of this report, the Company has maintained the prescribed public float under the Listing Rules, based on the information that is publicly available to the Company and within the knowledge of the directors of the Company.

COMPLIANCE WITH THE MODEL CODE

The Company has adopted the Model Code for Securities Transactions by Directors of Listed Issuers as set out in Appendix 10 of the Listing Rules ("Model Code"). Having made specific enquiry, the Company confirmed that all directors have complied with the required standard set out in the Model Code.

AUDIT COMMITTEE

The audit committee comprises Messrs. Chan Kay Cheung, Wong Po Yan and Yin Yongli, who are independent non-executive directors. The audit committee examined the accounting principles and practices adopted by the Group and discussed with management its internal controls and accounts. During the year, the audit committee has reviewed the unaudited interim accounts for the six months ended 30 June 2004 and the audited accounts for the year ended 31 December 2004.

AUDITORS

The accounts have been audited by PricewaterhouseCoopers who retire and, being eligible, offer themselves for re-appointment.

On behalf of the Board

Yang Xiaotang
Chairman

Hong Kong, 18 March 2005

Auditors' Report

PRICEWATERHOUSECOOPERS

羅兵咸永道會計師事務所

PricewaterhouseCoopers
22/F, Prince's Building
Central, Hong Kong
Telephone (852) 2289 8888
Facsimile (852) 2810 9888
www.pwchk.com

TO THE SHAREHOLDERS OF

CHINA ELECTRONICS CORPORATION HOLDINGS COMPANY LIMITED

(formerly Winsan (China) Investment Group Company Limited)

(incorporated in the Cayman Islands and continued in Bermuda with limited liability)

We have audited the accounts on pages 27 to 66 which have been prepared in accordance with accounting principles generally accepted in Hong Kong.

RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITORS

The Company's directors are responsible for the preparation of accounts which give a true and fair view. In preparing accounts which give a true and fair view it is fundamental that appropriate accounting policies are selected and applied consistently.

It is our responsibility to form an independent opinion, based on our audit, on those accounts and to report our opinion solely to you, as a body, in accordance with section 90 of the Companies Act 1981 of Bermuda, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

BASIS OF OPINION

We conducted our audit in accordance with Statements of Auditing Standards issued by the Hong Kong Institute of Certified Public Accountants. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the accounts. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the accounts, and of whether the accounting policies are appropriate to the circumstances of the Company and the Group, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance as to whether the accounts are free from material misstatement. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the accounts. We believe that our audit provides a reasonable basis for our opinion.

Auditors' Report

OPINION

In our opinion, the accounts give a true and fair view of the state of affairs of the Company and the Group as at 31 December 2004 and of the loss and cash flows of the Group for the year then ended and have been properly prepared in accordance with the disclosure requirements of the Hong Kong Companies Ordinance.

PricewaterhouseCoopers
Certified Public Accountants

Hong Kong, 18 March 2005

Consolidated Profit and Loss Account

For the year ended 31 December 2004

	Note	2004 HK$'000	2003 HK$'000 (Note 1(b))	*(Winsan Group – not comparable)* 2003 HK$'000 (Note 1(c))
Turnover	3	**4,590,123**	2,862,236	3,369
Cost of sales		**(4,352,639)**	(2,707,366)	(5,773)
Gross profit/(loss)		**237,484**	154,870	(2,404)
Other revenues	3	**40,780**	18,791	3
Selling and distribution costs		**(43,032)**	(27,383)	(1,178)
Administrative expenses		**(106,436)**	(52,785)	(25,142)
Other operating expenses		**(31,159)**	(22,583)	(17)
Operating profit/(loss)	4	**97,637**	70,910	(28,738)
Finance costs	5	**(21,180)**	(6,484)	(1,041)
Profit/(loss) after finance costs		**76,457**	64,426	(29,779)
Provision for impairment on goodwill	13	**(61,498)**	–	(55,977)
Profit/(loss) before taxation		**14,959**	64,426	(85,756)
Taxation	6	**(8,518)**	(5,186)	–
Profit/(loss) after taxation		**6,441**	59,240	(85,756)
Minority interests		**(25,704)**	(20,734)	–
(Loss)/profit attributable to shareholders		**(19,263)**	38,506	(85,756)
Basic (loss)/earnings per share	9	**HK cents (0.27)**	HK cents 0.59	HK cents (5.50)

Consolidated Balance Sheet

As at 31 December 2004

	Note	2004 HK$'000	2003 HK$'000 (Note 1(b))	(Winsan Group – not comparable) 2003 HK$'000 (Note 1(c))
Non-current assets				
Intangible assets	13	**3,498**	3,841	–
Fixed assets	14	**119,402**	88,022	4,166
		122,900	91,863	4,166
Current assets				
Inventories	16	**388,620**	254,727	115
Trade and other receivables	17	**931,391**	1,010,079	2,019
Bank balances and cash		**217,433**	23,444	1,234
		1,537,444	1,288,250	3,368
Current liabilities				
Amounts due to related companies of Winsan Group		**–**	–	53,957
Trade and other payables	18	**768,237**	783,646	12,626
Taxation payable		**3,537**	2,665	–
Warranty provision	19	**2,214**	1,172	–
Current portion of long-term bank loans		**–**	–	2,893
Short-term bank loans, unsecured	20	**392,231**	309,259	3,583
Bank overdrafts		**–**	–	464
		1,166,219	1,096,742	73,523
Net current assets/(liabilities)		**371,225**	191,508	(70,155)
Total assets less current liabilities		**494,125**	283,371	(65,989)
Financed by				
Issued equity	21	**373,750**	169,437	15,585
Reserves	22	**(4,509)**	14,754	(82,808)
Shareholders' funds/ (shareholders' deficiency)		**369,241**	184,191	(67,223)
Minority interests		**124,884**	99,180	–
Long-term bank loans		**–**	–	1,234
		494,125	283,371	(65,989)

Yang Xiaotang
Director

Fan Qingwu
Director

Balance Sheet

As at 31 December 2004

	Notes	2004 HK$'000	2003 HK$'000
Non-current assets			
Fixed assets	14	**681**	117
Investments in subsidiaries	15	**260,639**	443
		261,320	560
Current assets			
Trade and other receivables	17	**800**	1,706
Bank balances and cash		**137,342**	469
		138,142	2,175
Current liabilities			
Amounts due to related companies of Winsan Group		–	27,150
Trade and other payables	18	**1,899**	2,720
Current portion of long-term bank loans		–	1,458
Bank overdrafts		–	464
		1,899	31,792
Net current assets/(liabilities)		**136,243**	(29,617)
Total assets less current liabilities		**397,563**	(29,057)
Financed by			
Share capital	21	**86,685**	15,585
Reserves	22	**310,878**	(44,642)
Shareholders' funds/(shareholders' deficiency)		**397,563**	(29,057)

