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CHINA ELECTRONICS HUADA TECHNOLOGY COMPANY LIMITED

中國電子華大科技有限公司

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

(Stock Code: 00085)

2019 INTERIM RESULTS ANNOUNCEMENT

The board of directors (the “Board”) of China Electronics Huada Technology Company Limited (the “Company”) presents the unaudited condensed consolidated results of the Company and its subsidiaries (the “Group”) for the six months ended 30 June 2019 as follows:

CONSOLIDATED STATEMENT OF PROFIT OR LOSS

	Note	Unaudited Six months ended 30 June	
		2019 HK\$'000	2018 HK\$'000
Revenue	3	908,572	981,034
Cost of sales		(608,522)	(662,451)
Gross profit		300,050	318,583
Other income	4	24,369	19,709
Selling and marketing costs		(43,533)	(50,616)
Administrative expenses		(165,378)	(168,933)
Impairment losses on trade and other receivables		(8,055)	(1,634)
Operating profit		107,453	117,109
Finance income	5	876	2,874
Finance costs	5	(53,054)	(48,919)
Finance costs – net	5	(52,178)	(46,045)
Share of results of associates		16,878	13,251
Share of result of a joint venture		–	236
Profit before taxation	6	72,153	84,551
Taxation	7	972	(4,559)
Profit for the period		73,125	79,992

CONSOLIDATED STATEMENT OF PROFIT OR LOSS (*Continued*)

		Unaudited	
		Six months ended 30 June	
		2019	2018
	<i>Note</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Profit for the period attributable to:			
Owners of the Company		72,231	78,080
Non-controlling interests		894	1,912
		<u>73,125</u>	<u>79,992</u>
		<i>HK cents</i>	<i>HK cents</i>
Basic earnings per share	<i>9</i>	<u>3.56</u>	<u>3.85</u>

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

	Unaudited	
	Six months ended 30 June	
	2019	2018
	<i>HK\$'000</i>	<i>HK\$'000</i>
Profit for the period	73,125	79,992
Other comprehensive income for the period, net of taxation:		
Items that may be subsequently reclassified to profit or loss:		
Exchange differences on translation of financial statements	<u>(14,572)</u>	<u>(107,731)</u>
Total comprehensive income for the period	<u>58,553</u>	<u>(27,739)</u>
Total comprehensive income for the period attributable to:		
Owners of the Company	58,401	(27,366)
Non-controlling interests	<u>152</u>	<u>(373)</u>
	<u>58,553</u>	<u>(27,739)</u>

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

	30 June	31 December
	2019	2018
	(Unaudited)	(Audited)
<i>Note</i>	HK\$'000	HK\$'000
ASSETS		
Non-current assets		
Property, plant and equipment	84,973	367,599
Right-of-use assets	91,437	–
Investment properties	48,801	48,847
Land use rights	–	11,302
Intangible assets	4,902	2,059
Investment in associates	2,646,795	2,665,777
Deferred tax assets	45,599	38,024
	2,922,507	3,133,608
Current assets		
Inventories	520,844	603,679
Trade and other receivables	10 1,026,331	722,947
Financial assets at fair value through profit or loss	102,669	42,029
Short-term deposits	238,718	91,303
Cash and cash equivalents	230,217	375,525
	2,118,779	1,835,483
Total assets	5,041,286	4,969,091

CONSOLIDATED STATEMENT OF FINANCIAL POSITION *(Continued)*

	30 June	31 December
	2019	2018
	(Unaudited)	(Audited)
<i>Note</i>	HK\$'000	HK\$'000
EQUITY AND LIABILITIES		
Equity attributable to owners of the Company		
Share capital and premium	825,454	825,454
Reserves	(721,196)	(707,366)
Retained earnings	<u>1,879,203</u>	<u>1,804,305</u>
	1,983,461	1,922,393
Non-controlling interests	<u>18,942</u>	<u>18,790</u>
	2,002,403	1,941,183
Liabilities		
Non-current liabilities		
Lease liabilities	68,868	–
Deferred tax liabilities	<u>8,776</u>	<u>24,511</u>
	<u>77,644</u>	<u>24,511</u>
Current liabilities		
Deferred government grants	40,978	44,083
Contract liabilities	4,931	13,377
Trade and other payables	11 594,052	638,480
Bank and other borrowings	2,286,051	2,295,297
Lease liabilities	22,604	–
Income tax payable	<u>12,623</u>	<u>12,160</u>
	<u>2,961,239</u>	<u>3,003,397</u>
Total liabilities	<u>3,038,883</u>	<u>3,027,908</u>
Total equity and liabilities	<u><u>5,041,286</u></u>	<u><u>4,969,091</u></u>

