



TCL International Holdings Limited



GROWING
GLOBAL

Interim Report 2003

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GROWING

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Corporate Information

BOARD OF DIRECTORS

Chairman

Mr. Li Dong Sheng, Tomson

Vice Chairman

Mr. Yuan Xin Cheng

Executive Directors

Ms. Lu Zhong Li

Mr. Hu Qiu Sheng

Mr. Yan Yong

Mr. Suen Hay Wai

Independent Non-Executive Directors

Mr. Hon Fong Ming

Mr. Albert Thomas da Rosa, Junior

COMPANY SECRETARY

Ms. Pang Siu Yin, Solicitor, Hong Kong

PRINCIPAL BANKERS

Bank of China (Hong Kong) Ltd

CITIC Ka Wah Bank Ltd

DBS Bank (Hong Kong) Ltd

Hang Seng Bank Ltd

The Hongkong and Shanghai Banking Corporation Ltd

Industrial and Commercial Bank of China (Asia) Ltd

Nanyang Commercial Bank, Ltd

Standard Chartered Bank

Sumitomo Mitsui Banking Corporation

AUDITOR

Ernst & Young

Certified Public Accountants

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LEGAL ADVISOR

Cheung Tong & Rosa

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PRINCIPAL REGISTRAR

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18 Harcourt Road

Hong Kong

Interim Results

The board of directors of TCL International Holdings Limited (the "Company") is pleased to announce the unaudited consolidated results and financial position of the Company and its subsidiaries (the "Group") for the six months ended 30 June 2003 with comparative figures for the previous year as follows:

CONDENSED CONSOLIDATED PROFIT AND LOSS ACCOUNT

		6 months ended 30 June 2003 (unaudited)	6 months ended 30 June 2002 (unaudited)	3 months ended 30 June 2003 (unaudited)	3 months ended 30 June 2002 (unaudited)
	Notes	HK\$'000	HK\$'000	HK\$'000	HK\$'000
TURNOVER	2	6,247,682	5,385,234	2,770,741	2,396,091
Cost of sales		(5,244,230)	(4,375,472)	(2,323,878)	(1,966,844)
Gross profit		1,003,452	1,009,762	446,863	429,247
Other revenue and gains		59,633	62,923	39,690	23,175
Selling and distribution costs		(592,386)	(601,007)	(268,434)	(254,266)
Administrative expenses		(266,319)	(247,490)	(127,551)	(139,096)
Other operating expenses		(30,175)	(33,626)	(18,575)	(19,364)
PROFIT FROM OPERATING ACTIVITIES	2	174,205	190,562	71,993	39,696
Finance costs		(17,399)	(8,002)	(9,157)	(3,776)
Share of profits and losses of:					
Jointly-controlled entities	3	194,816	122,669	82,409	58,389
Associate		—	(66)	—	(11)
Others		(39,216)	(26,590)	(19,608)	(20,473)
PROFIT BEFORE TAX		312,406	278,573	125,637	73,825
Tax	5	(36,577)	(33,595)	(19,880)	(7,379)
PROFIT BEFORE MINORITY INTERESTS		275,829	244,978	105,757	66,446
Minority interests		(10,460)	8,015	(3,324)	2,419
NET PROFIT FROM ORDINARY ACTIVITIES ATTRIBUTABLE TO SHAREHOLDERS		265,369	252,993	102,433	68,865
DIVIDEND	6	Nil	Nil		
EARNINGS PER SHARE	7				
— Basic		10.05 cents	10.03 cents		
— Diluted		9.70 cents	9.77 cents		

Interim Results

CONDENSED CONSOLIDATED BALANCE SHEET

		30 June 2003 (unaudited) HK\$'000	31 December 2002 (audited) HK\$'000
	Notes		
NON-CURRENT ASSETS			
Fixed assets		814,732	734,262
Trademarks		26,794	25,910
Goodwill		261,244	277,949
Interests in jointly-controlled entities		1,537,452	1,543,143
Long term investments		2,298	1,682
		2,642,520	2,582,946
CURRENT ASSETS			
Inventories		2,159,463	2,579,118
Trade and bills receivable	8	1,037,361	1,029,005
Other receivables		396,740	408,413
Pledged bank deposits		47,506	89,340
Cash and bank balances		681,740	1,093,187
		4,322,810	5,199,063
CURRENT LIABILITIES			
Trade and bills payable	9	1,812,736	2,769,271
Tax payable		26,934	23,056
Other payables and accruals		634,859	612,751
Bank borrowings	10	80,022	23,845
		2,554,551	3,428,923
NET CURRENT ASSETS		1,768,259	1,770,140
TOTAL ASSETS LESS CURRENT LIABILITIES		4,410,779	4,353,086

Interim Results

	Notes	30 June 2003 (unaudited) HK\$'000	31 December 2002 (audited) HK\$'000
NON-CURRENT LIABILITIES			
Bank borrowings	10	329,412	382,785
Convertible notes		350,000	350,000
Deferred tax		1,915	1,915
		681,327	734,700
MINORITY INTERESTS			
		67,602	60,378
		3,661,850	3,558,008
CAPITAL AND RESERVES			
Issued capital	11	265,002	263,100
Reserves	12	3,396,848	3,110,353
Proposed final dividend		—	184,555
		3,661,850	3,558,008

Interim Results

CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

	Six months ended 30 June	
	2003 (unaudited) HK\$'000	2002 (unaudited) HK\$'000
1 January — Total equity	3,558,008	2,933,938
Net gains not recognised in the profit and loss account:		
Exchange differences on translation of the financial statements of foreign entities	4,261	13,298
Net profit for the period	265,369	252,993
Dividend	(185,483)	(75,869)
Issue of shares, including share premium	19,550	22,546
Write off of exchange reserve	145	—
30 June — Total equity	3,661,850	3,146,906

