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If you are in any doubt as to any aspect of this circular or as to the action to be taken, you should consult your licensed securities dealer, bank manager, solicitor, professional accountant or other professional adviser.

If you have sold or transferred all your shares in China Electronics Corporation Holdings Company Limited, you should at once hand this circular and the accompanying form of proxy to the purchaser or the transferee or to the bank, licensed securities dealer or other agent through whom the sale or transfer was effected for transmission to the purchaser or the transferee.

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CHINA ELECTRONICS CORPORATION HOLDINGS COMPANY LIMITED

中國電子集團控股有限公司*

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

(Stock Code: 00085)

**MAJOR TRANSACTION,
CONNECTED TRANSACTION
AND
CONTINUING CONNECTED TRANSACTIONS**

*Independent Financial Adviser to the Independent Board Committee
and the Independent Shareholders*

ALTUS CAPITAL LIMITED

A notice convening a special general meeting of the Company to be held at 3:00 p.m. on Monday, 21 July 2008 at Plaza I-III, Lower Lobby, Novotel Century Hong Kong, 238 Jaffe Road, Wanchai, Hong Kong is set out on pages 158 to 160 of this circular. Whether or not you are able to attend the special general meeting, you are requested to complete the accompanying form of proxy, in accordance with the instructions printed thereon and return the same to the Company's branch share registrar in Hong Kong, Tricor Abacus Limited, at 26th Floor, Tesbury Centre, 28 Queen's Road East, Wanchai, Hong Kong as soon as possible and in any event not less than 48 hours before the time appointed for holding the special general meeting or any adjournment thereof. Completion and return of the form of proxy will not preclude you from attending and voting in person at the special general meeting or any adjournment thereof should you so wish.

A letter from the independent board committee of the Company containing its recommendation to the independent shareholders of the Company is set out on pages 34 to 35 of this circular. A letter from Altus Capital Limited, the independent financial adviser, containing its advice to the independent board committee and the independent shareholders of the Company is set out on pages 36 to 53 of this circular.

** For identification purpose only*

30 June 2008

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DEFINITIONS

In this circular, unless the context otherwise requires, the following expressions have the following meanings:

“Acquisition”	together, the China Hua Da Acquisition, the Beijing Shoufa Xinan Acquisition and the Other Vendors Acquisition
“Altus”	Altus Capital Limited, a licensed corporation to carry out type 4 (advising on securities), type 6 (advising on corporate finance) and type 9 (asset management) regulated activities under the SFO, being the independent financial adviser to the Independent Board Committee and the Independent Shareholders in respect of the terms of the Acquisition and the terms of the Non-exempt Continuing Connected Transactions
“associates”	has the meaning ascribed to this term under the Listing Rules
“Beijing Hua Da Xinan”	北京華大信安科技有限公司 (Beijing Huada Infosec Technology Co., Ltd.), a company established under the law of the PRC
“Beijing Huada Zhibao”	北京華大智寶電子系統有限公司 (Beijing Huada Zhibao Electronic System Co., Ltd.), a company established under the law of the PRC
“Beijing Shoufa Xinan”	北京首發信安數據系統科技有限公司 (Beijing Shoufa Xinan Data System Technology Company Limited), a company established under the law of the PRC, the vendor under the Beijing Shoufa Xinan Agreement
“Beijing Shoufa Xinan Acquisition”	the acquisition of a 7.50% equity interest in Hua Da Electronics by the Company from Beijing Shoufa Xinan pursuant to the Beijing Shoufa Xinan Agreement
“Beijing Shoufa Xinan Agreement”	the conditional equity transfer agreement dated 20 June 2008 entered into between the Company and Beijing Shoufa Xinan in relation to the Beijing Shoufa Xinan Acquisition
“Board”	the board of Directors

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“Business Day”	a day (excluding Saturdays) on which banks in Hong Kong and the PRC are generally open for the transaction of normal banking business
“Business Services Agreement”	the business services agreement dated 17 June 2004 and entered into between CEC and Sang Fei as supplemented by the supplemental business services agreement dated 21 December 2006 and entered into between Sang Fei and CEC
“CEC”	中國電子信息產業集團公司 (China Electronics Corporation), a state-owned enterprise established under the laws of the PRC, the Company’s ultimate controlling Shareholder
“CEC Finance”	中國電子財務有限責任公司 (China Electronics Corporation Finance Co., Ltd.)
“CEC Group”	CEC and its subsidiaries (other than the Group)
“China Hua Da”	中國華大集成電路設計集團有限公司 (China Huada Integrated Circuit Design (Group) Co., Ltd.), a company established under the laws of the PRC, the vendor under the China Hua Da Agreement
“China Hua Da Acquisition”	the acquisition of the 64.75% equity interest in Hua Da Electronics by the Company pursuant to the China Hua Da Agreement
“China Hua Da Agreement”	the conditional equity transfer agreement dated 20 June 2008 entered into between the Company and China Hua Da in relation to the China Hua Da Acquisition
“CIDC”	CIDC (H.K.) Limited, a company incorporated in Hong Kong
“Company”	China Electronics Corporation Holdings Company Limited
“Completion”	completion of the China Hua Da Acquisition, the Beijing Shoufa Xinan Acquisition and the Other Vendors Acquisition in accordance with the terms of the China Hua Da Agreement, the Beijing Shoufa Xinan Agreement and the Other Vendors Agreement, respectively

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“connected person”	has the meaning ascribed to this term under the Listing Rules
“Consideration Shares”	608,000,000 new Shares to be allotted and issued at the Issue Price for settlement of the consideration for the Acquisition and a “Consideration Share” shall be construed accordingly
“Continuing Connected Transactions”	the continuing connected transactions described in the paragraph headed “Continuing Connected Transactions” in the section headed “Letter from the Board” of this circular
“Deposit Services Agreement”	the deposit services agreement dated 20 September 2007 and entered into between Sang Fei and CEC Finance
“Directors”	the directors of the Company
“Enlarged Group”	the Group immediately after completion of the Acquisition
“Excluded Assets”	together, a 71.26% equity interest in Beijing Hua Da Xinan, a 80% equity interest in Guangdong Hua Da and Hua Da Electronics’ entire shareholding in CIDC
“Great Wall Tenancy Agreement”	the tenancy agreement dated 3 July 2006 entered into between Great Wall Technology Company Limited and China Great Wall Computer (Shenzhen) Co., Ltd. as landlords and Sang Fei as tenant in relation to the lease of the factory premises situated at Nanshan District, Shenzhen, PRC
“Group”	the Company and its subsidiaries
“Guangdong Hua Da”	廣東華大集成電路設計有限責任公司 (Guangdong Huada Electronic Design Co., Ltd.), a company established under the law of the PRC
“HK\$”	Hong Kong dollars, the lawful currency of Hong Kong
“Hong Kong”	the Hong Kong Special Administrative Region of the PRC