Yang Xiaotang
Director

Fan Qingwu
Director

Consolidated Statement of Changes in Equity

For the year ended 31 December 2004

			(Winsan Group – not comparable)
	2004	2003	2003
	HK$'000	HK$'000	HK$'000
		(Note 1(b))	(Note 1(c))
At 1 January	**184,191**	145,366	18,533
Capital injection	**–**	319	–
Issue of shares	**142,130**	–	–
Arising from reverse acquisition	**62,183**	–	–
(Loss)/profit for the year	**(19,263)**	38,506	(85,756)
At 31 December	**369,241**	184,191	(67,223)

Consolidated Cash Flow Statement

For the year ended 31 December 2004

	Note	2004 HK$'000	2003 HK$'000 (Note 1(b))	*(Winsan Group – not comparable)* 2003 HK$'000 (Note 1(c))
Operating activities				
Net cash inflow/(outflow) from operations	23(a)	**85,576**	(119,565)	(14,911)
Interest paid		**(21,445)**	(5,935)	(1,041)
PRC income tax paid		**(7,646)**	(6,959)	–
Net cash inflow/(outflow) from operating activities		**56,485**	(132,459)	(15,952)
Investing activities				
Interest received		**916**	486	3
Purchase of fixed assets and intangible assets (excluding goodwill)		**(82,651)**	(45,832)	(332)
Cash received from disposal of fixed assets		**112**	–	–
Net cash outflow from investing activities		**(81,623)**	(45,346)	(329)
Net cash outflow before financing activities		**(25,138)**	(177,805)	(16,281)
Financing activities	23(b)			
Issue of ordinary shares		**142,130**	–	–
Transaction costs of the Acquisition		**(5,975)**	–	–
Cash received from capital injection		**–**	490	–
Increase in amounts due to related companies of Winsan Group		**–**	–	33,974
New loans payable		**1,470,621**	309,259	–
Repayment of loans borrowed		**(1,387,649)**	(141,429)	(13,045)
Net cash inflow from financing		**219,127**	168,320	20,929
Increase/(decrease) in cash and cash equivalents		**193,989**	(9,485)	4,648
Cash and cash equivalents at 1 January		**23,444**	32,929	(3,878)
Cash and cash equivalents at 31 December		**217,433**	23,444	770
Analysis of balances of cash and cash equivalents:				
Bank balances and cash		**217,433**	23,444	1,234
Bank overdrafts		**–**	–	(464)
		217,433	23,444	770

Notes to the Accounts

1. BASIS OF PREPARATION

(a) Preparation of accounts

The accounts have been prepared in accordance with accounting principles generally accepted in Hong Kong and comply with accounting standards issued by the Hong Kong Institute of Certified Public Accountants (the "HKICPA") (collectively "HK GAAP"). They have been prepared under the historical cost convention.

The HKICPA has issued a number of new and revised Hong Kong Financial Reporting Standards and Hong Kong Accounting Standards ("new HKFRSs") which are effective for accounting periods beginning on or after 1 January 2005. The Company and its subsidiaries (the "Group") has not early adopted these new HKFRSs in the accounts for the year ended 31 December 2004. The Group has already commenced an assessment of the impact of these new HKFRSs but is not yet in a position to state whether these new HKFRSs would have a significant impact on its results of operations and financial position.

(b) The Acquisition

On 10 December 2003, China Electronics Corporation ("CEC"), the Company and the Company's then holding company, Winsan International Holdings Limited, entered into a sale and purchase agreement to acquire CEC's 65% equity interest in Shenzhen Sang Fei Consumer Communications Company Limited ("Sang Fei"), a Sino-foreign joint venture company established in the People's Republic of China (the "PRC") principally engaged in the manufacturing and sale of mobile telephones (the "Acquisition"), at a consideration of HK$260,000,000. The consideration was satisfied by the issuance of 6,500,000,000 shares of the Company (the "Consideration Shares") to CEC. The Acquisition was completed on 24 September 2004.

Under HK GAAP and as stated in the circular to the shareholders dated 21 June 2004, the Acquisition has been accounted for as a reverse acquisition since the issuance of the Consideration Shares in exchange for the 65% equity interest in Sang Fei resulted in CEC becoming the controlling shareholder of the Company. For accounting purpose, Sang Fei is regarded as the acquirer while the Company and its then subsidiaries (the "Winsan Group") are deemed to have been acquired by Sang Fei.

1. BASIS OF PREPARATION *(CONTINUED)*

(b) The Acquisition *(continued)*

In preparing these consolidated accounts, Sang Fei has applied the purchase method in accounting for the deemed acquisition of the Winsan Group. The assets and liabilities of the Winsan Group were recorded on the balance sheet of the Group at their fair value as at the date of completion of the Acquisition. In addition, goodwill arising from the Acquisition of the Winsan Group of HK$63,075,000 (note 13) was recorded, representing the excess of the cost of acquisition deemed to be incurred by Sang Fei over the fair value of the separable assets and liabilities of the Winsan Group at the date of completion of the Acquisition.

Provision for impairment on the year-end balance of goodwill arising from the Acquisition was fully made as at 31 December 2004.

These consolidated accounts have been prepared as a continuation of the consolidated accounts of Sang Fei and accordingly:

(i) the assets and liabilities of Sang Fei are recognised and measured at their historical carrying values prior to the completion of the Acquisition;

(ii) the retained earnings and other equity balances recognised in these consolidated accounts are those of Sang Fei;

(iii) the amount recognised as issued equity, which consists of share capital and share premium, has been determined by adding to the issued equity of Sang Fei immediately before the completion of the Acquisition the cost of the acquisition of the Winsan Group. However, the equity structure (i.e. the number and type of shares issued) reflects the equity structure of the Company including the Consideration Shares;

(iv) the 2003 comparative information presented is that of Sang Fei.

(c) Additional information

Additional information of the Winsan Group for the year ended and as at 31 December 2003 are also presented. However, they are not comparable to the basis of preparation of the accounts as set out above.

Notes to the Accounts

2. PRINCIPAL ACCOUNTING POLICIES

The principal accounting policies adopted in the preparation of these accounts are set out below:

(a) Group accounting

(i) Consolidation

The consolidated accounts include the accounts of the Company and its subsidiaries made up to 31 December.

Subsidiaries are those entities in which the Company, directly or indirectly, controls more than one half of the voting power; has the power to govern the financial and operating policies; to appoint or remove the majority of the members of the board of directors; or to cast majority of votes at the meetings of the board of directors.

The results of subsidiaries acquired or disposed of during the year are included in the consolidated profit and loss account from the effective date of acquisition or up to the effective date of disposal, as appropriate.

All significant intercompany transactions and balances within the Group are eliminated on consolidation.

The gain or loss on the disposal of a subsidiary represents the difference between the proceeds of the disposal and the Group's share of its net assets together with any unamortised goodwill/ negative goodwill or goodwill/negative goodwill taken to reserves and which as not previously charged or recognised in the consolidated profit and loss account and any related accumulated foreign currency translation reserve.

Minority interests represent the interests of outside shareholders in the operating results and net assets of subsidiaries of the Group.

In the Company's balance sheet the investments in subsidiaries are stated at cost less provision for impairment losses. The results of subsidiaries are accounted for by the Company on the basis of dividends received and receivable.