Interim Results

CONDENSED CONSOLIDATED CASH FLOW STATEMENT

	Six months ended 30 June	
	2003 (unaudited) HK\$'000	2002 (unaudited) HK\$'000
Net cash inflow/(outflow) from operating activities	(393,725)	191,028
Net cash inflow/(outflow) from investing activities	145,192	(400,730)
Net cash outflow from financing activities	(163,600)	(76,836)
Decrease in cash and cash equivalents	(412,133)	(286,538)
Cash and cash equivalents at beginning of period	1,093,187	1,021,009
Effect of foreign exchange rate changes, net	686	3,745
Cash and cash equivalents at end of period	681,740	738,216
Analysis of balances of cash and cash equivalents		
Cash and bank balances	681,740	738,216

Interim Results

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. Principal Accounting Policies

The directors of the Company ("Directors") are responsible for the preparation of the Group's unaudited interim financial statements. These financial statements have been prepared in accordance with Hong Kong Statements of Standard Accounting Practice, the accounting principles generally accepted in Hong Kong and the disclosure requirements of the Hong Kong Companies Ordinance. They have been prepared under the historical cost convention.

2. Segment Information

An analysis of the Group's turnover and profit from operating activities by principal activities for the six months ended 30 June 2003 is as follows:

	Turnover		Profit from operating activities	
	2003	2002	2003	2002
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Continuing operations:				
Television	5,179,358	4,259,989	218,593	291,261
Computers	728,320	391,368	12,864	(3,915)
Other audio-visual products	159,354	95,500	(7,791)	(15,473)
Others	180,650	125,883	(16,364)	(14,911)
	6,247,682	4,872,740	207,302	256,962
Discontinued operations:				
White goods	—	512,494	—	(29,740)
	6,247,682	5,385,234	207,302	227,222
Less: Amortisation of goodwill			(16,705)	(16,568)
Corporate expenses			(16,392)	(20,092)
			174,205	190,562

Interim Results

3. Share of Profits and Losses of Jointly-controlled Entities

More than 90% of the Group's share of results of its jointly-controlled entities was derived from Huizhou TCL Mobile Communication Co., Ltd and its subsidiaries (together "TCL Mobile Group"), which are engaged in the manufacture and sale of mobile phones. The condensed summary of certain additional financial information of TCL Mobile Group is as follows:

Results for the six months ended 30 June 2003:

	6 months ended 30 June 2003 (unaudited) HK\$'000	6 months ended 30 June 2002 (unaudited) HK\$'000	3 months ended 30 June 2003 (unaudited) HK\$'000	3 months ended 30 June 2002 (unaudited) HK\$'000
TURNOVER	4,879,799	3,064,271	2,216,107	1,512,752
Cost of sales	(3,904,409)	(2,268,118)	(1,745,528)	(1,162,803)
Gross profit	975,390	796,153	470,579	349,949
Other revenue and gains	8,202	19,441	873	16,734
Selling and distribution costs	(419,168)	(240,090)	(239,952)	(87,801)
Administrative and other operating expenses	(87,766)	(121,634)	(30,278)	(47,561)
PROFIT FROM OPERATING ACTIVITIES	476,658	453,870	201,222	231,321
Finance costs	(9,258)	(1,456)	(6,936)	(128)
PROFIT BEFORE TAX	467,400	452,414	194,286	231,193
Tax	(19,255)	(31,546)	(13,527)	(13,466)
NET PROFIT	448,145	420,868	180,759	217,727

Interim Results

3. Share of Profits and Losses of Jointly-controlled Entities (Continued)

Financial position:

	30 June 2003 (unaudited) HK\$'000	31 December 2002 (audited) HK\$'000
NON CURRENT ASSETS	240,627	194,020
CURRENT ASSETS		
Inventories*	1,363,420	1,409,987
Trade receivables	123,100	76,058
Bills receivable	1,877,630	1,272,208
Cash and bank balances	702,948	629,003
Other current assets	698,604	840,584
	4,765,702	4,227,840
CURRENT LIABILITIES		
Bank borrowings	81,062	67,643
Trade and bills payable	1,666,626	1,409,207
Other payables and accruals	1,523,901	1,260,498
Other current liabilities	53,432	73,944
	3,325,021	2,811,292
NET CURRENT ASSETS	1,440,681	1,416,548
NON-CURRENT LIABILITIES	684	2,456
	1,680,624	1,608,112
CAPITAL AND RESERVES		
Paid-up capital	232,215	232,215
Reserves	1,448,409	1,375,897
	1,680,624	1,608,112

* Included in the inventories are raw materials of HK\$493,182,000 (31 December 2002: HK\$847,466,000), work in progress of HK\$167,689,000 (31 December 2002: HK\$120,616,000) and finished goods of HK\$702,549,000 (31 December 2002: HK\$441,905,000).

4. Depreciation and Amortization

During the period, depreciation of HK\$69,577,000 (2002: HK\$68,250,000) was charged to the profit and loss account in respect of the Group's property, plant and equipment; and amortization of HK\$57,369,000 (2002: HK\$27,491,000) was charged to the profit and loss account in respect of the Group's intangible assets and goodwill arising on consolidation.