DEFINITIONS

“Hua Da Business Services Agreement”	the business services agreement dated 20 June 2008 entered into between CEC and Hua Da Electronics
“Hua Da Deposit Services Agreement”	the deposit services agreement dated 20 June 2008 entered into between CEC Finance and Hua Da Electronics
“Hua Da Electronics” or “Target Company”	北京中電華大電子設計有限責任公司 (CEC Huada Electronic Design Co., Ltd.), a company established under the laws of the PRC
“Hua Da Tenancy Agreement”	the tenancy agreement dated 20 June 2008 entered into between Beijing Huada Zhibao as landlord and Hua Da Electronics as tenant in relation to the lease of the premises located at Beijing, PRC
“Hua Da Group” or “Target Group”	Hua Da Electronics and its then subsidiaries
“Independent Board Committee”	the committee of Directors consisting of Mr. Chan Kay Cheung, Mr. Wong Po Yan and Mr. Yin Yongli, being all the independent non-executive Directors, formed to advise the Independent Shareholders in respect of the terms of the Acquisition and the Non-exempt Continuing Connected Transactions
“Independent Shareholders”	Shareholders other than CEC and its associates
“Issue Price”	the issue price of HK\$2.50 per Consideration Share
“Last Trading Day”	20 June 2008, being the last trading day prior to the entering into of the Agreement
“Latest Practicable Date”	27 June 2008, being the latest practicable date prior to the printing of this circular for the purpose of ascertaining certain information contained in this circular
“Listing Committee”	the listing committee of the Stock Exchange
“Listing Rules”	the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited

DEFINITIONS

“Non-exempt Continuing Connected Transactions”	the continuing connected transactions contemplated under the Hua Da Business Services Agreement, such transactions and agreement are further described under the paragraph headed “Continuing Connected Transactions” in the section headed “Letter from the Board” of this circular
“Option(s)”	option(s) which have been granted under the Company’s share option scheme approved and adopted by the Shareholders on 20 June 2002
“Other Vendors”	Ms. Wang Qinsheng, Mr. Liu Weiping, Mr. Dong Haoran, Mr. Huang Guoyong, Mr. Sun Xiaonian, Mr. Cheng Jing, Mr. Xiao Gang and Mr. Jiang Shiping, being all the vendors under the Other Vendors Agreement
“Other Vendors Acquisition”	the acquisition of an aggregate of 27.75% equity interest in Hua Da Electronics by the Company pursuant to the Other Vendors Agreement
“Other Vendors Agreement”	the conditional equity transfer agreement dated 20 June 2008 entered into between the Company and the Other Vendors in relation to the Other Vendors Acquisition
“PRC”	the People’s Republic of China
“RMB”	Renminbi, the lawful currency of the PRC
“Sang Da Tenancy Agreement”	the tenancy agreement dated 9 April 2008 entered into between 深圳市桑達實業股份有限公司 (Shenzhen SED Industry Co., Ltd.), a member of the CEC Group, as landlord and Sang Fei as tenant in relation to the lease of the premises situated at Levels 2 to 5 and a multi-purpose room on Level 4 of Sang Da Technology Building, Keji Road, Technology and Industrial Park, Nanshan District, Shenzhen, PRC
“Sang Fei”	深圳桑菲消費通信有限公司 (Shenzhen Sang Fei Consumer Communications Company Limited), a sino-foreign equity joint venture company established in the PRC and owned as to 65% by the Company
“SFO”	the Securities and Futures Ordinance (Chapter 571 of the Laws of Hong Kong)

DEFINITIONS

“SGM”	the special general meeting of the Company convened to be held on 21 July 2008 to consider and, if thought fit, to approve the Acquisition and the Non-exempt Continuing Connected Transactions, notice of which is set out at the end of this circular
“Share(s)”	ordinary shares in the Company’s issued share capital with a par value of HK\$0.01 per share which are listed on the Stock Exchange
“Shareholder(s)”	shareholder(s) of the Company
“Stock Exchange”	The Stock Exchange of Hong Kong Limited
“%”	per cent.

For ease of reference only, the names of PRC established companies and entities have been included in this circular in both Chinese and English and the English names of these companies and entities are either English translations of their respective official Chinese names or English tradenames used by them. In the event of any inconsistency between the English names and their respective Chinese names, the Chinese names shall prevail.



CHINA ELECTRONICS CORPORATION HOLDINGS COMPANY LIMITED

中國電子集團控股有限公司*

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

(Stock Code: 00085)

Non-executive Directors:

Xiong Qunli (*Chairman*)

Tong Baoan (*Vice Chairman*)

Executive Directors:

Fan Qingwu (*Managing Director*)

Hua Longxing

Independent Non-executive Directors:

Chan Kay Cheung

Wong Po Yan

Yin Yongli

Registered office:

Clarendon House

2 Church Street

Hamilton HM 11

Bermuda

*Principal place of business
in Hong Kong:*

Room 3503, 35th Floor

China Resources Building

26 Harbour Road

Wanchai

Hong Kong

30 June 2008

To the Shareholders

Dear Sir or Madam,

**MAJOR TRANSACTION,
CONNECTED TRANSACTION
AND
CONTINUING CONNECTED TRANSACTIONS**

INTRODUCTION

On 20 June 2008, the Board announced that the Company had, on the same date after trading hours, entered into the China Hua Da Agreement, the Beijing Shoufa Xinan Agreement and the Other Vendors Agreement in respect of the China Hua Da Acquisition, the Beijing Shoufa Xinan Acquisition and the Other Vendors Acquisition, respectively.

Pursuant to the China Hua Da Agreement, the Company has conditionally agreed to purchase and China Hua Da has conditionally agreed to sell a 64.75% equity interest in Hua

* For identification purpose only

LETTER FROM THE BOARD

Da Electronics at a consideration of HK\$984.20 million. Pursuant to the Beijing Shoufa Xinan Agreement, the Company has conditionally agreed to purchase and Beijing Shoufa Xinan has conditionally agreed to sell a 7.50% equity interest in Hua Da Electronics at a consideration of HK\$114 million. Pursuant to the Other Vendors Agreement, the Company has conditionally agreed to purchase and the Other Vendors have conditionally agreed to sell an aggregate equity interest of 27.75% in Hua Da Electronics at an aggregate consideration of HK\$421.80 million. Completions of each of the China Hua Da Agreement, the Beijing Shoufa Xinan Agreement and the Other Vendors Agreement are not conditional upon each other.

The aggregate consideration payable by the Company under the China Hua Da Agreement, the Beijing Shoufa Xinan Agreement and the Other Vendors Agreement is HK\$1,520 million, which shall be satisfied by the Company allotting and issuing an aggregate of 608,000,000 Consideration Shares, credited as fully paid, at an issue price of HK\$2.50 per Consideration Share, among which, 393,680,000 Consideration Shares will be allotted and issued to China Hua Da, 45,600,000 Consideration Shares will be allotted and issued to Beijing Shoufa Xinan and an aggregate of 168,720,000 Consideration Shares will be allotted and issued to the Other Vendors. The Consideration Shares will be allotted and issued on the completion date of the China Hua Da Agreement, the Beijing Shoufa Xinan Agreement and the Other Vendors Agreement.