Notes:

1 BASIS OF PREPARATION

(a) Compliance with HKFRS and Listing Rules

The condensed consolidated interim financial statements have been prepared in accordance with the applicable disclosure requirements of Appendix 16 to the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the “Listing Rules”) and with Hong Kong Accounting Standard 34 “Interim Financial Reporting” issued by the Hong Kong Institute of Certified Public Accountants.

The condensed consolidated interim financial statements should be read in conjunction with the consolidated financial statements of the Group for the year ended 31 December 2018, which have been prepared in accordance with Hong Kong Financial Reporting Standards (“HKFRSs”).

The condensed consolidated interim financial statements have been prepared under the historical cost convention as modified by the revaluation of investment properties and certain financial assets at fair value through profit or loss which are carried at fair value.

(b) Going concern

At 30 June 2019, the Group’s current liabilities exceeded its current assets by HK\$842,460,000 primarily due to the fact that the Group has liabilities under short-term bank and other borrowings (the “Short-term Borrowings”) of HK\$2,286,051,000.

The Board has reviewed the Group’s cash flow projections which covers a period of not less than twelve months from 30 June 2019. Given that the Short-term Borrowings of HK\$2,160.4 million are guaranteed by China Electronics Corporation Limited, and taking into account the financial resources available to the Group, including the internally generated funds, expected renewal and extension of borrowings upon their maturities and the available committed borrowing facilities, the Board considers that there are sufficient financial resources available to the Group to meet its financial liabilities as and when they fall due in the coming twelve months from 30 June 2019. Accordingly, the Board has prepared the condensed consolidated interim financial statements on a going concern basis.

2 PRINCIPAL ACCOUNTING POLICIES

Except for the adoption for the first time of all the new and amended Hong Kong Financial Reporting Standards issued by the Hong Kong Institute of Certified Public Accountants that are relevant to the Group’s operations and effective for the accounting period beginning on 1 January 2019, the accounting policies adopted in the preparation of the condensed consolidated interim financial statements are consistent with those adopted in the consolidated financial statements of the Group for the year ended 31 December 2018.

Except as disclosed below, the adoption of these new and amended standards had no material effect on the results and financial position of the Group and/or disclosures set out in the condensed consolidated interim financial statements.

HKFRS16 “Leases”

In the current period, the Group has adopted HKFRS16 “Leases”. HKFRS16 sets out the principles for the recognition, measurement, presentation and disclosure of leases. The Group has applied HKFRS16 retrospectively with the cumulative effect of initial adoption as an adjustment to the retained earnings at 1 January 2019, and the comparative information of the condensed consolidated interim financial statements continues to be reported under the accounting policies and disclosure requirements prevailing prior to 1 January 2019.

Under HKFRS16, a contract is, or contains a lease if the contract conveys a right to control the use of an identified asset for a period of time in exchange for consideration. Upon adoption of HKFRS16, the Group recognised right-of-use assets and lease liabilities for those leases previously classified as operating leases, except for leases with terms of 12 months or less (“short-term leases”) and leases of low-value assets. Right-of-use assets are initially measured at cost and subsequently carried at cost less accumulated depreciation and impairment losses. The cost of right-of-use assets includes the amount of lease liabilities recognised, initial direct costs incurred, and less any lease incentives received. Lease liabilities are initially measured at the present value of the remaining lease payments discounted using the incremental borrowing rate of the lessee. Subsequently, lease liabilities are adjusted by interest accretion and lease payments. For short-term leases and leases of low-value assets, lease payments are recognised as an expense on a straight-line basis over the lease term.