Interim Results

5. Tax

Hong Kong profits tax has been provided at the rate of 17.5% (2002: 16%) on the estimated assessable profits arising in Hong Kong during the period. Taxes on profits assessable elsewhere have been calculated at the rates of tax prevailing in the countries in which the Group operates, based on existing legislation, interpretations and practices in respect thereof:

	Six months ended 30 June	
	2003	2002
	(unaudited)	(unaudited)
	HK\$'000	HK\$'000
Group:		
Hong Kong	7,270	2,614
Elsewhere	21,274	21,740
	28,544	24,354
Share of tax attributable to:		
Jointly-controlled entities	8,033	9,241
	36,577	33,595

6. Dividend

The Directors do not recommend any payment of interim dividend for the six months ended 30 June 2003 (2002: Nil).

7. Earnings per Share

The calculation of basic earnings per share is based on the net profit attributable to shareholders for the period of HK\$265,369,000 (2002: HK\$252,993,000) and the weighted average of 2,640,504,430 (2002: 2,521,147,479) shares in issue during the period.

The calculation of diluted earnings per share is based on the net profit attributable to shareholders for the period of HK\$265,369,000 (2002: HK\$252,993,000), adjusted by the reduction of interest expenses of HK\$5,250,000 (2002: Nil) relating to the convertible notes. The weighted average number of shares used in the calculation is 2,640,504,430 (2002: 2,521,147,479) shares in issue during the period, as used in the basic earnings per share calculation; the weighted average of 12,673,692 (2002: 67,436,463) shares assumed to have been issued at no consideration on the deemed exercise of all share options during the period; and the weighted average of 136,932,707 (2002: Nil) shares on the deemed conversion of all convertible notes during the period.

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8. Trade and Bills Receivable

The majority of the Group's sales in China were made on cash-on-delivery basis and on commercial bills guaranteed by banks with credit period ranging from 30 days to 90 days. For overseas sales, the Group usually requires settlement by letter of credit with tenure ranging from 90 days to 180 days. Sales to certain long term strategic customers were also made on open-account basis with credit term of no more than 90 days. An aged analysis of the trade and bills receivable as at the balance sheet date, based on the invoice date and net of provisions, is as follows:

	30 June 2003 (unaudited) HK\$'000	31 December 2002 (audited) HK\$'000
Current to 90 days	777,802	543,311
91 days to 180 days	234,044	454,415
181 days to 365 days	17,277	21,690
Over 365 days	8,238	9,589
	1,037,361	1,029,005

9. Trade and Bills Payable

The aged analysis of the trade and bills payable as at the balance sheet date, based on invoice date, is as follows:

	30 June 2003 (unaudited) HK\$'000	31 December 2002 (audited) HK\$'000
Current to 90 days	1,446,918	2,391,738
91 days to 180 days	328,229	344,983
181 days to 365 days	18,632	17,780
Over 365 days	18,957	14,770
	1,812,736	2,769,271

Interim Results

10. Bank Borrowings

	30 June 2003 (unaudited) HK\$'000	31 December 2002 (audited) HK\$'000
Bank loans:		
Secured	—	6,630
Unsecured	409,434	400,000
	409,434	406,630
Bank loans repayable:		
Within one year	80,022	23,845
In the second year	94,118	94,443
In the third to fifth year, inclusive	235,294	283,389
Beyond five years	—	4,953
	409,434	406,630
Portion classified as current liabilities	(80,022)	(23,845)
Long term portion	329,412	382,785

At 31 December 2002, certain bank loans were secured by the Group's land and buildings with a total net book value of HK\$10,309,000.

11. Share Capital

	30 June 2003 (unaudited) HK\$'000	31 December 2002 (audited) HK\$'000
Authorised:		
5,000,000,000 shares of HK\$0.10 each	500,000	500,000
Issued and fully paid:		
2,650,019,451 (2002: 2,630,998,852) shares of HK\$0.10 each	265,002	263,100

Interim Results

11. Share Capital (Continued)

A summary of the movements in the Company's share capital is as follows:

	Number of shares issued	Paid-up nominal value HK\$'000
Issued capital at 1 January 2003	2,630,998,852	263,100
Share options exercised	19,020,599	1,902
Issued capital at 30 June 2003	<u>2,650,019,451</u>	<u>265,002</u>

Details of the movements in respect of the share option schemes during the period are set out under the "Share option schemes" section on page 28.

12. Reserves

	Share premium account HK\$'000	Capital reserve HK\$'000	Reserve funds HK\$'000	Exchange fluctuation reserve HK\$'000	Retained profits HK\$'000	Total HK\$'000
At 1 January 2003	1,205,670	66,204	427,321	14,772	1,396,386	3,110,353
Issue of shares upon exercise of share options	17,648	—	—	—	—	17,648
Exchange realignments	—	—	—	4,261	—	4,261
Write off of exchange reserve	—	—	—	145	—	145
Net profit for the period	—	—	—	—	265,369	265,369
Final 2002 dividend	—	—	—	—	(928)	(928)
At 30 June 2003	<u>1,223,318</u>	<u>66,204</u>	<u>427,321</u>	<u>19,178</u>	<u>1,660,827</u>	<u>3,396,848</u>

Interim Results

13. Capital Commitments

The Group had the following commitments at the balance sheet date:

	30 June 2003 (unaudited) HK\$'000	31 December 2002 (audited) HK\$'000
Contracted, but not provided for	102,080	169,772
Authorised, but not contracted for	3,462	10,854
	105,542	180,626

In addition, the Group's share of capital commitments of jointly-controlled entities not included in the above is as follows:

	30 June 2003 (unaudited) HK\$'000	31 December 2002 (audited) HK\$'000
Contracted, but not provided for	5,257	1,522

14. Contingent Liabilities

At balance sheet date, the Group had contingent liabilities not provided for in the financial statements in respect of:

	30 June 2003 (unaudited) HK\$'000	31 December 2002 (audited) HK\$'000
Bills receivable endorsed to suppliers	77,966	138,623
Bills discounted with recourse	429,059	1,086,659
	507,025	1,225,282

Interim Results

14. Contingent Liabilities (Continued)

In addition, the Group's share of contingent liabilities of jointly-controlled entities not included above is as follows:

	30 June 2003 (unaudited) HK\$'000	31 December 2002 (audited) HK\$'000
Bills receivable endorsed to suppliers	402,654	—
Bills discounted with recourse	875,731	341,267
	1,278,385	341,267

15. Related Party Transactions

The Group had the following material transactions with related parties during the period:

		Six months ended 30 June	
		2003 (unaudited) HK\$'000	2002 (unaudited) HK\$'000
	Notes		
Jointly-controlled entities:			
Sales of raw materials	(i)	605,663	203,977
Purchase of raw materials and finished goods	(ii)	610,350	32,637
Sales commission income	(iii)	522	20,416
Minority shareholder of a subsidiary:			
Sales of finished goods	(iv)	12,201	23,983
Rental expenses	(v)	1,585	—
Companies controlled by the ultimate holding company:			
Sales of raw materials	(i)	8,274	—
Purchase of raw materials	(ii)	180,356	160,780
Purchase of finished goods	(ii)	21,279	—
Sales handling fee income	(vi)	4,381	—
Contract fee	(vii)	15,004	13,535
Company controlled by a jointly-controlled entity:			
Purchase of raw materials	(ii)	34,237	28,699

Interim Results

15. Related Party Transactions (Continued)

Notes:

- (i) The sales of raw materials were made at cost.
- (ii) The purchases of raw materials and finished goods were made at prices similar to those set by independent third party suppliers.
- (iii) The sales commission was calculated at 10% of the retail price of the products distributed.
- (iv) The Group sold its finished goods at an average mark-up of 1.5% (2002: 2%).
- (v) The rent was determined with reference to open market rentals.
- (vi) The sales handling fee income was calculated at 1.7% of the invoiced sales of products distributed.
- (vii) The contract fee was the sum of the followings:
 - (1) A fee equivalent to 8% of net asset value of the contracted operation as at the end of preceding financial year; and
 - (2) Depreciation costs of the contracted operation for this financial year.

Management Discussion and Analysis

BUSINESS REVIEW AND OUTLOOK

Operational Highlights

For the six months ended 30 June 2003

	<i>Sales volume (Thousand)</i>		<i>% Change</i>
	2003	2002	
TVs — PRC market	3,251	3,054	+6%
— Overseas	1,472	512	+188%
Mobile Handsets	4,725	2,212	+114%
PCs	209	88	+138%

- The Group maintained an 18% market share in the domestic TV market.
 - Enhanced product mix with rapid rollout of high-end products increased its share in the high-end segment.
- Continued to record strong growth in overseas TV sales with a surge of 188%.
- Ranked as the top three best selling handset brands with a 12% market share in the domestic handset market.
 - The colour display handsets increased rapidly in the sales mix which helped maintain the gross margin and average selling price.
- Ranked as the 3rd best selling consumer desktop PC brand in China, with a 6% market share, and the 4th best selling PC brand in China.

Management Discussion and Analysis

The TV Business

Sales of TVs in the China market saw a slight decline in the first half of 2003. Nevertheless, as the proportion of high-end models in the total sales mix increased, sales turnover was up marginally. At the same time, the market saw a further consolidation towards major brands. Competition in high-end models intensified, with the battlefield shifting to rear projection and pure flat screen TVs.

During the period under review, the Group adjusted its product mix through the launch of new products. The widened product offering strengthened the Group's competitive edge in the different market segments. Domestic TV sales in China amounted to 3.25 million sets, representing a year-on-year growth of 6%. According to the Ministry of Information Industry, TCL's market share in the domestic TV market was 18% in the first half of 2003, staying on a similar level as last year.

A total of 43 new models were launched during the period under review. Among the new products, 17 were high-end TV models which include Plasma, HID rear projection, LCOS rear projection, LCD TVs etc. The remaining 26 were CRT TVs with enhanced progressive scanning functions. Statistics from the China Economy Consultancy indicate that TCL's share in rear projection TVs increased to 7%, ranking as the 7th in the PRC market, while TCL's plasma TVs accounted for 14% of the share to rank 3rd in the PRC marketplace.

Increased sales of high-end products in the first half of 2003 enabled TCL to maintain a stable average selling price. Unfortunately, since sales and marketing activities were delayed due to the outbreak of SARS in the second quarter, sales turnover in the first half of the year was lower than expected. Owing to ferocious market competition and the increase in CRT price which was exceptionally low in the first half of 2002, the earnings of this business were lower than the corresponding period last year, with the gross margin narrowing from 22% to 19% this year.

The Group achieved a major breakthrough in the development and application of driving circuitry and control technology of Plasma TVs in China. These pioneering technologies were recognized by the State as one of the most advanced in China.

The Handset Business

The demand for mobile handsets remained strong during the period under review. In an effort to increase market share, handset manufacturers speeded up product rollout to stimulate consumption sentiment, intensifying market competition.

Management Discussion and Analysis

With an acclaimed brand name and superb product design, sales of TCL handsets continued to grow strongly by 114% to 4.72 million handsets during the period under review. According to the Ministry of Information Industry, TCL enjoyed a 12% market share, ranked as the third best selling handset brand in the PRC in the first half of 2003.