After Completion, Hua Da Electronics will be converted into a wholly foreign-owned enterprise and will become a wholly-owned subsidiary of the Company and the financial statements of Hua Da Electronics will be consolidated into those of the Group.

China Hua Da is owned as to 50% by CEC, the ultimate controlling shareholder of the Company holding approximately 74.98% of the issued Shares as at the Latest Practicable Date. Accordingly, China Hua Da is a connected person of the Company and the China Hua Da Acquisition constitutes a connected transaction of the Company.

The China Hua Da Acquisition, the Beijing Shoufa Xinan Acquisition and the Other Vendors Acquisition, when aggregated, constitute a major transaction of the Company and are subject to the shareholders' approval requirements under the Listing Rules.

Since the China Hua Da Acquisition also constitutes a connected transaction of the Company and that CEC is considered to have a material interest in the Beijing Shoufa Xinan Acquisition and the Other Vendors Acquisition, CEC and its associates are required to abstain from voting on the ordinary resolutions approving the China Hua Da Acquisition, the Beijing Shoufa Xinan Acquisition and the Other Vendors Acquisition. Each of the China Hua Da Acquisition, the Beijing Shoufa Xinan Acquisition and the Other Vendors Acquisition is conditional upon, among other things, the approval by the Independent Shareholders at the SGM.

After completion of the China Hua Da Acquisition, the transactions contemplated under the Hua Da Business Services Agreement, the Hua Da Deposit Services Agreement and the Hua Da Tenancy Agreement will constitute continuing connected transactions of the Company under the Listing Rules.

LETTER FROM THE BOARD

Apart from the Hua Da Business Services Agreement, Sang Fei, the principal operating subsidiary of the Company, has also entered into the Business Services Agreement with CEC to set out the framework for the ongoing business relationship between the CEC Group and Sang Fei. Apart from the Hua Da Deposit Services Agreement, Sang Fei has also entered into the Deposit Services Agreement with CEC Finance, pursuant to which Sang Fei will utilise the deposit services offered by CEC Finance. Apart from the transactions contemplated under the Hua Da Tenancy Agreement, the Group has also been leasing and licensing certain properties from members of the CEC Group through the Sang Da Tenancy Agreement, the Great Wall Tenancy Agreement and other rental arrangements.

Under the Listing Rules, the transactions under the Hua Da Business Services Agreement and the Business Services Agreement, the transactions under the Hua Da Deposit Services Agreement and the Deposit Services Agreement, the transactions under the Hua Da Tenancy Agreement, the Sang Da Tenancy Agreement, the Great Wall Tenancy Agreement and other rental arrangements, will in each case be aggregated and treated as if they were one transaction.

Since the applicable percentage ratios set out in Rule 14.07 of the Listing Rules in respect of the transactions under the Hua Da Business Services Agreement and the Business Services Agreement, as aggregated, are more than 2.5%, the Hua Da Business Services Agreement is, pursuant to Rule 14A.35 of the Listing Rules, subject to the reporting, announcement and independent shareholders' approval requirements.

Since the applicable percentage ratios set out in Rule 14.07 of the Listing Rules in respect of the transactions under the Hua Da Deposit Services Agreement and the Deposit Services Agreement, as aggregated, are less than 2.5%, the Hua Da Deposit Services Agreement is, pursuant to Rule 14A.34 of the Listing Rules, only subject to the reporting and announcement requirements and is exempt from the independent shareholders' approval requirements.

Since the applicable percentage ratios set out in Rule 14.07 of the Listing Rules in respect of the transactions under the Hua Da Tenancy Agreement, the Sang Da Tenancy Agreement, the Great Wall Tenancy Agreement and other rental arrangements, as aggregated, are less than 2.5%, the Hua Da Tenancy Agreement is, pursuant to Rule 14A.34 of the Listing Rules, only subject to the reporting and announcement requirements and is exempt from the independent shareholders' approval requirements.

An Independent Board Committee has been established to advise the Independent Shareholders in respect of the terms of the Acquisition and the terms of the Non-exempt Continuing Connected Transactions. In this respect, Altus has been retained as the independent financial adviser to the Independent Board Committee and the Independent Shareholders.

The purpose of this circular is to provide you with further information relating to the Acquisition and the Continuing Connected Transactions and to seek your approval of the ordinary resolutions set out in the notice of the SGM at the end of this circular. The recommendation from the Independent Board Committee to the Independent Shareholders is set out on pages 34 to 35 of this circular and the letter from Altus is set out on pages 36 to 53 of this circular.

THE ACQUISITION

(1) China Hua Da Agreement

Date	:	20 June 2008
Vendor	:	China Hua Da
Purchaser	:	the Company
Subject assets	:	64.75% of the equity interest of Hua Da Electronics
Consideration	:	The consideration for the sale and purchase of 64.75% of the equity interest of Hua Da Electronics owned by China Hua Da shall be HK\$984.20 million, which shall be satisfied by the Company allotting and issuing 393,680,000 Consideration Shares to China Hua Da, credited as fully paid, at an issue price of HK\$2.50 per Consideration Share.

China Hua Da is a state-owned enterprise established under the laws of the PRC. The equity interest of China Hua Da is contributed as to 50% by CEC and as to 50% by SDIC High-Tech Investment Co., Ltd.. China Hua Da is principally engaged in the design and manufacturing of integrated circuits chips as well as research and development of integrated circuits designing tools and integrated circuits application systems.

CEC, a state-owned enterprise established under the laws of the PRC, is the ultimate controlling shareholder of the Company holding approximately 74.98% of the issued Shares as at the Latest Practicable Date. Established in 1989 with the approval of the State Council of the PRC, CEC is a nationwide electronics and information technology conglomerate directly administered by the PRC government. CEC actively focuses on communications, consumer electronics, semi-conductor and software sectors in the PRC. As China Hua Da is owned as to 50% by CEC, China Hua Da is therefore a connected person of the Company.

SDIC High-Tech Investment Co., Ltd. is a wholly-owned subsidiary of The State Development and Investment Corporation, which is a state-owned investment holding company established under the laws of the PRC. SDIC High-Tech Investment Co., Ltd. engages in investments in high technology projects. SDIC High-Tech Investment Co., Ltd. and The State Development and Investment Corporation are third parties independent of the Company and connected persons of the Company.

As at the Latest Practicable Date, China Hua Da did not own any Shares. China Hua Da will cease to hold any equity interest in Hua Da Electronics after completion of the China Hua Da Acquisition.

LETTER FROM THE BOARD

(2) Beijing Shoufa Xinan Agreement

Date	:	20 June 2008
Vendor	:	Beijing Shoufa Xinan
Purchaser	:	the Company
Subject assets	:	7.50% of the equity interest of Hua Da Electronics
Consideration	:	The consideration for the sale and purchase of 7.50% of the equity interest of Hua Da Electronics owned by Beijing Shoufa Xinan shall be HK\$114 million, which shall be satisfied by the Company allotting and issuing 45,600,000 Consideration Shares to Beijing Shoufa Xinan, credited as fully paid, at an issue price of HK\$2.50 per Consideration Share.