The effects of adoption of HKFRS16 at 1 January 2019 are as follows:

	Increase <i>HK\$’000</i>
Right-of-use assets	2,614
Investment in associates	43,322
Lease liabilities	2,672
Retained earnings	43,264
	<u><u> </u></u>

The reconciliation from operating lease commitments at 31 December 2018 to lease liabilities at 1 January 2019 is as follows:

	<i>HK\$’000</i>
Operating lease commitments at 31 December 2018	17,193
Weighted average incremental borrowing rate at 1 January 2019	4.89%
Discounted operating lease commitments at 1 January 2019	16,511
Less: Commitments relating to short-term leases and leases of low-value assets	<u>(13,839)</u>
Lease liabilities at 1 January 2019	<u><u> </u></u> 2,672

3 REVENUE AND SEGMENT INFORMATION

(a) Revenue

	Unaudited	
	Six months ended 30 June	
	2019	2018
	<i>HK\$'000</i>	<i>HK\$'000</i>
Sale of integrated circuit products	<u>908,572</u>	<u>981,034</u>

All the revenue of the Group are from sale of goods, which is recognised when the control of goods is transferred at a point in time.

(b) Operating segments

Management has determined the operating segments based on the reports reviewed by the Board (the chief operating decision maker) that are used to assess performance and allocate resources. The Board assesses the performance of an operating segment based on a measure of its operating profit excluding unallocated corporate income and expenses.

The Board considers that the Group's operations are operated and managed as a single segment and accordingly, no operating segment information is presented.

Nearly 100% of the Group's revenue is attributable to the market in the PRC and over 90% of the Group's non-current assets are located in the PRC. No geographical information is therefore presented.

4 OTHER INCOME

	Unaudited	
	Six months ended 30 June	
	2019	2018
	HK\$'000	HK\$'000
Government grants	6,720	6,733
Exchange gains	–	4,046
Fair value gains on financial assets at fair value through profit or loss	1,729	2,994
Gain on disposal of financial assets at fair value through profit or loss	–	4,587
Interest income	5,388	–
Rental income	1,260	1,349
Gain on disposal of a building in the PRC	9,122	–
Others	150	–
	24,369	19,709

5 FINANCE COSTS – NET

	Unaudited	
	Six months ended 30 June	
	2019	2018
	HK\$'000	HK\$'000
Finance costs		
– Interest expense on borrowings	53,054	48,919
Finance income		
– Interest income on cash and cash equivalents	(876)	(2,874)
Finance costs – net	52,178	46,045

6 PROFIT BEFORE TAXATION

The Group's profit before taxation has been arrived at after charging the following:

	Unaudited	
	Six months ended 30 June	
	2019	2018
	<i>HK\$'000</i>	<i>HK\$'000</i>
Depreciation of property, plant and equipment	6,551	12,015
Depreciation of right-of-use assets	9,779	–
Amortisation of intangible assets	3,339	3,542
Provision for inventories	1,050	14,860
Rental expenses from short-term leases and leases of low-value assets	5,007	–
Operating lease expenses on properties	–	6,228
	–	6,228

Research and development costs for the six months ended 30 June 2019 were HK\$105,994,000 (2018: HK\$108,762,000), and mainly comprised of employee costs of HK\$53,677,000 (2018: HK\$59,231,000) and material costs of HK\$31,050,000 (2018: HK\$18,111,000). No research and development costs were capitalised during the six months ended 30 June 2019 (2018: nil). For the six months ended 30 June 2019, provision for inventories of HK\$1,050,000 (2018: HK\$14,860,000) has been charged to cost of sales.