2. PRINCIPAL ACCOUNTING POLICIES *(CONTINUED)*

(a) Group accounting *(continued)*

(ii) Translation of foreign currencies

Transactions in foreign currencies are translated at exchange rates ruling at the transactions dates. Monetary assets and liabilities expressed in foreign currencies at the balance sheet date are translated at rates of exchange ruling at the balance sheet date. Exchange differences arising in these cases are dealt with in the profit and loss account.

The balance sheets of subsidiaries expressed in foreign currencies are translated at the rates of exchange ruling at the balance sheet date whilst the profit and loss account is translated at an average rate. Exchange differences are dealt with as movements in reserves.

(b) Intangible assets

(i) Goodwill

Goodwill represents the excess of the cost of an acquisition over the fair value of the Group's share of the net assets of the acquired subsidiary at the date of acquisition.

Goodwill on acquisitions is included in intangible assets and is amortised using the straight-line method over its estimated useful life.

(ii) Computer software

Costs associated with developing or maintaining computer software programmes are recognised as an expense as incurred. Costs that are directly associated with identifiable and unique software products acquired by the Group and probably generate economic benefits exceeding costs beyond one year, are recognised as intangible assets.

Expenditure which enhances or extends the performance of computer software programmes beyond their original specifications is recognised as a capital improvement and added to the original cost of the software. Computer software development costs recognised as assets are amortised using the straight-line method over their useful lives, not exceeding a period of 5 years.

Notes to the Accounts

2. PRINCIPAL ACCOUNTING POLICIES *(CONTINUED)*

(b) Intangible assets *(continued)*

(iii) Research and development costs

Research costs are expensed as incurred. Costs incurred on development projects relating to the design and testing of new or improved products are recognised as an intangible asset where the technical feasibility and intention of completing the product under development has been demonstrated and the resources are available to do so, costs are identifiable and there is an ability to sell or use the asset that will generate probable future economic benefits. Such development costs are recognised as an asset and amortised on a straight-line basis over a period of not more than 5 years to reflect the pattern in which the related economic benefits are recognised. Development costs that do not meet the above criteria are expensed as incurred. Development costs previously recognised as an expense are not recognised as an asset in a subsequent period.

(iv) Impairment of intangible assets

At each balance sheet date, both internal and external sources of information are considered to assess whether there is any indication that intangible assets including goodwill are impaired. If any such indication exists, the recoverable amount of the asset is estimated and where relevant, an impairment loss is recognised to reduce the asset to its recoverable amount. Such impairment losses are recognised in the profit and loss account.

(c) Fixed assets

Fixed assets, comprising leasehold improvements, plant and machinery, motor vehicles and furniture and fixtures are stated at cost less accumulated depreciation and accumulated impairment losses.

Fixed assets are depreciated at rates sufficient to write off their cost less accumulated impairment losses to their residual value over their estimated useful lives on a straight-line basis. The principal estimated useful lives are as follows:

Leasehold improvements	5 years
Plant and machinery	3 – 4 years
Motor vehicles	5 years
Furniture and fixtures	4 – 5 years

2. PRINCIPAL ACCOUNTING POLICIES *(CONTINUED)*

(c) Fixed assets *(continued)*

Improvements are capitalised and depreciated over their expected useful lives to the Group.

At each balance sheet date, both internal and external sources of information are considered to assess whether there is any indication that fixed assets are impaired. If any such indication exists, the recoverable amount of the asset is estimated and where relevant, an impairment loss is recognised to reduce the asset to its recoverable amount. Such impairment losses are recognised in the profit and loss account.

The gain or loss on disposal of a fixed asset is the difference between the net sales proceeds and the carrying amount of the relevant asset, and is recognised in the profit and loss account.

(d) Operating leases

Leases where substantially all the risks and rewards of ownership of assets remain with the leasing company are accounted for as operating leases. Payments made under operating leases net of any incentives received from the leasing company are charged to the profit and loss account on a straight-line basis over the lease periods.

(e) Inventories

Inventories comprise raw materials, work in progress and finished goods and are stated at the lower of cost and net realisable value. Cost, calculated on the first-in, first-out basis, comprises materials, direct labour and an appropriate proportion of all production overhead expenditure. Net realisable value is determined on the basis of anticipated sales proceeds less estimated selling expenses.

(f) Accounts receivable

Provision is made against accounts receivable to the extent that they are considered to be doubtful. Accounts receivable in the balance sheet are stated net of such provision.

Notes to the Accounts

2. PRINCIPAL ACCOUNTING POLICIES *(CONTINUED)*

(g) Cash and cash equivalents

Cash and cash equivalents are carried in the balance sheet at cost. For the purposes of the cash flow statement, cash and cash equivalents comprise cash on hand, deposit held at call with banks, cash investments with a maturity of three months or less from date of investment and bank overdraft.

(h) Provisions

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation, and a reliable estimate of the amount can be made. Where the Group expects a provision to be reimbursed, the reimbursement is recognised as a separate asset but only when the reimbursement is virtually certain.

The Group recognised a provision for repairs or replacements of products still under warranty at the balance sheet date. This provision is calculated based on past history of the level of repair and replacements.

(i) Employee benefits

(i) Employee leave entitlements

Employee entitlements to annual leave are recognised when they accrue to employees. A provision is made for the estimated liability for annual leave as a result of services rendered by employees up to the balance sheet date.

Employee entitlements to sick leave and maternity leave are not recognised until the time of leave.

(ii) Bonus plans

The expected cost of bonus payments are recognised as a liability when the Group has a present legal or constructive obligation as a result of services rendered by employees and a reliable estimate of the obligation can be made.

Liabilities for profit sharing and bonus plans are expected to be settled within 12 months and are measured at the amounts expected to be paid when they are settled.

2. PRINCIPAL ACCOUNTING POLICIES *(CONTINUED)*

(i) Employee benefits *(continued)*

(iii) Pension obligations

The Group operates a mandatory provident fund scheme ("MPF") for the eligible employees in Hong Kong. The Group's contributions to MPF are set at 5% of employees' salaries, including basic salaries and other cash allowances and are expensed as incurred.

The principal subsidiary, Sang Fei, that operating in the PRC has to make contribution to staff retirement scheme managed by local government authorities in accordance with the relevant rules and regulations. Contributions to these schemes are charged to the profit and loss account as and when incurred.

(j) Contingent liabilities

A contingent liability is a possible obligation that arises from past events and whose existent will only be confirmed by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the Group. It can also be a present obligation arising from past events that is not recognised because it is not probable that outflow of economic resources will be required or the amount of obligation cannot be measured reliably.

A contingent liability is not recognised but is disclosed in the notes to the accounts. When a change in the probability of an outflow occurs so that outflow is probable, they will then be recognised as a provision.

(k) Deferred taxation

Deferred taxation is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the accounts. Taxation rates enacted or substantively enacted by the balance sheet date are used to determine deferred taxation.

Deferred tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

Notes to the Accounts

2. PRINCIPAL ACCOUNTING POLICIES *(CONTINUED)*

(k) Deferred taxation *(continued)*

Deferred taxation is provided on temporary differences arising on investments in subsidiaries, except where the timing of the reversal of the temporary difference can be controlled and it is probable that the temporary difference will not reverse in the foreseeable future.