Beijing Shoufa Xinan is a company established under the laws of the PRC. It is principally engaged in the research and development, manufacturing and sales of information security products and the provision of safety solution services for information system. Beijing Shoufa Xinan and its ultimate beneficial shareholders are third parties independent of the Company and connected persons of the Company.

As at the Latest Practicable Date, Beijing Shoufa Xinan did not own any Shares. Beijing Shoufa Xinan will cease to hold any equity interest in Hua Da Electronics after completion of the Beijing Shoufa Xinan Acquisition.

(3) The Other Vendors Agreement

Date	:	20 June 2008
Vendors	:	(1) WANG Qinsheng, who has agreed to sell 9.1668% of the equity interests of Hua Da Electronics for a consideration of HK\$139,334,600 (2) LIU Weiping, who has agreed to sell 5.4251% of the equity interests of Hua Da Electronics for a consideration of HK\$82,461,900 (3) DONG Haoran, who has agreed to sell 5.2078% of the equity interests of Hua Da Electronics for a consideration of HK\$79,157,800

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- (4) HUANG Guoyong, who has agreed to sell 2.1506% of the equity interests of Hua Da Electronics for a consideration of HK\$32,689,500
- (5) SUN Xiaonian, who has agreed to sell 1.2395% of the equity interests of Hua Da Electronics for a consideration of HK\$18,840,400
- (6) CHENG Jinge, who has agreed to sell 1.2811% of the equity interests of Hua Da Electronics for a consideration of HK\$19,473,100
- (7) XIAO Gang, who has agreed to sell 1.8454% of the equity interests of Hua Da Electronics for a consideration of HK\$28,049,700
- (8) JIANG Shiping, who has agreed to sell 1.4337% of the equity interests of Hua Da Electronics for a consideration of HK\$21,793,000

Purchaser : the Company

Subject assets : an aggregate of 27.75% of the equity interest of Hua Da Electronics

Consideration : The aggregate consideration for the sale and purchase of the aggregate of 27.75% of the equity interest of Hua Da Electronics under the Other Vendors Agreement shall be HK\$421.80 million, which shall be satisfied by the Company allotting and issuing an aggregate of 168,720,000 Consideration Shares to the Other Vendors, credited as fully paid, at an issue price of HK\$2.50 per Consideration Share, of which:

- (i) 55,733,840 Consideration Shares will be allotted and issued to Ms. Wang Qinsheng;
- (ii) 32,984,760 Consideration Shares will be allotted and issued to Mr. Liu Weiping;
- (iii) 31,663,120 Consideration Shares will be allotted and issued to Mr. Dong Haoran;
- (iv) 13,075,800 Consideration Shares will be allotted and issued to Mr. Huang Guoyong;

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- (v) 7,536,160 Consideration Shares will be allotted and issued to Mr. Sun Xiaonian;
- (vi) 7,789,240 Consideration Shares will be allotted and issued to Mr. Cheng Jinge;
- (vii) 11,219,880 Consideration Shares will be allotted and issued to Mr. Xiao Gang; and
- (viii) 8,717,200 Consideration Shares will be allotted and issued to Mr. Jiang Shiping;

Ms. Wang Qinsheng and Mr. Sun Xiaonian currently are directors of Hua Da Electronics and Mr. Liu Weiping is a director and president of Hua Da Electronics. Mr. Dong Haoran and Mr. Jiang Shiping are employees of Hua Da Electronics. The remaining Other Vendors, being Mr. Huang Guoyong, Mr. Cheng Jinge and Mr. Xiao Gang are third parties independent of the Company and connected persons of the Company.

As at the Latest Practicable Date, none of the Other Vendors owned any Shares. The Other Vendors will cease to hold any equity interest in Hua Da Electronics after completion of the Other Vendors Acquisition.

Consideration Shares to be issued pursuant to the Acquisition

The aggregate consideration payable by the Company under the China Hua Da Agreement, the Beijing Shoufa Xinan Agreement and the Other Vendors Agreement is HK\$1,520 million, which shall be satisfied by the Company allotting and issuing an aggregate of 608,000,000 Consideration Shares to China Hua Da, Beijing Shoufa Xinan and the Other Vendors, credited as fully paid, at an issue price of HK\$2.50 per Consideration Share. The Consideration Shares will be allotted and issued on the completion date of the China Hua Da Agreement, the Beijing Shoufa Xinan Agreement and the Other Vendors Agreement.

The Consideration Shares to be issued under the China Hua Da Agreement, the Beijing Shoufa Xinan Agreement and the Other Vendors Agreement shall rank *pari passu* in all respects with the Shares in issue on the date of allotment and issue of such Consideration Shares. The Consideration Shares are not subject to any lock-up restrictions.

As at the Latest Practicable Date, the Company had 1,083,560,000 Shares in issue. The 393,680,000 Consideration Shares to be issued as consideration under the China Hua Da Agreement, the 45,600,000 Consideration Shares to be issued as consideration under the Beijing Shoufa Xinan Agreement and the 168,720,000 Consideration Shares to be issued as consideration under the Other Vendors Agreement represent:

- (i) approximately 36.33%, 4.21% and 15.57% of the existing issued share capital of the Company, respectively; and

LETTER FROM THE BOARD

- (ii) approximately 23.27%, 2.70% and 9.97% of the issued share capital of the Company as enlarged by the allotment and issue of the Consideration Shares, respectively.

The Consideration Shares will be allotted and issued pursuant to a specific mandate to be sought at the SGM and will be allotted and issued to China Hua Da, Beijing Shoufa Xinan and the Other Vendors upon Completion. An application has been made by the Company to the Listing Committee for the listing of, and permission to deal in, the Consideration Shares.

The Issue Price of HK\$2.50 per Consideration Share represents:

- (a) a premium of approximately 28.87% over the closing price of HK\$1.94 per Share as quoted on the Stock Exchange on the Last Trading Day;
- (b) a premium of approximately 25.38% over the average closing price of approximately HK\$1.994 per Share as quoted on the Stock Exchange for the last five consecutive trading days up to and including the Last Trading Day;
- (c) a premium of approximately 25.06% over the average closing price of approximately HK\$1.999 per Share as quoted on the Stock Exchange for the last ten consecutive trading days up to and including the Last Trading Day;
- (d) a premium of approximately 20.19% over the closing price of HK\$2.08 per Share as quoted on the Stock Exchange on the Latest Practicable Date; and
- (e) a premium of approximately 5.74 times over the underlying net asset value per Share attributable to equity holders of the Company of approximately HK\$0.435 per Share as at 31 December 2007 (based on the audited consolidated balance sheet of the Group as at 31 December 2007).

Based on the closing price of HK\$1.94 per Share as quoted on the Stock Exchange on the Last Trading Day, the Consideration Shares were valued at HK\$1,179.52 million. The consideration for the Acquisition represents a price to earnings ratio of Hua Da Electronics of approximately 12 times. The consideration was determined and agreed between the parties after arm's length negotiations and was based on the said price to earnings ratio of Hua Da Electronics and other various factors, including the quality of the assets being acquired, their historical performance, the competitive advantages in their respective markets, as well as by reference to other financial and operational indicators and the industrial prospects of the integrated circuits industry in the PRC. The Issue price was determined and agreed between the parties after arm's length negotiations with reference to the market prices of the Shares. After taken into account the factors set out above and the reasons and benefits set out in the paragraph headed "Reasons for and benefits of the Acquisition" below, the Directors consider that the consideration and the Issue Price are fair and reasonable when the interests of the Shareholders taken a whole are considered.