7 TAXATION

	Unaudited	
	Six months ended 30 June	
	2019	2018
	HK\$'000	HK\$'000
Current taxation		
– PRC corporate income tax	11,704	10,115
– Withholding tax on distributed profits (<i>Note (c)</i>)	(5,790)	(5,276)
	<u>5,914</u>	<u>4,839</u>
Deferred taxation		
– PRC corporate income tax	(10,392)	(4,005)
– Withholding tax on undistributed profits (<i>Note (c)</i>)	3,506	3,725
	<u>(6,886)</u>	<u>(280)</u>
	<u>(972)</u>	<u>4,559</u>

- (a) No provision for Hong Kong profits tax had been made as the Group did not generate any assessable profit in Hong Kong for the six months ended 30 June 2019 (2018: nil).
- (b) In accordance with the corporate income tax laws of the PRC, the applicable statutory tax rate of CEC Huada Electronic Design Co., Ltd (“Huada Electronics”) and Shanghai Huahong Integrated Circuit Co., Ltd (“Huahong”) is 25%. However, Huada Electronics and Huahong qualify as an “Integrated Circuit Design Enterprises in National Planning Layout” and thus enjoy a 10% preferential tax rate for the six months ended 30 June 2019 (2018: 10% and 15% preferential tax rate, respectively).
- (c) According to the relevant regulations of the corporate income tax laws of the PRC, when a foreign investment enterprise distributed dividends out of the profits earned from 1 January 2008 onwards to its overseas investors, such dividends are subject to withholding tax at a rate of 10%.

8 DIVIDEND

The Board has resolved not to declare any dividend for the six months ended 30 June 2019 (2018: nil).

9 EARNINGS PER SHARE

The calculation of the basic earnings per share is based on the following data:

	Unaudited	
	Six months ended 30 June	
	2019	2018
Profit for the period attributable to owners of the Company (HK\$'000)	72,231	78,080
Weighted average number of ordinary shares for the purposes of basic earnings per share	2,029,872,000	2,029,872,000
Basic earnings per share (HK cents)	<u>3.56</u>	<u>3.85</u>

No diluted earnings per share is presented as the Company did not have any potential ordinary shares outstanding.

10 TRADE AND OTHER RECEIVABLES

The majority of the Group's sales are with credit terms of 30 days to 135 days. The remaining amounts are due immediately after the delivery of goods. The ageing analysis of the Group's trade receivables (net of loss allowance for impairment) is as follows:

	30 June 2019 (Unaudited) HK\$'000	31 December 2018 (Audited) HK\$'000
Current to 30 days	230,298	330,280
31-60 days	156,092	63,652
61-180 days	395,057	169,427
Over 180 days and within 1 year	98,864	112,669
Over 1 year	37,577	16,155
	917,888	692,183

11 TRADE AND OTHER PAYABLES

The ageing analysis of the Group's trade payables is as follows:

	30 June 2019 (Unaudited) HK\$'000	31 December 2018 (Audited) HK\$'000
Current to 30 days	125,122	258,037
31-60 days	123,186	58,261
Over 60 days	59,460	85,674
	307,768	401,972

BUSINESS REVIEW

Results overview

Revenue of the Group for the six months ended 30 June 2019 amounted to HK\$908.6 million, representing a decrease of 7.4% when comparing with the corresponding period of last year. Profit attributable to owners of the Company amounted to HK\$72.2 million, representing a decrease of 7.5% when comparing with the corresponding period of last year. The basic earnings per share was HK3.56 cents (2018: HK3.85 cents).

Integrated circuits design operation

The Group's integrated circuits design operation comprises the design of security smart card chips and the development of application system. Currently, the Group's products are mainly used in sectors such as identity authentication, financial payment, government utilities, telecommunication and mobile payment. For the six months ended 30 June 2019, the Group has obtained 13 new patents, registered 1 new software copyright and 3 new integrated circuits layout designs.

During the first half of 2019, as domestic-made bank card chips were increasingly recognised by various banks, the market demand for domestic-made bank card chips continued to increase, and sales volume of bank card chips increased significantly when comparing with the corresponding period of last year. For social security cards, given the population coverage of the second-generation social security cards has reached a fairly high level, demand for the second-generation social security cards gradually declined, whereas issuance of the third-generation social security cards has started in most provinces leading to a growth in demand. During the period, sales volume of social security card chips increased slightly when comparing with the corresponding period of last year. Sales volume of other major products such as identity authentication as well as telecommunication and mobile payment smart card chips remained stable when comparing with the corresponding period of last year. Sales volume of other products such as public transportation card chips decreased when comparing with the corresponding period of last year. For the six months ended 30 June 2019, overall sales volume of the Group decreased by 3.9% when comparing with the corresponding period of last year.