(l) Revenue recognition

Revenue from the sale of goods is recognised on the transfer of risks and rewards of ownership, which generally coincides with the time when the goods are delivered to customers and title has passed.

Interest income is recognised on a time proportion basis, taking into account the principal amounts outstanding and the interest rates applicable.

Dividend income is recognised when the right to receive payment is established.

(m) Borrowing costs

Borrowing costs that are directly attributable to the acquisition, construction or production of an asset that necessarily takes a substantial period of time to get ready for its intended use or sale are capitalised as part of the cost of that asset.

All other borrowing costs are charged to the profit and loss account in the year in which they are incurred.

(n) Segment reporting

In accordance with the Group's internal financial reporting, the Group has determined that business segments be presented as the primary reporting format and geographical segments as the secondary reporting format.

In respect of geographical segments reporting, sales are based on the country in which the customer is located. Total assets and capital expenditure are where the assets are located.

2. PRINCIPAL ACCOUNTING POLICIES *(CONTINUED)*

(n) Segment reporting *(continued)*

Unallocated costs represent corporate expenses. Segment assets consist primarily of receivables. Segment liabilities comprise operating liabilities and exclude items such as taxation and certain corporate borrowings. Capital expenditure comprises additions to fixed assets and intangible assets.

3. TURNOVER, REVENUE AND SEGMENT INFORMATION

(a) The Group is principally engaged in manufacturing and selling of mobile telephones. Revenues recognised during the year are as follows:

	2004	2003
	HK$'000	HK$'000
Turnover		
– Sales of mobile telephones	**4,590,123**	2,862,236
Other revenues		
– Interest income	**916**	486
– Sales of samples and materials	**39,864**	18,305
	40,780	18,791
Total revenues	**4,630,903**	2,881,027

Notes to the Accounts

3. TURNOVER, REVENUE AND SEGMENT INFORMATION *(CONTINUED)*

(b) Primary reporting format – business segments

	Philips branded products		Own branded products		OEM other products and other operations		Total	
	2004 HK$'000	2003 HK$'000	**2004 HK$'000**	2003 HK$'000	**2004 HK$'000**	2003 HK$'000	**2004 HK$'000**	2003 HK$'000
Turnover	**4,149,406**	2,595,274	**368,665**	112,792	**72,052**	154,170	**4,590,123**	2,862,236
Segment results	**182,718**	135,267	**39,833**	6,741	**14,933**	14,304	**237,484**	156,312
Unallocated revenue							**916**	486
Unallocated costs							**(140,763)**	(85,888)
Operating profit							**97,637**	70,910
Finance costs							**(21,180)**	(6,484)
Profit after finance costs							**76,457**	64,426
Provision for impairment on goodwill							**(61,498)**	–
Profit before taxation							**14,959**	64,426
Taxation							**(8,518)**	(5,186)
Profit after taxation							**6,441**	59,240
Minority interests							**(25,704)**	(20,734)
(Loss)/profit attributable to shareholders							**(19,263)**	38,506
Segment assets	**728,981**	826,312	**65,876**	28,981	**6,951**	154,786	**801,808**	1,010,079
Unallocated assets							**858,536**	370,034
Total assets							**1,660,344**	1,380,113
Segment liabilities	**30,476**	135,396	**5,409**	5,008	**–**	–	**35,885**	140,404
Unallocated liabilities							**1,130,334**	956,338
Total liabilities							**1,166,219**	1,096,742
Capital expenditure							**82,651**	45,832
Depreciation							**43,081**	42,511
Amortisation charge							**2,756**	701

3. TURNOVER, REVENUE AND SEGMENT INFORMATION *(CONTINUED)*

(c) Secondary reporting format – geographical segments

	Turnover		Total assets		Capital expenditure	
	2004	2003	**2004**	2003	**2004**	2003
	HK$'000	HK$'000	**HK$'000**	HK$'000	**HK$'000**	HK$'000
Mainland China	**2,116,578**	1,360,993	**417,336**	504,583		
Europe	**1,528,452**	1,067,153	**247,412**	320,445		
Asia excluding mainland China and Hong Kong	**199,375**	384,057	**139,989**	169,525		
Hong Kong	**745,718**	50,033	**32,655**	15,525		
Unallocated assets			**822,952**	370,035	**82,651**	45,832
	4,590,123	2,862,236	**1,660,344**	1,380,113	**82,651**	45,832

4. OPERATING PROFIT

Operating profit is stated after charging the following:

	2004	2003
	HK$'000	HK$'000
Depreciation of owned fixed assets	**43,081**	42,511
Impairment of fixed assets	**7,359**	–
Amortisation of intangible assets	**2,756**	701
Loss on disposal of fixed assets	**–**	793
Staff costs (including directors' remuneration) (note 10)	**108,218**	59,433
Cost of inventories sold	**4,123,676**	2,584,262
Provision for inventories	**17,224**	943
Provision for warranty (note 19)	**5,949**	3,981
Operating leases of buildings	**14,734**	10,685
Research and development costs	**10,497**	5,844
Auditors' remuneration	**889**	478

Notes to the Accounts

5. FINANCE COSTS

	2004 HK$'000	2003 HK$'000
Interest on bank loans	**21,180**	6,484

6. TAXATION

The amount of taxation charged to the consolidated profit and loss account represents:

	2004 HK$'000	2003 HK$'000
Current taxation – PRC income tax	**8,518**	5,186

(a) No provision for Hong Kong profits tax has been made as the Group has no assessable profit for the year (2003: Nil).

(b) The principal subsidiary, Sang Fei, is a foreign investment production enterprise established in Shenzhen Special Economic Zone in the PRC, the prevailing enterprise income tax rate is 15%. As approved by the tax authorities in 1998, Sang Fei is entitled to exemption from income taxes for two years followed by a 50% tax reduction for three years, commencing from the year ended 31 December 2000, the first cumulative profit-making year net of losses carried forward. Enterprise income taxes have been provided at the rate of 7.5% (2003: 7.5%) for the year ended 31 December 2004.

(c) The taxation on the Group's profit before taxation differs from the theoretical amount that would arise using the taxation rate in the PRC as follows:

	2004 HK$'000	2003 HK$'000
Profit before taxation	**14,959**	64,426
Calculated at a taxation rate of 15% (2003: 15%)	**2,244**	9,664
Profit earned in the tax holiday period	**(6,323)**	(4,832)
Expenses not deductible for taxation purposes	**12,008**	354
Unrecognised tax losses	**589**	–
Taxation charge	**8,518**	5,186

(d) As at 31 December 2004, the Group did not have any significant deferred tax assets and liabilities (2003: Nil).

7. PROFIT/(LOSS) ATTRIBUTABLE TO SHAREHOLDERS

The profit attributable to shareholder is dealt with in the accounts of the Company to the extent of HK$30,465,000 (2003: loss of HK$47,590,000).