Conditions precedent

Completions of the China Hua Da Acquisition, the Beijing Shoufa Xinan Acquisition and the Other Vendors Acquisition are conditional upon the fulfilment (or waiver, in certain cases as stated below) of the following conditions on or before 30 June 2009:

- (a) the Company having completed and satisfied with the results of the legal, financial and business due diligence exercise to be carried out by it on Hua Da Electronics;
- (b) Hua Da Electronics having notified and obtained consent from other signing parties to certain agreements (to which Hua Da Electronics is a party) as required by such agreements in the event of a change in the shareholders or shareholding structure of Hua Da Electronics;
- (c) in respect of the China Hua Da Acquisition:
 - (i) the passing of an ordinary resolution by the Independent Shareholders at the SGM approving the China Hua Da Agreement and the transactions contemplated thereunder;
 - (ii) all necessary approvals from government and relevant regulatory authorities in respect of the China Hua Da Agreement and the China Hua Da Acquisition having been obtained and such approvals not having in any way altered the rights and obligations of any party to the China Hua Da Agreement and the China Hua Da Acquisition;
 - (iii) the Listing Committee granting the listing of, and permission to deal in, the Consideration Shares to be issued under the China Hua Da Agreement;
 - (iv) the completion of the disposal by Hua Da Electronics of the Excluded Assets (other than CIDC);
 - (v) all representations and warranties being true and accurate in all respects and not misleading in any respect as of Completion; and
 - (vi) no notice having been received from the Stock Exchange and the Securities and Futures Commission to the effect that the listing of the Shares on the Stock Exchange will or is likely to be cancelled or suspended or that new onerous conditions will or are likely to be attached to such listing as a result of the China Hua Da Acquisition;

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- (d) in respect of the Beijing Shoufa Xinan Acquisition:
- (i) the passing of an ordinary resolution by the Independent Shareholders at the SGM approving the Beijing Shoufa Xinan Agreement and the transactions contemplated thereunder;
 - (ii) all necessary approvals from government and relevant regulatory authorities in respect of the Beijing Shoufa Xinan Agreement and the Beijing Shoufa Xinan Acquisition having been obtained and such approvals not having in any way altered the rights and obligations of any party to the Beijing Shoufa Xinan Agreement and the Beijing Shoufa Xinan Acquisition;
 - (iii) the Listing Committee granting the listing of, and permission to deal in, the Consideration Shares to be issued under the Beijing Shoufa Xinan Agreement;
 - (iv) the completion of the disposal by Hua Da Electronics of the Excluded Assets (other than CIDC);
 - (v) all representations and warranties being true and accurate in all respects and not misleading in any respect as of Completion; and
 - (vi) no notice having been received from the Stock Exchange and the Securities and Futures Commission to the effect that the listing of the Shares on the Stock Exchange will or is likely to be cancelled or suspended or that new onerous conditions will or are likely to be attached to such listing as a result of the Beijing Shoufa Xinan Acquisition; and
- (e) in respect of the Other Vendors Acquisition:
- (i) the passing of an ordinary resolution by the Independent Shareholders at the SGM approving the Other Vendors Agreement and the transactions contemplated thereunder;
 - (ii) all necessary approvals from government and relevant regulatory authorities in respect of the Other Vendors Agreement and the Other Vendors Acquisition having been obtained and such approvals not having in any way altered the rights and obligations of any party to the Other Vendors Agreement and the Other Vendors Acquisition;
 - (iii) the Listing Committee granting the listing of, and permission to deal in, the Consideration Shares to be issued under the Other Vendors Agreement;
 - (iv) the completion of the disposal by Hua Da Electronics of the Excluded Assets (other than CIDC);

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- (v) all representations and warranties being true and accurate in all respects and not misleading in any respect as of Completion; and
- (vi) no notice having been received from the Stock Exchange and the Securities and Futures Commission to the effect that the listing of the Shares on the Stock Exchange will or is likely to be cancelled or suspended or that new onerous conditions will or are likely to be attached to such listing as a result of the Other Vendors Acquisition;

Except for conditions (a), (b), (c)(v), (d)(v) and (e)(v) which may be waived by the Company at its sole discretion, none of the above conditions can be waived by any party to the agreements. As at the Latest Practicable Date, none of the above conditions have been fulfilled. The Company currently does not intend to waive any of such conditions. Completions of each of the China Hua Da Acquisition, the Beijing Shoufa Xinan Acquisition and the Other Vendors Acquisition are not conditional upon each other.

If any of the above conditions have not been fulfilled or (in the case of conditions (a), (b), (c)(v), (d)(v) and (e)(v)) waived by the Company on or before 30 June 2009, the China Hua Da Agreement, the Beijing Shoufa Xinan Agreement or the Other Vendors Agreement (as the case may be) will lapse.

Completion of the China Hua Da Acquisition, the Beijing Shoufa Xinan Acquisition and the Other Vendors Acquisition shall take place on the tenth Business Day after all of the above conditions have been fulfilled or (in the case of conditions (a), (b), (c)(v), (d)(v) and (e)(v)) waived by the Company, or on such other date as agreed between the parties to the China Hua Da Agreement, the Beijing Shoufa Xinan Acquisition or the Other Vendors Agreement (as the case may be). On the date of Completion, an aggregate of 608,000,000 Consideration Shares will be allotted and issued to China Hua Da, Beijing Shoufa Xinan and the Other Vendors, credited as fully paid, by the Company to satisfy the consideration payable under the China Hua Da Agreement, the Beijing Shoufa Xinan Agreement and the Other Vendors Agreement.

After Completion, Hua Da Electronics will become a wholly-owned subsidiary of the Company and the financial statements of Hua Da Electronics will be consolidated into those of the Group. Hua Da Electronics will also be converted into a wholly foreign-owned enterprise upon completion of the Acquisition.

Information on Hua Da Electronics

Hua Da Electronics is a leading company in the design of integrated circuits established under the laws of the PRC. It is principally engaged in the design and sale of integrated circuits and the research and development of electronic design automation tools. The technologies and products of Hua Da Electronics have been widely applied in the areas of telecommunications, social security, electronic payments and consumer electronics.

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The registered capital of Hua Da Electronics is RMB34,594,600 which is contributed as to 64.75% by China Hua Da, as to 7.50% by Beijing Shoufa Xinan and as to 27.75% by the Other Vendors (9.1668% by Ms. Wang Qinsheng, 5.4251% by Mr. Liu Weiping, 5.2078% by Mr. Dong Haoran, 2.1506% by Mr. Huang Guoyong, 1.2395% by Mr. Sun Xiaonian, 1.2811% by Mr. Cheng Jinge, 1.8454% by Mr. Xiao Gang and 1.4337% by Mr. Jiang Shiping).