Given that an increase in sales volume of bank card chips and social security card chips was recorded for the six months ended 30 June 2019, the impact of a general decline in the selling price of smart card chips when comparing with the corresponding period of last year as a result of further intensification in market price competition on the revenue during the period was partially offset. Revenue of the Group for the six months ended 30 June 2019 was HK\$908.6 million, representing a decrease of 7.4% when comparing with the corresponding period of last year.

For the six months ended 30 June 2019, the overall gross profit margin was 33.0% (2018: 32.5%). During the period, cost reduction and control were achieved to a certain extent through accelerating the launching of and switching to new products, improving efficiency in the production of new products, etc., and had compensated the impact of the increasingly fierce competition in the market of bank card chips and telecommunication and mobile payment smart card chips that led to a fall in the selling price of these products on the overall gross profit margin of the period.

Selling and marketing costs for the six months ended 30 June 2019 amounted to HK\$43.5 million (2018: HK\$50.6 million). The percentage of selling and marketing costs to revenue decreased to 4.8% from 5.2% of the corresponding period of last year. The decrease was mainly attributable to the continuous implementation by the Group of stringent cost control measures during the period.

Administrative expenses for the six months ended 30 June 2019 amounted to HK\$165.4 million, representing a decrease of 2.1% when comparing with the corresponding period of last year. The percentage of administrative expenses to revenue was 18.2% (2018: 17.2%). The Group continued to implement stringent cost control measures during the period.

Research and development costs for the six months ended 30 June 2019 amounted to HK\$106.0 million (2018: HK\$108.8 million). The percentage of research and development costs to revenue was 11.7% (2018: 11.1%). During the period, the Group established plans for the development of new Internet of Things security chip products and the upgrading of existing products and continued to invest in the improvement of product safety technology, enhancement of product functions and performance, advanced research of new process, etc.

Other income

For the six months ended 30 June 2019, the Group recognised a gain on disposal of a building in the PRC of HK\$9.1 million following the termination of the agreement to purchase Block C of China Electronics Information Security Technology Research and Development Foundation in the PRC.

Share of result of an associate

China Electronics Optics Valley Union Holding Company Limited (“CEOVU”), the Group’s associate listed on The Stock Exchange of Hong Kong Limited, is principally engaged in the business of development and operation of large-scale business parks in the PRC. The Group’s share of result from CEOVU for the six months ended 30 June 2019 was HK\$16.8 million (2018: HK\$13.0 million).

OUTLOOK

Looking forward, the market demand for smart card chips is expected to enter a stage of steady development. Application of the domestic-made substitutes and the state cryptographic algorithm will continue to advance in certain sectors of the smart card chips market, and the domestic integrated circuits design industry and the momentum for market development will further improve. However, competition will also be fiercer, and selling price of products will see a more apparent decreasing trend. With opportunities and challenges coexisting, the Group will continue to closely track domestic market demands, seize market opportunities, and actively explore potential customers to ensure its leading position in the field of smart card chips.

On the other hand, based on its smart card chips security and application technology accumulated over the years, the Group, with a market orientated approach, will continue to strengthen its product development in the direction of Internet of Things security chips and promote the application of such products in the industry. At the same time, the Group will focus on expanding the applications for industries such as smart cities, smart home and Internet of Vehicles, continuously striving to enhance its core competitiveness in the market of Internet of Things.

DIVIDEND

The Board has resolved not to declare any dividend for the six months ended 30 June 2019 (2018: nil).

FINANCIAL REVIEW

The Group generally finances its working capital and funding requirements through internal resources, and bank and other borrowings. At 30 June 2019, the Group had cash and cash equivalents amounted to HK\$230.2 million, of which 97.1% was denominated in Renminbi, 1.8% in United States dollars and 1.1% in Hong Kong dollars (31 December 2018: HK\$375.5 million, of which 90.2% was denominated in Renminbi, 8.0% in Hong Kong dollars and 1.8% in United States dollars).