In line with the Group's expectation, the average selling price in the first half of 2003 decreased while inventory increased — a result of the rigorous competition and the adverse impact of SARS. In spite of these factors, riding on its cost advantage, economies of scale, product differentiation and effective marketing strategies, the Group met its preset sales target and penetrated into the high-end colour display and low end markets.

In response to market changes, the Group increased the scale of its chipset-based production and its ratio in total manufacturing output to lower production costs. A total of 15 new handset products were launched during the period under review, including colour display models as well as handsets with camera functions. Receiving overwhelming market response, the Group believes that sales of colour display models will rise continuously, stabilizing the overall gross margin and the average selling price.

The PC Business

The PC industry in China recorded double-digit growth in the first half of 2003. With respect to product prices, the price line continued to move down as no technological breakthrough in terms of CPUs or related parts were developed. While the application of PCs as a domestic electrical appliance is still in an infancy stage, the Group expects this application to enjoy higher popularity within a year or two.

PC business was not hurt by the SARS outbreak. Following its operational restructuring and enhancement, the PC business showed a solid and stable growth trend. The Group is pleased to see that sales increased during peak seasons, remained stable during low tides, and resulted in record growth.

Sales of PCs in the first half of 2003 increased by 138% to 209,000 sets. According to an IDC report released in the first quarter this year, TCL was ranked number 3 in the home desktop PC market, with a share of 6%, while the ranking in the overall PC industry was number 4, with a share of 3%. These satisfactory performances have reduced the distance between TCL and other major players.

Cost control is regarded as a major task during the period under review. Launching a "Customised PCs" initiative, the Group is focused on optimizing R&D, procurement, logistics, etc. Gross margin increased from 8% to 9%. Addressing the gradual decline in product prices, the Group improved its earnings by expanding the sales network, strengthening the supply chain, streamlining its retail shop fronts as

Management Discussion and Analysis

well as maintaining product competitiveness. Meeting the trend of applying PCs as a general domestic electrical appliance, the "Ruixiang 7000" series PC, the Group's key high end product that carries standalone TV viewing functions, recorded satisfactory sales during the period under review.

The Overseas Business

In addition to its customer-driven and market-oriented focus, the Group is also committed to developing its business globally. Overseas TV sales, having grown significantly in 2002, experienced further high growth in the first half of 2003. Sales achieved in the first half of this year exceeded full year sales of 2002. Overseas TV exports increased 1.9 times during the period, with sales of both TCL branded and OEM products reaping fruitful results. However, as the percentage of sales in the OEM business increased slightly, the overall gross margin decreased marginally.

TCL branded TVs are primarily sold in Southeast Asian markets and are widely accepted in these regions. Sales recorded a year-on-year increase of over 20%. As these markets become more mature and are ready for large display TVs and high end products, the Group is exposed to ample growth opportunities. The Group will continue to develop both TCL branded and OEM products. With existing markets forming the solid basis for business expansion, it will continue to explore nearby markets and new emerging markets.

During the period under review, the anti-dumping lawsuit against the import of CRT TVs of over 21" in size to the US market was submitted to the US Department of Commerce (DOC) and US International Trade Committee (ITC). Results of the ruling will not be available until the first half of 2004. Although the Group did not adopt a low pricing strategy to acquire market share, in face of the uncertainty, the Group is prepared to take necessary steps to adjust its US business strategy.

Schneider in Germany was still in its investment stage during the period under review, incurring a loss of about HK\$23 million. Despite the loss, the Group made considerable progress in developing its business network in Europe. It has also developed and realized new product series to be launched at the IFA Consumer Electronic Products Expo in Berlin by the end of August. It is anticipated that the new products launched at the IFA will be the key products for the second half of 2003. As such, the Group expected Schneider's business to be in full operation after the IFA Expo.

The AV Business

Markets in the urban area grew rapidly during the period under review. Prices of DVDs declined despite the increase in market size. No major change was seen in the market for VCDs, whereas the demand for Super VCDs decreased substantially.

Management Discussion and Analysis

As is the case with other businesses, the AV business was adversely affected by SARS. Sales revenues from the AV business were therefore lower than expected. However, with improved operational efficiencies, losses were narrowed.

The Group launched a mini audio system 5.1 compact set during the first half of the year. The light-weight product with good sound quality was welcomed by customers. It stands a good chance of becoming a popular mainstream consumer product in the near future.

In response to market changes, the Group underwent an internal management restructuring in research and development, procurement and sales in order to generate synergies and to strike a balance between domestic and overseas markets so that the two arms complement each other. The Group also adopted an adjusted strategy — penetrating the market with low-end products while building a quality image with high-end products. The rollout of low-end products was expedited to meet this goal. A handful of new products will be released in the second half of the year.

The IT Business

The Group strategically adjusted the focus of its distance learning business during the period under review, moving from offering network education service for the China Central Radio Television University (CCRTU), to a self-developed open distance-learning educational platform for the community as a part of the public services. In addition, the Group also launched an examination software, a search engine for the CCRTU, and a distance training and educational management system. In terms of R&D development, the Group expanded from a single formal academic software product to include the provision of both academic and non-academic educational software products on a diversified range of topics.

To consolidate its resources for the development of distance education, the Group has entered into an agreement for the disposal of its networking equipment business. An accounting profit of about HK\$2 million will be realized upon the completion of the transaction. The market for distance education is emerging. Though in a premature stage, it is rapidly gaining ground in terms of acceptance and understanding in the community. The Group believes that it will soon become a major focal point for consumer spending.