As at the Latest Practicable Date, each of China Hua Da, Beijing Shoufa Xinan and the Other Vendors has fully contributed towards the registered capital of Hua Da Electronics in accordance with their respective capital contribution ratios. Save for the above capital contribution, none of China Hua Da, Beijing Shoufa Xinan nor the Other Vendors has advanced any shareholder's loans to Hua Da Electronics.

The consolidated profit before income tax and profit for the year of Hua Da Electronics, as extracted from the audited financial statements of Hua Da Group prepared in accordance with the Hong Kong Financial Reporting Standards issued by the Hong Kong Institute of Certified Public Accountants (the "HKICPA") as set out in Appendix I to this circular, were as follows:

	Year ended 31 December	Year ended 31 December
	2006	2007
	<i>(HK\$'000)</i>	<i>(HK\$'000)</i>
Profit before income tax	128,716	132,063
Profit for the year	120,026	127,307

The consolidated net asset value of Hua Da Electronics as at 31 December 2007 based on the audited financial statements was approximately HK\$302,636,000.

The shareholders of Hua Da Electronics had approved the payment of final dividends for the year ended 31 December 2007 in an aggregate amount of RMB138,378,400, to the existing shareholders of Hua Da Electronics. Other than the said profit appropriations, there were not, and will not be, any other distributions before completion of the Acquisition. The remaining retained earnings will remain with Hua Da Electronics upon completion of the Acquisition. The Directors consider that the payment of final dividends by Hua Da Electronics will not have any material adverse effect on the working capital position of Hua Da Electronics. Further details of the said profit appropriations are set out in Note 24 to the Accountant's Report of Target Group as set out in Appendix I to this circular.

Excluded assets

Hua Da Electronics has carried out a restructuring to carve out the Excluded Assets after the year ended 31 December 2007. Such Excluded Assets include a 71.26% equity interest in Beijing Hua Da Xinan, a 80% equity interest in Guangdong Hua Da and Hua Da Electronics' entire shareholding in CIDC. The purpose of the restructuring is to facilitate the future development of Hua Da Electronics' core businesses.

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The Excluded Assets have an unaudited net asset value of an aggregate amount of HK\$3,003,922 as at 31 December 2007 and have incurred a net loss of an aggregate amount of HK\$1,746,010 for the year ended 31 December 2007, based on their respective unaudited management accounts.

Further details about the disposal of the Excluded Assets are set out in Note 29 to the Accountant's Report of Target Group as set out in Appendix I to this circular.

Reasons for and benefits of the Acquisition

The Company is an investment holding company. Currently, Sang Fei is the principal operating subsidiary of the Company and is primarily engaged in the manufacturing and sales of mobile handsets and other portable electronic products.

The acquisition of Hua Da Electronics provides the Group with a valuable opportunity to enter into the integrated circuits chips design market, which is a high-tech area with better profit margin, and enables the Group to offer products for a wider range of applications such as telecommunications, home network, consumer electronics in the future. Hua Da Electronics has a strong presence in the integrated circuits industry. Integrated circuits have been widely applied in a wide range of areas including communications, home and personal entertainment, social and public business. The Group intends to leverage off Hua Da Electronics' expertise in the integrated circuits industry to enhance its capability in the consumer electronics and communications products sector. Through the acquisition of Hua Da Electronics, the Group intends to transform itself from a manufacturer of mobile handsets and other portable electronic products to an active player in the industry possessing comprehensive capability in the upstream of the industry value chain.

The global information technology industry tends to focus on the advancement and development of their core technologies and businesses. The Group will seize this opportunity to continue the business development in its existing mobile handset operations and at the same time to explore new businesses at the upstream of the industry value chain. The Group's ultimate objective is to advance its core technology from low end to mid-to-high end stream and to promote its core business to the upstream of the industry value chain.

The Directors consider that the Acquisition offers the Group a valuable opportunity to expand its business into the integrated circuits sector and the upstream of the industry value chain. Based on the aforesaid, the Directors consider that the terms of the China Hua Da Agreement, the Beijing Shoufa Xinan Agreement and the Other Vendors Agreement are fair and reasonable and on normal commercial terms and that the entering into of the China Hua Da Agreement, the Beijing Shoufa Xinan Agreement and the Other Vendors Agreement is in the interest of the Company and the Shareholders as a whole.

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Shareholding structure of the Company

To the best knowledge of the Directors, having made all reasonable enquiries, (i) the existing shareholding structure of the Company; (ii) the shareholding structure of the Company upon the allotment and issue of the Consideration Shares and (iii) the shareholding structure of the Company upon the allotment and issue of the Consideration Shares and the exercise of the outstanding Options in full, are as follows:

Shareholders	As at the Latest Practicable Date (Note 1)		Immediately after completion of the Acquisition (Note 1)		Immediately after completion of the Acquisition and exercise of the outstanding Options in full (Note 2)	
	No. of Shares	%	No. of Shares	%	No. of Shares	%
CEC	812,500,000	74.98	812,500,000	48.03	812,500,000	47.44
China Hua Da	—	—	393,680,000	23.27	393,680,000	22.99
Beijing Shoufa Xinan*	—	—	45,600,000	2.70	45,600,000	2.66
Other Vendors						
Ms. Wang Qinsheng* (Note 3)	—	—	55,733,840	3.30	55,733,840	3.25
Mr. Liu Weiping (Note 4)	—	—	32,984,760	1.95	32,984,760	1.93
Mr. Dong Haoran*	—	—	31,663,120	1.87	31,663,120	1.85
Mr. Huang Guoyong*	—	—	13,075,800	0.77	13,075,800	0.76
Mr. Sun Xiaonian* (Note 3)	—	—	7,536,160	0.45	7,536,160	0.44
Mr. Cheng Jing*	—	—	7,789,240	0.46	7,789,240	0.46
Mr. Xiao Gang*	—	—	11,219,880	0.66	11,219,880	0.66
Mr. Jiang Shiping*	—	—	8,717,200	0.51	8,717,200	0.51
Holders of Options						
Mr. Tong Baoan	—	—	—	—	3,800,000	0.22
Mr. Fan Qingwu	—	—	—	—	3,600,000	0.21
Mr. Hua Longxing	—	—	—	—	3,600,000	0.21
Directors and chief executive of Sang Fei	—	—	—	—	1,600,000	0.09
Aggregate of employees and other participants*	—	—	—	—	8,350,000	0.49
Other Public Shareholders*	271,060,000	25.02	271,060,000	16.03	271,060,000	15.83
Total	1,083,560,000	100.00	1,691,560,000	100.00	1,712,510,000	100.00
Percentage of Public Float		25.02		26.75		26.91

Notes:

- The percentages stated above assume that the outstanding Options as at the Latest Practicable Date will not be exercised and that there will not be any changes to the total issued share capital of the Company as at the Latest Practicable Date prior to the completion of the Acquisition.