At 30 June 2019, the Group had bank and other borrowings of HK\$2,286.1 million, of which 97.5% were denominated in Renminbi and 2.5% in Hong Kong dollars (31 December 2018: HK\$2,295.3 million, of which 97.5% were denominated in Renminbi and 2.5% in Hong Kong dollars). Among these borrowings, (i) HK\$57.5 million were secured by deposits of the Group and HK\$2,228.6 million were unsecured (31 December 2018: HK\$57.5 million were secured by deposits of the Group and HK\$2,237.8 million were unsecured), and (ii) HK\$2,228.6 million and HK\$57.5 million were borrowed at fixed and variable interest rates respectively (31 December 2018: HK\$2,237.8 million and HK\$57.5 million were borrowed at fixed and variable interest rates respectively). At 30 June 2019, committed borrowing facilities available to the Group but not drawn amounted to HK\$2,000.8 million.

At 30 June 2019, certain assets of the Group with an aggregate carrying value of HK\$62.5 million were pledged as collateral for borrowings of the Group (31 December 2018: HK\$62.8 million).

The Group's revenue are mainly denominated in Renminbi and payments are denominated in Renminbi and Hong Kong dollars. The Group will make use of hedging contracts, when appropriate, to hedge the risk of foreign exchange fluctuation arising from its operations.

At 30 June 2019, the Group had net current liabilities of HK\$842.5 million (31 December 2018: HK\$1,167.9 million). The gearing ratio, which is calculated as net debt divided by total equity and net debt of the Group, was 47.6% (31 December 2018: 48.5%).

At 30 June 2019, the Group did not have any material outstanding capital commitment (31 December 2018: nil) for the acquisition of fixed assets and intangible assets. The Group did not have any material contingent liability at 30 June 2019 (31 December 2018: nil).

EMPLOYEE AND REMUNERATION POLICIES

At 30 June 2019, the Group had approximately 380 employees, the majority of whom were based in the PRC. Employee benefit expenses during the period were HK\$97.3 million.

The Group recognises the importance of high calibre and competent staff and has a strict recruitment policy and performance appraisal scheme. Remuneration policies are largely in line with industry practices, and are formulated on the basis of performance and experience and will be reviewed regularly. Bonuses and other merit payments are linked with the performance of the Group and of the individuals as incentive to optimise performance.

PURCHASE, SALE OR REDEMPTION OF SECURITIES

Neither the Company nor any of its subsidiaries had purchased or sold any of the Company's shares and the Company had not redeemed any of its shares during the six months ended 30 June 2019.

CORPORATE GOVERNANCE CODE

The Company is committed to achieving the best corporate governance practices by emphasising its accountability, transparency, independence, responsibility and fairness. The Company is dedicated to exercise corporate governance through regular reviews of its adopted practices with reference to the Corporate Governance Code (the "CG Code") as set out in Appendix 14 to the Listing Rules. The Company has complied with all the applicable code provisions in the CG Code throughout the six months ended 30 June 2019.

AUDIT COMMITTEE

The audit committee of the Board has reviewed the unaudited condensed consolidated interim financial statements of the Group for the six months ended 30 June 2019.

PUBLICATION OF INTERIM REPORT

The 2019 interim report will be published on the website of the Company (www.cecht.com.cn) and on the website of The Stock Exchange of Hong Kong Limited (www.hkex.com.hk) in due course.

By Order of the Board
China Electronics Huada Technology Company Limited
Dong Haoran
Chairman

Hong Kong, 28 August 2019

As at the date of this announcement, the Board comprises two Non-executive Directors, namely Mr. Dong Haoran (Chairman) and Ms. Liu Jinmei, two Executive Directors, namely Mr. Yu Jian (Deputy Chairman) and Mr. Liu Hongzhou (Managing Director), and three Independent Non-executive Directors, namely Mr. Chan Kay Cheung, Mr. Qiu Hongsheng and Mr. Chow Chan Lum.