Management Discussion and Analysis

Future Outlook

Having experienced the difficulties brought about by SARS, we are pleased to see that SARS is now under successful control, and business in general is returning to normal. For the domestic TV business, the Group will increase its sales and distribution capabilities in the first and second-tier markets in the second half of the year. It will also strengthen its high-end product range to enhance earnings and reinforce its market leadership.

As the inventory for handsets started to pile up in the market, in parallel with keener market competition, manufacturers are facing higher uncertainties. The average selling price is expected to decrease even further under the current fragmented, complicated, and unstable market environment. It is expected that the market will experience a consolidation phase, and inevitably only the strong players will survive. The Group will be devoting resources to build its brand and introduce new market-driven products, strengthening product differentiation and speeding up the pace of new product launches. To bolster its presence further and increase market share, the Group will further penetrate the market with both low-end products as well as high-end colour display models.

In the PC business, TCL will concentrate on raising its competitiveness. Looking in the second half of the year, the Group's strategy will be focused on the provision of "Customised TCL PCs". The Group will keep an eye on opportunities for the establishment of new sales points. The aim is to achieve a sales breakthrough during the high season through a highly flexible product combination. New products to be launched will offer a comprehensive solution for the set up of a "personal AV centre", while PCs for commercial use will, building on the foundation of TCL's advantages in the educational sector, extend to government units and related projects to pursue volume growth.

Manufacturers in China are playing an increasingly important role in the international arena after China's entry into WTO. Competition on a global basis, in conjunction with the adjustments within the industry, have brought about both opportunities and challenges. Under this backdrop, the Group is formulating a global strategy that will optimize its position, attend to market changes, and encourage innovation. In anticipation of continued growth in the second half of the year, the Group will stiffen its competitive edge by exploring win-win opportunities with strategic alliance partners to deepen relationships. These initiatives will all drive towards one goal — to boost TCL's competitiveness in the international marketplace.

Management Discussion and Analysis

FINANCIAL REVIEW

Results

The Group achieved a turnover of approximately HK\$6,248 million for the first half of 2003, representing an increase of 16% compared to the same period last year. Profit attributable to shareholders was HK\$265 million, compared to the corresponding period last year of HK\$253 million. Televisions and mobile handsets business continued to be the Group's major profit contributors. Profit from TV and mobile handsets represented 54% and 50%, respectively, of the Group's net profit in the current year.

Turnover and gross margin of televisions was HK\$5,179 million and 17.4% respectively, an increase of 21.6% and a decrease of 3.4% as compared to the same period last year. The major growth in turnover came from export sales. Export sales represented 20% of the total TV sales in 2003 (2002: 10%). The generally lower margin of the exports sales resulted in the decline in overall gross margin from 20.8% in 2002 to 17.4% in the current year. Operating profit is further affected by the initial set-up and investment cost of Schneider, our new sales and manufacturing arm in Europe.

Mobile handsets business continued to maintain its leading position in the PRC. Turnover increased more than 59% to HK\$4,880 million. As expected, as a result of severe competition and the Group's strategy to broaden its product mix to mid-end product lines, overall gross margin of handsets reduced by 6% to 20%.

With the gradual recovery of the PC industry in China and the Group's effective cost-control policies, turnover of PCs surged by 86% to HK\$728 million with gross margin of 9%, a slight improvement as compared with last year.

The unexpected outbreak of the SARS in China and other parts of the world during the second quarter of 2003 had a widespread effect on both the domestic and international economy. Under this backdrop, consumer consumption weakened, and the May 1st national holidays, which is usually associated with strong spending sprees, passed without much sales stimulation this year. Sales of TVs and handsets slowed down during the second quarter as a result. Despite all these challenges, being a leading consumer electronic brand in the PRC, and with the Group's successful experience in beating other competitors during the TV price war in the previous years, we have full confidence of meeting our sales target, maintaining a reasonable level of margin and continue to provide satisfactory return to shareholders.

Management Discussion and Analysis

Significant Acquisitions and Disposals

On 18 June 2003, the Group entered into an agreement with subsidiaries of TCL Corporation, its ultimate holding company, for the disposal of the entire equity interest in TCL 網絡設備(深圳)有限公司 ("TCL Network") at a consideration of approximately HK\$12.5 million. The principal activity of TCL Network is the development and sale of computer network equipment. Details of the transaction are set out in the Company's announcement dated 18 June 2003.

Apart from the disposal as set out above and certain additions to the Group's plant and equipment, there was no major investment or disposals during the period. Total capital expenditure amounted to approximately HK\$159 million.

Liquidity and Financial Resources

The Group consistently maintained a strong liquidity position throughout the period. Through its centralized treasury function, the Group was able to make efficient allocation of its financial resources and reduce any unnecessary financial expenses. The cash and bank balances as at 30 June 2003 amounted to HK\$729 million, of which 24% was maintained in Hong Kong Dollars, 40% in US Dollars, 33% in Renminbi and 3% in other currencies for the overseas operations. At the period end, all the bank loans were clean loans without any charges or securities required. All of them were subject to floating interest rates. The Group's gearing ratio at the period end was 0.2 which is calculated based on the Group's total interest-bearing borrowings at approximately HK\$759 million and the shareholders' funds of approximately HK\$3,662 million.

There was no material change in available credit facilities when compared with the year ended 31 December 2002 and there was no asset held under finance lease at the period end. Convertible notes were subject to fixed interest rate at 3% per annum. No convertible notes were converted or redeemed during the period.