* Public shareholders of the Company

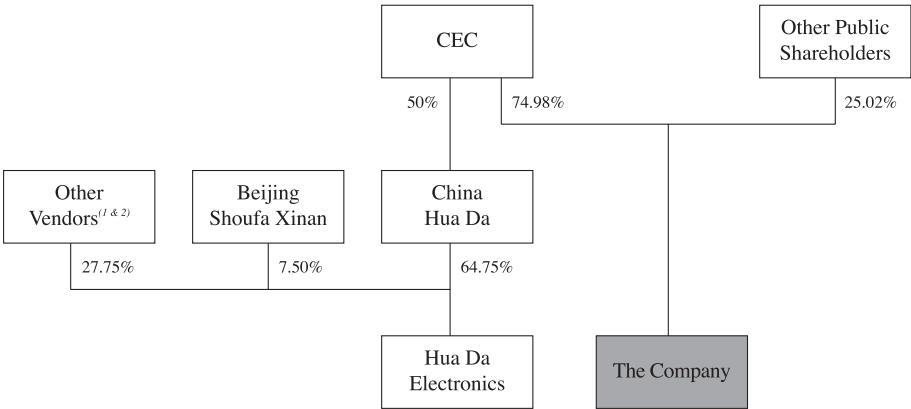
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- 2. The percentages stated above assume that other than the allotment and issue of Shares as a result of the exercise of the Options, there will not be any changes to the total issued share capital of the Company as at the Latest Practicable Date prior to the completion of the Acquisition.
- 3. Ms. Wang Qinsheng and Mr. Sun Xiaonian currently are directors of Hua Da Electronics. In view of the Acquisition, Hua Da Electronics will dissolve its board of directors and Ms. Wang Qinsheng and Mr. Sun Xiaonian will resign from directorships of Hua Da Electronics before completion of the Acquisition. Accordingly, Ms. Wang Qinsheng and Mr. Sun Xiaonian will be regarded as public shareholders of the Company upon completion of the Acquisition.
- 4. Mr. Liu Weiping currently is a director and president of Hua Da Electronics. In view of the Acquisition, Hua Da Electronics will dissolve its board of directors and Mr. Liu Weiping will resign as director of Hua Da Electronics. Since Mr. Liu Weiping will continue to hold the position of president of Hua Da Electronics, he, being the chief executive of Hua Da Electronics, will be regarded as connected person of the Company and his shareholding in the Company will not be counted towards the public float of the Company.

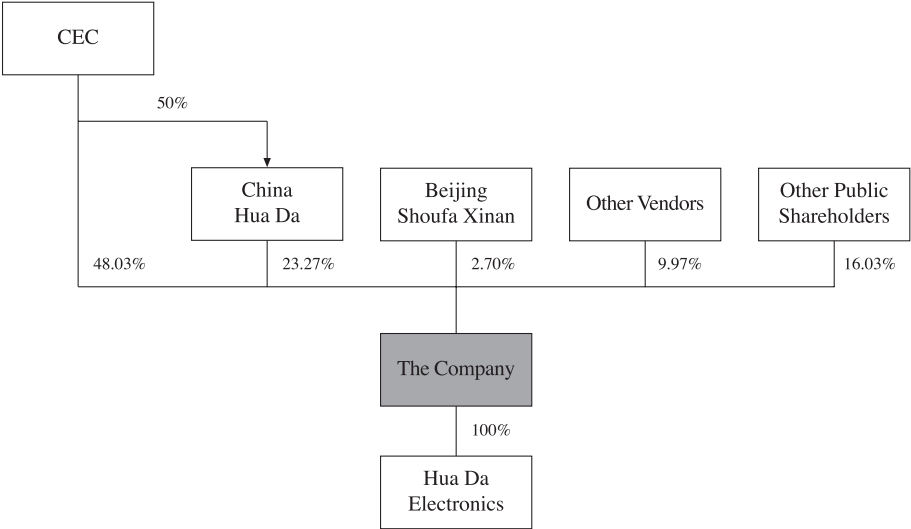
The Acquisition which involves the issue of Consideration Shares will not result in change of control (as defined in the Code of Takeovers and Mergers) of the Company.

Set out below are the shareholding structures of the Company immediately prior and following completion of the Acquisition:

Corporate structure immediately prior to completion of the Acquisition



Corporate structure immediately following completion of the Acquisition



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Notes:

1. The Other Vendors represent the vendors under the Other Vendors Agreement.
2. As at the Latest Practicable Date, the 27.75% equity interest of Hua Da Electronics was owned as to 9.1668% by Ms. Wang Qinsheng, as to 5.4251% by Mr. Liu Weiping, as to 5.2078% by Mr. Dong Haoran, as to 2.1506% by Mr. Huang Guoyong, as to 1.2395% by Mr. Sun Xiaonian, as to 1.2811% by Mr. Cheng Jinge, as to 1.8454% by Mr. Xiao Gang and as to 1.4337% by Mr. Jiang Shiping.
3. Immediately following completion of the Acquisition, Ms. Wang Qinsheng, Mr. Liu Weiping, Mr. Dong Haoran, Mr. Huang Guoyong, Mr. Sun Xiaonian, Mr. Cheng Jinge, Mr. Xiao Gang and Mr. Jiang Shiping will be interested in approximately 3.30%, 1.95%, 1.87%, 0.77%, 0.45%, 0.46%, 0.66% and 0.51% of the issued share capital of the Company as enlarged by the allotment and issue of the Consideration Shares.

Financial effects of the Acquisition on the Group

The aggregate consideration for the Acquisition, being HK\$1,520 million, will be satisfied by the Company allotting and issuing a total of 608,000,000 Consideration Shares. Accordingly, the cash and bank balances of the Group, as well as the amount of short-term borrowings of the Group, will not be affected by the Acquisition. Since the Group has applied principles of merger accounting as prescribed in Hong Kong Accounting Guideline 5 “Merger Accounting for Common Control Combinations” issued by the HKICPA for the Acquisition, the total equity of the Company would increase by HK\$296,653,000, representing the amount of increase in net asset value of Hua Da Electronics less an estimated transaction costs of approximately HK\$5,983,000 as if the Acquisition was completed on 31 December 2007.

Upon completion of the Acquisition, Hua Da Electronics will become a wholly-owned subsidiary of the Company and the financial statements of Hua Da Electronics will be consolidated with those of the Group.

Earnings

For the year ended 31 December 2007, the Group recorded an audited consolidated loss before income tax of HK\$19,117,000 and the net profit for the year attributable to the equity holders of the Company was HK\$8,074,000.

Given the track record of Hua Da Electronics and the industrial prospects of the integrated circuits industry in the PRC, the Directors consider the Acquisition could benefit the results of the Enlarged Group in the future.

Net asset value

As at 31 December 2007, the audited consolidated net asset value of the Group amounted to approximately HK\$600,836,000. Based on the unaudited pro forma consolidated statement of assets and liabilities of the Enlarged Group as set out in Appendix IV to this circular, the unaudited pro forma consolidated net asset value of the Enlarged Group immediately after completion of the Acquisition would be approximately HK\$897,489,000.