8. DIVIDEND

The directors do not recommend the payment of a dividend for the year ended 31 December 2004 (2003: Nil).

9. (LOSS)/EARNINGS PER SHARES

Under the reverse acquisition method of accounting described in note 1(b) to the accounts, the 6,500,000,000 ordinary shares issued by the Company to acquire the 65% equity interest of Sang Fei as set out in note 21 are deemed to have been in issue on 1 January 2003 for the purpose of computing the 2003 earnings per share.

The calculation of the basic (loss)/earnings per share is based on the Group's loss attributable to shareholders for the year ended 31 December 2004 of HK$19,263,000 (2003: profit of HK$38,506,000) and the weighted average of 7,086,556,066 (2003: 6,500,000,000 ordinary shares deemed to have been in issue on 1 January 2003) ordinary shares in issue during the year.

No diluted (loss)/earnings per share is presented as there were no potential dilutive ordinary shares in issue during the years ended 31 December 2003 and 2004.

10. STAFF COSTS

Staff costs, including directors' emoluments, were analysed as follows:

	2004	2003
	HK$'000	HK$'000
Salaries, allowance and bonuses	**91,891**	49,035
Retirement benefit contributions (notes)	**6,423**	3,876
Others	**9,904**	6,522
	108,218	59,433

(a) The Group operates a MPF for the eligible employees in Hong Kong. The Group's contributions to MPF are set at 5% of employees' salaries, including basic salaries and other cash allowances and are expensed as incurred.

Notes to the Accounts

10. STAFF COSTS *(CONTINUED)*

(b) The principal subsidiary, Sang Fei, participates in a defined contribution retirement scheme based on laws and regulations in the PRC. Each employee covered by the scheme is entitled, after their retirement from Sang Fei, to a pension equal to the basis salary of the employees as at their retirement dates in the PRC. The local government authority of the PRC is responsible for the pension liabilities to these retired employees in the PRC. Sang Fei made monthly contributions to the retirement scheme at a minimum rate of 8% (2003: 8%) of the basis salaries of employees in the PRC.

11. DIRECTORS' EMOLUMENTS

The emoluments payable to directors during the year were as follows:

	2004	2003
	HK$'000	HK$'000
Directors' fees	**409**	360
Basic salaries, allowances or benefits in kind	**2,832**	2,220
Bonuses	**38**	–
Contributions to retirement schemes	**48**	39
	3,327	2,619

The emoluments fell within the following band:

	Number of individual	
	2004	2003
Emolument band		
HK$Nil – HK$1,000,000	**10**	5
HK$1,500,001 – HK$2,000,000	**1**	1
	11	6

11. DIRECTORS' EMOLUMENTS *(CONTINUED)*

The directors' fees paid to independent non-executive directors of the Company for the year ended 31 December 2004 amounted to HK$409,000 (2003: HK$360,000).

None of the directors of the Company has waived any emolument in respect of the year ended 31 December 2004 (2003: Nil).

12. FIVE HIGHEST PAID INDIVIDUALS

The five individuals whose emoluments were the highest in the Group for the year included one (2003: four) director of the Company whose emolument is reflected in the analysis presented in note 11. The emoluments paid to the remaining four individuals (2003: one individual) during the year are as follows:

	2004	2003
	HK$'000	HK$'000
Basic salaries, allowances and benefits in kind	**5,329**	2,400
Bonuses	**1,667**	–
Contributions to retirement schemes	**522**	12
	7,518	2,412

The emoluments fell within the following band:

	Number of individuals	
	2004	2003
Emolument band		
HK$1,000,001 – HK$1,500,000	**1**	–
HK$1,500,001 – HK$2,000,000	**1**	–
HK$2,000,001 – HK$2,500,000	**1**	1
HK$2,500,001 – HK$3,000,000	**1**	–
	4	1

Notes to the Accounts

13. INTANGIBLE ASSETS – GROUP

	Goodwill	Computer software	Total
	HK$'000	HK$'000	HK$'000
Year ended 31 December 2004			
Opening net book amount	–	3,841	3,841
Reverse acquisition of a subsidiary	63,075	–	63,075
Additions	–	836	836
Impairment charge	(61,498)	–	(61,498)
Amortisation charge	(1,577)	(1,179)	(2,756)
Closing net book amount	–	3,498	3,498
At 31 December 2004			
Cost	63,075	10,609	73,684
Accumulated amortisation and impairment	(63,075)	(7,111)	(70,186)
Net book amount	–	3,498	3,498
At 31 December 2003			
Cost	–	9,773	9,773
Accumulated amortisation	–	(5,932)	(5,932)
Net book amount	–	3,841	3,841

14. FIXED ASSETS

(a) Group

	Leasehold improvements HK$'000	Plant and machinery HK$'000	Motor vehicles HK$'000	Furniture and fixtures HK$'000	Total HK$'000
Cost					
At 1 January 2004	25,695	209,414	2,146	23,701	260,956
Acquisition of subsidiaries	102	–	–	58	160
Additions	7,673	67,807	749	5,586	81,815
Disposals	(4)	(1,147)	(8)	(3,991)	(5,150)
At 31 December 2004	**33,466**	**276,074**	**2,887**	**25,354**	**337,781**
Accumulated depreciation and impairment					
At 1 January 2004	20,882	141,592	1,114	9,346	172,934
Acquisition of subsidiaries	25	–	–	18	43
Depreciation charge	1,042	38,464	402	3,173	43,081
Impairment charge	–	3,830	58	3,471	7,359
Disposals	(1)	(1,094)	(8)	(3,935)	(5,038)
At 31 December 2004	**21,948**	**182,792**	**1,566**	**12,073**	**218,379**
Net book value					
At 31 December 2004	**11,518**	**93,282**	**1,321**	**13,281**	**119,402**
At 31 December 2003	4,813	67,822	1,032	14,355	88,022

Notes to the Accounts

14. FIXED ASSETS *(CONTINUED)*

(b) Company

	Motor vehicles HK$'000	Furniture and fixtures HK$'000	Total HK$'000
Cost			
At 1 January 2004	118	137	255
Additions	684	40	724
Disposals	(118)	(125)	(243)
At 31 December 2004	**684**	**52**	**736**
Accumulated depreciation			
At 1 January 2004	47	91	138
Depreciation charge	57	10	67
Disposals	(59)	(91)	(150)
At 31 December 2004	**45**	**10**	**55**
Net book value			
At 31 December 2004	**639**	**42**	**681**
At 31 December 2003	71	46	117

15. INVESTMENTS IN SUBSIDIARIES – COMPANY

	2004 HK$'000	2003 HK$'000
Investments in subsidiaries – unlisted shares, at cost	**260,000**	777,006
Amounts due from subsidiaries	**639**	639
	260,639	777,645
Less: Provision	**–**	(777,202)
	260,639	443

Particulars of the subsidiaries of the Group as at 31 December 2004 are set out in note 28 to the accounts. The amounts due from subsidiaries are unsecured, interest free and are not requested to pay within one year.