Foreign Exchange Exposure

Since most business transactions conducted by the Group and payments made to suppliers are made in either Hong Kong Dollars, US Dollars or Renminbi, no use of financial instruments for hedging purposes is considered necessary.

Management Discussion and Analysis

Employees and Remuneration Policy

The Group had a total of 18,000 dynamic and talented employees, of which approximately 3% was management level, 18% was technical staff, 9% was clerical staff, 30% was sales & marketing staff, and 40% was workers. They were all dedicated to advancing the quality and reliability of our operations. Total staff costs for the period was HK\$221 million. Remuneration policy was reviewed regularly, making reference to current legislation, market condition and both the individual and company performance. In order to align the interests of staff with those of shareholders, share options were granted to employees under the Company's share option schemes. Share options granted to directors and employees and remained outstanding at the period end totaled 103,481,838 units.

Other Information

DIRECTORS' INTERESTS

As at 30 June 2003, the interests and short positions in the shares, underlying shares and debentures of the Company and its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance ("SFO")) as recorded in the register kept by the Company under Section 352 of the SFO were as follows:

(A) Long Positions in Shares of the Company

<u>Directors</u>	<u>Capacity</u>	<u>No. of shares held</u>	<u>% of issued share capital of the Company</u>
Li Dong Sheng, Tomson	Beneficial owner	21,206,000	0.80
Lu Zhong Li	Beneficial owner	10,500,000	0.40
Yan Yong	Beneficial owner	200,000	0.01
Suen Hay Wai	Beneficial owner	176,000	0.01
Wong Toe Yeung (Resigned on 19 July 2003)	Beneficial owner	1,000,000	0.04

(B) Long Positions in Underlying Shares of the Company

Convertible Notes:

<u>Director</u>	<u>Capacity</u>	<u>No. of underlying shares held</u>
Wong Toe Yeung (Resigned on 19 July 2003)	Interest of controlled corporation	121,283,254 underlying shares under 3% convertible notes due 2005 (<i>Note</i>)

Note: Wong Toe Yeung is deemed to be interested in 121,283,254 underlying shares under 3% convertible notes due 2005 (i.e. 82,159,624 and 39,123,630 underlying shares were respectively held by United Asset Investments Limited and Go-Win Limited, in each of which he has entire interest.)

Other Information

Share Option Schemes

The following share options were outstanding under the share option schemes during the period:

Name or category of participant	Number of share options				At 30 June 2003	Date of grant	Exercise price HK\$	Exercise period	Price of Company's shares	
	At 1 January 2003	Granted during the period	Exercised during the period	Lapsed during the period					at date of grant* HK\$	at date of exercise# HK\$
Directors										
Li Dong Sheng, Tomson	12,000,000	—	—	(12,000,000)	—	3 December 1999	2.236	Note 1	3.075	
	—	6,950,000	—	—	6,950,000	15 May 2003	1.550	Note 7	1.590	
	<u>12,000,000</u>	<u>6,950,000</u>	<u>—</u>	<u>(12,000,000)</u>	<u>6,950,000</u>					
Yuan Xin Cheng	6,000,000	—	—	(6,000,000)	—	3 December 1999	2.236	Note 1	3.075	
	—	5,300,000	—	—	5,300,000	15 May 2003	1.550	Note 7	1.590	
	<u>6,000,000</u>	<u>5,300,000</u>	<u>—</u>	<u>(6,000,000)</u>	<u>5,300,000</u>					
Lu Zhong Li	5,000,000	—	—	(5,000,000)	—	3 December 1999	2.236	Note 1	3.075	
	—	4,600,000	—	—	4,600,000	15 May 2003	1.550	Note 7	1.590	
	<u>5,000,000</u>	<u>4,600,000</u>	<u>—</u>	<u>(5,000,000)</u>	<u>4,600,000</u>					
Hu Qiu Sheng	5,000,000	—	—	(5,000,000)	—	3 December 1999	2.236	Note 1	3.075	
	—	4,600,000	—	—	4,600,000	15 May 2003	1.550	Note 7	1.590	
	<u>5,000,000</u>	<u>4,600,000</u>	<u>—</u>	<u>(5,000,000)</u>	<u>4,600,000</u>					
Yan Yong	300,000	—	—	(300,000)	—	1 June 2000	2.508	Note 2	3.200	
	200,000	—	(200,000)	—	—	2 May 2001	0.928	Note 3	1.130	
	—	200,000	—	—	200,000	30 January 2003	2.114	Note 6	2.075	
	—	1,550,000	—	—	1,550,000	15 May 2003	1.550	Note 7	1.590	
	<u>500,000</u>	<u>1,750,000</u>	<u>(200,000)</u>	<u>(300,000)</u>	<u>1,750,000</u>					
Suen Hay Wai	—	700,000	—	—	700,000	30 January 2003	2.114	Note 6	2.075	
Wong Toe Yeung ^o	3,000,000	—	(1,000,000)	(2,000,000)	—	3 December 1999	2.236	Note 1	3.075	
Other employees	30,000	—	—	(30,000)	—	1 June 2000	2.508	Note 2	3.200	
	9,066,000	—	(8,870,000)	(196,000)	—	2 May 2001	0.928	Note 3	1.130	
	23,432,437	—	(8,950,599)	—	14,481,838	29 October 2001	0.994	Note 4	0.990	
	10,000,000	—	—	—	10,000,000	4 November 2002	2.305	Note 5	2.175	
	—	50,100,000	—	—	50,100,000	30 January 2003	2.114	Note 6	2.075	
	—	5,000,000	—	—	5,000,000	15 May 2003	1.550	Note 7	1.590	
	<u>42,528,437</u>	<u>55,100,000</u>	<u>(17,820,599)</u>	<u>(226,000)</u>	<u>79,581,838</u>					
<u>74,028,437</u>	<u>79,000,000</u>	<u>(19,020,599)</u>	<u>(30,526,000)</u>	<u>103,481,838</u>						

^o Wong Toe Yeung resigned from directorship on 19 July 2003.

Other Information

Note 1: The exercise period for such share options commenced from the expiry of three years from the respective commencement date of services of each grantee with the Group. Such dates ranged from 3 December 1999 to 1 December 2002, and ended on 14 May 2003.

Note 2: One-third of such share options was exercisable after the expiry of 9 months from the date of grant, a further one-third was exercisable after the expiry of 18 months from the date of grant, and the remaining one-third was exercisable after the expiry of 27 months from the date of grant, up to 14 May 2003.

Note 3: Half of such share options was exercisable after the expiry of 9 months from the date of grant, and the remaining half was exercisable after the expiry of 18 months from the date of grant, up to 14 May 2003.

Note 4: One-third of such share options is exercisable after the expiry of 9 months from the date of grant, a further one-third is exercisable after the expiry of 18 months from the date of grant, and the remaining one-third is exercisable after the expiry of 27 months from the date of grant, up to 28 April 2005.

Note 5: Such share options are exercisable after the expiry of 9 months from the date of grant, up to 3 May 2006.

Note 6: One-third of such share options is exercisable after the expiry of 9 months from the date of grant, a further one-third is exercisable after the expiry of 18 months from the date of grant, and the remaining one-third is exercisable after the expiry of 27 months from the date of grant, up to 29 July 2006.

Note 7: Such share options are exercisable at any time from the date of grant to 14 November 2006.

** The price of the Company's shares disclosed as at the date of grant of the share options is the Stock Exchange of Hong Kong Limited ("Stock Exchange") closing price on the trading day immediately prior to the date of grant of the options.*

The price of the Company's shares disclosed as at the date of the exercise of the share options is the weighted average of the Stock Exchange closing prices over all of the exercises of options within the disclosure category.

Other Information

(C) Long Position in shares of associated corporations of the Company

Directors	Name of associated corporation	Capacity	% of interest in associated corporation
Li Dong Sheng, Tomson	TCL Corporation	Beneficial owner	9.08
Yuan Xin Cheng	TCL Corporation	Beneficial owner	1.56
Lu Zhong Li	TCL Corporation	Beneficial owner	1.48
Hu Qiu Sheng	TCL Corporation	Beneficial owner	1.19
Wong Toe Yeung (Resigned on 19 July 2003)	Huizhou TCL Mobile Communication Co., Ltd. ("TCL Mobile")	Interest of controlled corporation	19.00 (Note)

Note: Wong Toe Yueng is deemed to be interested in 19% interest in TCL Mobile (i.e. 9% and 10% interest were respectively held by Jasper Ace Limited and Cheerful Asset Investment Limited in which he has 100% and 50% interest respectively.)

Save as disclosed above, none of the Directors or chief executives of the Company had, as at 30 June 2003, any interests or short positions in the shares, underlying shares and debentures of the Company or any of its associated corporations (within the meaning of Part XV of the SFO) which were recorded in the register required to be kept by the Company under Section 352 of the SFO.

Other Information

SUBSTANTIAL SHAREHOLDERS' INTERESTS

So far as is known to any Director or chief executives of the Company, as at 30 June 2003, shareholders (other than Directors or chief executives of the Company) who had interests or short positions in the shares or underlying shares of the Company which were recorded in the register kept by the Company under Section 336 of the SFO were as follows:

Long Positions in shares of the Company

<u>Shareholders</u>	<u>Capacity</u>	<u>No. of shares held</u>	<u>% of issued share capital of the Company</u>
T.C.L. Industries Holdings (H.K.) Ltd.	Beneficial owner	1,461,685,289 <i>(Note 1)</i>	55.16
TCL Corporation	Interest of controlled corporation	1,461,685,289 <i>(Note 2)</i>	55.16
Huizhou Investment Holdings Limited	Interest of controlled corporation	1,461,685,289 <i>(Note 3)</i>	55.16

Note 1: 1,461,685,289 shares of the Company are held by T.C.L. Industries Holdings (H.K.) Ltd. in the capacity of beneficial owner.

Note 2: TCL Corporation is deemed to be interested in 1,461,685,289 shares of the Company through T.C.L. Industries Holdings (H.K.) Ltd., its wholly owned subsidiary. These interests are duplicated in the interests described in Note 1 above.

Note 3: Huizhou Investment Holdings Limited is deemed to be interested in 1,461,685,289 shares of the Company through its 40.97% interest in TCL Corporation. These interests are duplicated in the interests described in Notes 1 and 2 above.

Save as disclosed above, as at 30 June 2003, the Company has not been notified by any persons (other than Directors or chief executives of the Company) who had interests or short positions in the shares or underlying shares of the Company which were recorded in the register required to be kept by the Company under Section 336 of the SFO.

Other Information

PURCHASE, SALE OR REDEMPTION OF SHARES

Neither the Company, nor any of its subsidiaries purchased, sold or redeemed any of the Company's listed securities during the period under review.

CODE OF BEST PRACTICE

In the opinion of the directors, the Company has complied with the Code of Best Practice as set out in Appendix 14 of the Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong Limited during the period.

On behalf of the Board
LI Dong Sheng, Tomson
Chairman

Hong Kong, 20 August 2003