16. INVENTORIES – GROUP

	2004 HK$'000	2003 HK$'000
Raw materials	**234,231**	178,851
Work in progress	**109,726**	45,991
Finished goods	**62,830**	31,381
	406,787	256,223
Less: Provision for impairment	**(18,167)**	(1,496)
	388,620	254,727

At 31 December 2004, the carrying amount of inventories that are carried at net realisable value amounted to zero (2003: Nil).

Notes to the Accounts

17. TRADE AND OTHER RECEIVABLES

	Note	Group 2004 HK$'000	Group 2003 HK$'000	Company 2004 HK$'000	Company 2003 HK$'000
Trade receivables	(a)	**801,085**	945,548	**–**	–
Notes receivable	(b)	**3,255**	27,020	**–**	–
Other receivables due from related parties		**25,240**	16,219	**–**	–
Prepayments and deposits		**27,867**	6,306	**791**	1,706
Value-added tax refundable		**65,690**	8,634	**–**	–
Other receivables		**8,254**	6,352	**9**	–
		931,391	1,010,079	**800**	1,706

(a) The credit terms of the Group generally range from 30 to 60 days. At 31 December 2004, the ageing analysis of the Group's trade receivables was as follows:–

	2004 HK$'000	2003 HK$'000
Current to 30 days	**798,907**	940,798
31 – 60 days	**25**	2,480
Over 60 days	**2,153**	2,270
	801,085	945,548

Included in the balance were trade receivables from related parties of HK$729,925,000 (2003: HK$830,962,000). About 91% (2003: 95%) of the trade receivables from related parties as at 31 December 2004 was covered by bank issued guarantee documents.

(b) The balance represents bank acceptance notes with maturity period within six months. At 31 December 2004, none of the notes receivable is from related parties (2003: HK$10,984,000).

18. TRADE AND OTHER PAYABLES

	Group		Company	
	2004	2003	**2004**	2003
	HK$'000	HK$'000	**HK$'000**	HK$'000
Trade payables	**640,669**	682,775	**–**	2,490
Other payables due to related parties	**9,079**	38,887	**–**	–
Accrued expenses	**17,792**	19,049	**1,899**	230
Advance from customers	**44,037**	3,199	**–**	–
Other payables	**56,660**	39,736	**–**	–
	768,237	783,646	**1,899**	2,720

At 31 December 2004, the ageing analysis of the Group's trade payables was as follows:

	Group		Company	
	2004	2003	**2004**	2003
	HK$'000	HK$'000	**HK$'000**	HK$'000
Current to 30 days	**578,606**	678,632	**–**	2,490
31– 60 days	**27,257**	1,471	**–**	–
Over 60 days	**34,806**	2,672	**–**	–
	640,669	682,775	**–**	2,490

Included in the balance were trade payables to related parties of HK$46,358,000 (2003: HK$94,337,000).

Notes to the Accounts

19. WARRANTY PROVISION – GROUP

	2004 HK$'000	2003 HK$'000
At beginning of the year	**1,172**	102
Additional provision charged to profit and loss account	**5,949**	3,981
Less: amount utilised	**(4,907)**	(2,911)
At end of the year	**2,214**	1,172

The Group gives 15-month warranties on products distributed by Sang Fei for end users in the PRC market and undertakes to repair and replace items that fail to operate satisfactorily. Provision has been recognised for expected warranty claims based on past experience of the level of repairs and returns.

20. SHORT-TERM BANK LOANS, UNSECURED – GROUP

The bank loans are unsecured, repayable within one year and bear interest at the average borrowing rate of 4.438% (2003: 4.536%) per annum.

21. ISSUED EQUITY/SHARE CAPITAL

	Group	
	Number of shares	**Issued equity** HK$'000
At 31 December 2004	**8,668,480,000**	**373,750**

(a) By adopting reverse acquisition method of accounting as described in note 1(b), the amount of issued equity of the Group which includes share capital and share premium in the consolidated balance sheet represents the amount of issued equity of Sang Fei, the cost of the Acquisition and the issuance of new shares as described in note (b)(ii) below.

21. ISSUED EQUITY/SHARE CAPITAL *(CONTINUED)*

(b) The following information is provided to trace the movements in the share capital of the Company:

		Company			
		Number of shares		**Amounts**	
		2004	2003	**2004**	2003
	Note			**HK$'000**	HK$'000
Ordinary share of HK$0.01					
Authorised:					
At 1 January and 31 December		**30,000,000,000**	30,000,000,000	**300,000**	300,000
Issued and fully paid:					
At 1 January		**1,558,480,000**	1,558,480,000	**15,585**	15,585
Issue of Consideration Shares	(i)	**6,500,000,000**	–	**65,000**	–
Issue of shares	(ii)	**610,000,000**	–	**6,100**	–
At 31 December		**8,668,480,000**	1,558,480,000	**86,685**	15,585

(i) On 24 September 2004, 6,500,000,000 new ordinary shares of HK$0.01 each were issued to CEC for the acquisition of the 65% equity interest in Sang Fei (note 1(b)).

(ii) On 24 September 2004, 420,000,000 and 190,000,000 new ordinary shares of HK$0.01 each were issued to two respective new shareholders in cash for a total of HK$142,130,000.

As at 31 December 2004, there was no share option outstanding under the Share Option Scheme of the Company.

Notes to the Accounts

22. RESERVES

(a) Group

	Capital reserves HK$'000 (note (a))	Surplus reserves HK$'000 (note (b))	Retained earnings/ (accumulated losses) HK$'000	Total HK$'000
At 1 January 2004	(1,806)	14,906	1,654	14,754
Appropriation from retained earnings	–	6,104	(6,104)	–
Loss for the year	–	–	(19,263)	(19,263)
At 31 December 2004	**(1,806)**	**21,010**	**(23,713)**	**(4,509)**
At 1 January 2003	(1,806)	29,810	(36,852)	(8,848)
Capitalisation of reserve	–	(14,904)	–	(14,904)
Profit for the year	–	–	38,506	38,506
At 31 December 2003	(1,806)	14,906	1,654	14,754

(a) Capital reserves

Capital reserves represent the exchange differences arising from paid-in capital paid by foreign currencies in Sang Fei.

22. RESERVES *(CONTINUED)*

(a) Group *(continued)*

(b) Surplus reserves

In accordance with the "Laws of the PRC on Joint Ventures Using Chinese and Foreign Investment" and Sang Fei's Articles of Association, appropriations of the reserve fund and the enterprise expansion fund from profit after taxation have to be made prior to profit distribution to the equity owners. The percentage of appropriation of reserve fund and the enterprise expansion fund is approved by the board of directors.

Upon approval from the board of directors, the reserve fund can be used to offset against accumulated losses or to increase capital while the enterprise expansion fund can be used to expand production and to increase capital.

(b) Company

	Share premium	**Contributed surplus**	**Accumulated losses**	**Total**
	HK$'000	HK$'000	HK$'000	HK$'000
At 1 January 2004	–	140,263	(184,905)	(44,642)
Issue of shares	331,030	–	–	331,030
Transaction costs paid	(5,975)	–	–	(5,975)
Profit for the year	–	–	30,465	30,465
At 31 December 2004	**325,055**	**140,263**	**(154,440)**	**310,878**
At 1 January 2003	–	140,263	(137,315)	2,948
Loss for the year	–	–	(47,590)	(47,590)
At 31 December 2003	–	140,263	(184,905)	(44,642)

Under the Companies Act 1981 of Bermuda, the contributed surplus of the Company is distributable to shareholders in certain circumstances as specified in Section 54 thereof.

Notes to the Accounts

23. NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT

(a) Reconciliation of operating profit to net cash inflow/(outflow) from operating activities

	2004	2003
	HK$'000	HK$'000
Operating profit	**97,637**	70,910
Depreciation of owned fixed assets	**43,081**	42,511
Impairment of fixed assets	**7,359**	–
Amortisation of intangible assets	**2,756**	701
Loss on disposal of fixed assets	**–**	793
Provision for inventories	**17,224**	943
Interest income	**(916)**	(486)
Operating profit before working capital change	**167,141**	115,372
Increase in inventories	**(151,117)**	(190,448)
Decrease/(increase) in trade and other receivables	**84,756**	(538,802)
(Decrease)/increase in trade and other payables	**(16,246)**	493,243
Increase in warranty provision	**1,042**	1,070
Net cash inflow/(outflow) from operations	**85,576**	(119,565)

23. NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT *(CONTINUED)*

(b) Analysis of changes in financing during the year

	Issued equity	**Minority interests**	**Bank loans**
	HK$'000	HK$'000	HK$'000
At 1 January 2003	154,214	78,275	141,429
Capital injection	319	171	–
Capital transferring from surplus reserve	14,904	–	–
New loans raised	–	–	309,259
Repayment of loans borrowed	–	–	(141,429)
Minority interests' share of profit	–	20,734	–
At 31 December 2003	169,437	99,180	309,259
Shares issued	142,130	–	–
Arising from reverse acquisition	62,183	–	–
New loans raised	–	–	1,470,621
Repayment of loans borrowed	–	–	(1,387,649)
Minority interests' share of profit	–	25,704	–
At 31 December 2004	**373,750**	**124,884**	**392,231**

Notes to the Accounts

23. NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT *(CONTINUED)*

(c) Cash generated from the Acquisition

The Acquisition as described in note 1(b) to the accounts:

	2004
	HK$'000
Net assets acquired:	
Fixed assets	117
Trade and other receivables	6,068
Trade and other payables	(1,102)
	5,083
Goodwill arising on consolidation	63,075
	68,158
Satisfied by:	
Deemed consideration paid by Sang Fei	62,183
Transaction costs paid	5,975
	68,158
Net cash outflow on the Acquisition	5,975

Contribution to cash flow from the Acquisition of Winson Group is minimal.

24. COMMITMENTS UNDER OPERATING LEASES

At 31 December 2004, the Group had future aggregate minimum lease payments under non-cancellable operating lease in respect of land and buildings as follows:

	Group		Company	
	2004	2003	**2004**	2003
	HK$'000	HK$'000	**HK$'000**	HK$'000
Not later than one year	**24,676**	14,807	**175**	–
In the second to fifth year	**37,987**	32,252	**131**	–
	62,663	47,059	**306**	–

25. CAPITAL COMMITMENTS

	Group		Company	
	2004	2003	**2004**	2003
	HK$'000	HK$'000	**HK$'000**	HK$'000
Purchase of fixed assets and computer software				
Contracted but not provided for	**8,717**	13,268	**–**	–

26. CONTINGENT LIABILITIES

The Group did not have any material contingent liabilities outstanding as at 31 December 2003 and 2004.

Notes to the Accounts

27. RELATED PARTY TRANSACTIONS

Significant related party transactions of the Group's business are as follows:

During the year, the Group entered into transactions with companies under common control of:

– CEC, the ultimate holding company. These companies are denoted by * below;

– Koninklijke Philips Electronics N.V. ("KPE") (a company incorporated in Holland), the ultimate holding company of the minority shareholder with significant influence on operation of the principal subsidiary, Sang Fei. These companies are denoted by # below.

(a) Sales of products, samples and materials

		Group	
		2004	2003
		HK$'000	HK$'000
Sales of products:			
Philips Electronics (Shanghai) Co., Ltd.	#	**1,735,539**	1,092,279
Philips France S.A.S.	#	**1,525,193**	1,067,153
Philips Electronics Singapore Pte. Ltd.	#	**719,537**	384,056
Philips Electronics Hong Kong Ltd.	#	**169,136**	50,033
Shenzhen SED Coalition Electronics Co., Ltd.	*	**25,550**	90,037
CEC Wireless R&D Ltd.	*	**899**	–
Sales of samples and materials			
Philips Electronics (Shanghai) Co., Ltd.	#	**12,429**	3,413
Shenzhen SED Industry Co., Ltd.	*	**17,513**	–
Shenzhen SED Coalition Electronics Co., Ltd.	*	**–**	4,715
CEC Group, others	*	**76**	–
Philips Group, others	#	**293**	–

Members of KPE and its subsidiaries (the "Philips Group") are the major customers of the Group. Sales to the Philips Group were based on a long-term agreement in which the Philips Group was entitled to purchase goods from the Group at a price determined using a "cost plus" basis.

One of the distributors of the Group's mobile telephones is a member of CEC and its group companies (the "CEC Group"). Sales to the CEC Group were based on a business service agreement and were carried out on commercial terms and conditions and at market prices.

27. RELATED PARTY TRANSACTIONS *(CONTINUED)*

(b) Other transactions

		Note	Group 2004 HK$'000	Group 2003 HK$'000
Purchases of raw materials		(i)		
Philips France S.A.S.	#		**764**	17,348
Philips Electronics Hong Kong Ltd.	#		**1,033,030**	841,979
Oesterrichische Philips	#		**–**	6,309
Shenzhen Sang Da Baili Electronics Co., Ltd.	*		**8,052**	–
Philips Group, others	#		**407**	–
Corporate services:		(ii)		
Philips Electronics Hong Kong Ltd.	#		**15,535**	14,492
Processing services:		(iii)		
Shenzhen Sang Da Baili Electronics Co., Ltd.	*		**5,572**	2,084
Shenzhen SED Industry Co., Ltd.	*		**792**	–
Fitment and decoration services:		(iv)		
Shenzhen SED Fitment & Decoration Co., Ltd.	*		**5,065**	2,865
Canteen services:		(v)		
Shenzhen Sang Da Baili Electronics Co., Ltd.	*		**6,459**	3,341
Repair and maintenance services:		(vi)		
Shenzhen SED ARC Co., Ltd.	*		**1,175**	2,190
Rental:		(vii)		
Shenzhen SED Industry Co., Ltd.	*		**4,996**	5,539
Shenzhen Sang Da Baili Electronics Co., Ltd.	*		**1,014**	–
Purchases of fixed assets:		(viii)		
Assembleon Hong Kong Ltd.	#		**19,649**	–
Philips France S.A.S.	#		**–**	3,291
CEC Wireless R&D Ltd.	*		**–**	3,395

Notes to the Accounts

27. RELATED PARTY TRANSACTIONS *(CONTINUED)*

(b) Other transactions *(continued)*

(i) Members of the Philips Group are the major suppliers of raw materials. Purchases of raw materials from the Philips Group were based on a long term agreement and were carried out in the ordinary course of business and on commercial terms and conditions.

The Group from time to time purchases raw materials from members of the CEC Group. Purchases of raw materials from the CEC Group were based on a business service agreement and were carried out in the ordinary course of business and on commercial terms and conditions.

(ii) Members of the Philips Group from time to time provide certain in-house treasury, fiscal, legal services and non product related services to the Group. The corporate services are based on service agreements entered into by the relevant parties and the Group and were carried out on commercial terms and conditions.

(iii) The Group secured dedicated processing services of SMA production lines from members of the CEC Group. The processing services were based on service contracts entered into by the relevant parties and the Group and were carried out on commercial terms and conditions.

(iv) The Group engaged members of the CEC Group to undertake renovation works in connection with the expansion of the Group's production premises. The fitment and decoration services were based on a business service agreement and were on commercial terms and conditions.

(v) Shenzhen Sang Da Baili Electronics Co., Ltd. provides canteen services to the production staff of the Group. The canteen services were based on a business service agreement and the fee were calculated by reference to actual consumption and an agreed fixed premium and were on commercial terms and conditions.

(vi) The Group engaged Shenzhen SED ARC Co., Ltd. for after sales product repair and maintenance services in respect of its own-branded products. The repair and maintenance services were based on a business service agreement and carried out on commercial terms and conditions.

(vii) The production facilities and some of the staff quarters of the Group were located within an industrial complex owned by members of the CEC Group. The rentals were based on lease agreements entered into by the relevant parties and the Group and were calculated on commercial terms and conditions.

(viii) Purchases of fixed assets were based on agreements entered into by the related parties and the Group and were carried out on commercial terms and conditions.

27. RELATED PARTY TRANSACTIONS *(CONTINUED)*

(c) Year-end balance arising from sales and other transactions

		Group	
		2004	2003
		HK$'000	HK$'000
Receivables from related parties:			
Philips Electronics (Shanghai) Co., Ltd.	#	**329,251**	320,457
Philips France S.A.S.	#	**245,932**	320,445
Philips Electronics Singapore Pte. Ltd.	#	**139,989**	169,525
Philips Electronics Hong Kong Ltd.	#	**29,531**	15,884
Shenzhen SED Industry Co., Ltd.	*	**7,026**	1,634
Shenzhen Sang Da Baili Electronics Co., Ltd.	*	**1,327**	–
Shenzhen SED Coalition Electronics Co., Ltd.	*	**–**	28,981
Payables to related parties:			
Philips Electronics Hong Kong Ltd.	#	**35,887**	99,370
Shenzhen Sang Da Baili Electronics Co., Ltd.	*	**5,661**	–
Philips France S.A.S.	#	**4,622**	8,764
Philips Electronics Singapore Pte. Ltd.	#	**2,577**	4,402
Philips (China) Investment Co., Ltd.	#	**3**	13,743

The receivables/payables from/to related parties were interest-free, unsecured and settled in accordance with terms of the agreements and generally within one year. All sales of products made to the Philips Group in 2003 and 2004 were covered by guarantee documentation issued by banks.

Notes to the Accounts

28. SUBSIDIARIES

During the year, Winsan Group disposed of all its then subsidiaries which had no material business operations.

As at 31 December 2004, the Company held interest in the following principal subsidiaries which, in the opinion of the directors, were significant to the results of the year and/or formed a substantial portion of the net assets of the Group.

Company	Place of incorporation and kind of legal entity	Place of operation and principal activities	Particulars of issued/registered capital	Effective interest held
Indirectly held:				
Shenzhen Sang Fei Consumer Communications Company Limited	PRC, a Sino-foreign equity joint venture company	PRC, manufacture and sale of mobile telephones	Registered capital of RMB276,470,000	65%
China Electronics Corporation Management Limited	Hong Kong, limited company	Hong Kong, provision of group management services	2 ordinary shares of HK$1 each	100%

29. ULTIMATE HOLDING COMPANY

The directors regard China Electronics Corporation, a state-owned enterprise established under the laws of PRC, as being the ultimate holding company.

30. APPROVAL OF ACCOUNTS

The accounts were approved by the board of directors on 18 March 2005.

Financial Summary

Set out below is a summary of the financial information of the Group for the last five financial years.

RESULTS

	Year ended 31 December				
	2004	2003	2002	2001	2000
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
		(note)	(note)	(note)	(note)
Turnover	**4,590,123**	3,369	708	240,376	395,133
Profit/(loss) before taxation	**14,959**	(85,756)	(48,255)	(471,571)	(110,772)
Taxation	**(8,518)**	–	–	(10,821)	(1,001)
Profit/(loss) after taxation	**6,441**	(85,756)	(48,255)	(482,392)	(111,773)
Minority interests	**(25,704)**	–	1,078	2,992	628
Loss attributable to shareholders	**(19,263)**	(85,756)	(47,177)	(479,400)	(111,145)

ASSETS AND LIABILITIES

	As at 31 December				
	2004	2003	2002	2001	2000
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
		(note)	(note)	(note)	(note)
Total assets	**1,660,344**	7,534	76,283	102,138	1,856,277
Total liabilities	**(1,166,219)**	(74,757)	(57,750)	(86,557)	(1,121,407)
Minority interests	**(124,884)**	–	–	(1,078)	(250,841)
Net assets/(liabilities)	**369,241**	(67,223)	18,533	14,503	484,029

Note:

The financial information as at and for the four financial years ended 31 December 2000, 2001, 2002 and 2003 set out above is that of the Winsan Group, and is not comparable to the basis of preparation of the accounts for the year ended 31 December 2004.

Glossary of Technical Terms

"3G"	an abbreviation of "Third Generation" which is the third generation of mobile communication technology enabling voice, text images and video communication
"CDMA"	an abbreviation of "Code Division Multiple Access", a system that allows multiple users to share one or more radio channels for service by adding a unique code to each data signal that is being sent to and from each of the radio transceivers, which code is used to spread the data signal to a bandwidth much wider than is necessary to transmit the data signal without the code
"GSM"	an abbreviation of "Global System for Mobile Communications", a digital cellular telephone system which is now available in most parts of the world, and uses 200 kHz wide channels that allows eight simultaneous calls on the same radio frequency
"ODM"	an abbreviation of "Original Design Manufacturer", being a manufacturer that designs and makes products in accordance with the customers' conceptual requirements and which carry the customers' brandnames
"OEM"	an abbreviation of "Original Equipment Manufacturer" being a manufacturer that makes products in accordance with the specification, and which carry the brandnames, of its customers
"PHS"	an abbreviation of "Personal Handyphone System", a digital cordless technology developed in Japan and deployed by NTT DoCoMo and other Japanese operators. It offers two-way communications, data services and Internet access
"SMA"	an abbreviation for "Surface Mount Assembly", the production process during which the circuit board for a mobile phone product is produced