Financial and trading prospects of the Group

In the future, the Group will, on the one hand, continue the business development in its existing mobile handset operations and at the same time, explore new businesses at the upstream of the industry value chain. The ultimate objective is to advance its core technology from low end to mid-to-high end stream and to promote its core business to the upstream of the industry value chain and to bring the best return to its shareholders.

The Directors consider that the Acquisition provides the Group with valuable opportunity to enter into the integrated circuits chips design market, and enables the Group to offer products for a wider range of applications' such as telecommunications, home network, consumer electronic appliances in the future. Integrated circuits industry has been one of the major development focuses in the PRC and will continue to be a development focus under the Eleventh Five-Year Plan. In the recent years, integrated circuits cards and smart cards have been increasingly used in the PRC in areas such as resident identity cards, social security cards and petrol cards. In the "Specific Project Regarding Integrated Circuits Industry in the Eleventh Five-Year" announced by the former Ministry of Information Industry, it is expected that the production volume of the integrated circuits industry in the PRC will have an annual growth rate of 30%. The government of the PRC pays high regards to the development of the integrated circuits industry. Integrated circuits enterprises are benefited from different preferential government policies including but not limited to preferential taxation policy. Although the prospects of the integrated circuits industry will attract new competitors and will therefore increase competition, the Directors believe that Hua Da Electronics, with its leading position in the industry, will continue to enjoy competitive advantages in the industry.

As the global consumer communications products markets is expected to maintain its growth momentum in the coming years and given the rising demand of technologically advanced products in the PRC, the Board is optimistic about the business of the Enlarged Group.

After completion of the Acquisition, the financial results of Hua Da Electronics will be consolidated into the Group's results. The Directors believe that such consolidation will have positive impact on the Group's operational and financial prospects.

Listing Rules implications

China Hua Da is owned as to 50% by CEC, the ultimate controlling shareholder of the Company holding approximately 74.98% of the issued Shares as at the Latest Practicable Date. Accordingly, China Hua Da is a connected person of the Company and the China Hua Da Acquisition constitutes a connected transaction of the Company.

The China Hua Da Acquisition, the Beijing Shoufa Xinan Acquisition and the Other Vendors Acquisition, when aggregated, constitute a major transaction of the Company and are subject to the shareholders' approval requirements under the Listing Rules. There are no other prior transactions between the Company and the counterparties of the Acquisition which would require aggregation under the Listing Rules.

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Since the China Hua Da Acquisition also constitutes a connected transaction of the Company and that CEC is considered to have a material interest in the Beijing Shoufa Xinan Acquisition and the Other Vendors Acquisition, CEC and its associates are required to abstain from voting on the ordinary resolutions approving the China Hua Da Acquisition, the Beijing Shoufa Xinan Acquisition and the Other Vendors Acquisition. Each of the China Hua Da Acquisition, the Beijing Shoufa Xinan Acquisition and the Other Vendors Acquisition is conditional upon, among other things, the approval by the Independent Shareholders at the SGM.

CONTINUING CONNECTED TRANSACTIONS

Hua Da Electronics has on-going transactions with members of the CEC Group in its ordinary and usual course of business. These transactions will, after completion of the China Hua Da Acquisition, become continuing connected transactions of the Company. Hua Da Electronics and CEC have entered into certain continuing connected transactions agreements to regulate the continuing connected transactions between Hua Da Electronics and the CEC Group.

(1) Hua Da Business Services Agreement

On 20 June 2008 after trading hours, Hua Da Electronics entered into the Hua Da Business Services Agreement with CEC to set out the framework for the on-going business relationship between Hua Da Electronics and members of the CEC Group.

The Hua Da Business Services Agreement covers (i) the provision of products processing, testing and assembling services by the CEC Group and the purchase of raw materials and modules from the CEC Group; (ii) the sales of integrated circuit cards and smart cards modules, chips and electronic design automation (EDA) tools to the CEC Group; and (iii) the provision of canteen services by the CEC Group to Hua Da Electronics. The Hua Da Business Services Agreement takes effect from the date of completion of the China Hua Da Acquisition and will be valid until 31 December 2010.

Hua Da Electronics has been focusing on the design of integrated circuits and the development of new technology and has been subcontracting the processing, testing and assembling procedures to members of the CEC Group. The CEC Group also supplies raw materials and modules to Hua Da Electronics for its research and development uses. Members of the CEC Group are also customers of the products of Hua Da Electronics. The transactions contemplated under the Hua Da Business Services Agreement are, therefore, vital and integral to the business operations of Hua Da Electronics.

Details of the continuing connected transactions contemplated under the Hua Da Business Services Agreement are as follows:

- (i) *Provision of processing, testing and assembling services by the CEC Group and purchase of raw materials and modules from the CEC Group*

Pursuant to the Hua Da Business Services Agreement, members of the CEC Group will provide processing, testing and assembling services to Hua Da Electronics for products including integrated circuit cards, smart cards and chips.

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The service fees chargeable by members of the CEC Group for the processing, testing and assembling services are determined after arm's length negotiations between the parties with reference to market rates. The prices offered to Hua Da Electronics will be no less favourable than the prices of similar services offered by other third party service providers to Hua Da Electronics.

Hua Da Electronics will also, pursuant to the Hua Da Business Services Agreement, purchase from members of the CEC Group raw materials and modules for the research and development of integrated circuit cards, smart cards and chips, on a non-committed basis. Such raw materials and modules will include but not limited to wafer, integrated circuit modules, integrated circuit cards, integrated circuits and printed circuit boards. The Hua Da Business Services Agreement does not impose any obligation on the part of Hua Da Electronics to purchase raw materials and modules exclusively from the CEC Group. Hua Da Electronics may source raw materials and modules from any other parties.

The price of raw materials and modules to be supplied by the CEC Group to Hua Da Electronics is determined after arm's length negotiations between the parties with reference to market rates. The prices offered to Hua Da Electronics are no less favourable than the prices of similar products offered by other third party suppliers to Hua Da Electronics.

(ii) Sales of products to the CEC Group

Pursuant to the Hua Da Business Services Agreement, Hua Da Electronics will sell products including integrated circuit cards and smart cards modules, chips and electronic design automation tools to members of the CEC Group.

The products supplied to members of the CEC Group are priced in accordance with their models and specifications. The prices are determined after arm's length negotiations between the parties with reference to market rates. The prices offered to members of the CEC Group are no less favourable than the prices of similar products offered to other third party customers of Hua Da Electronics.

(iii) Provision of canteen services by CEC Group

Pursuant to the Hua Da Business Services Agreement, Hua Da Electronics retains members of the CEC Group to provide canteen facilities and meals to Hua Da Electronics' staff. In return, Hua Da Electronics will pay members of the CEC Group an agreed service fee, which is determined by reference to the actual consumption and an agreed fixed service fees for such services. The service fees chargeable by members of the CEC Group for the canteen services are determined after arm's length negotiations between the parties with reference to market rates. The prices offered to Hua Da Electronics will be no less favourable than those offered by other third party service providers to Hua Da Electronics.

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Historical figures of continuing connected transactions

In respect of the each category of continuing connected transactions contemplated under the Hua Da Business Services Agreement, the historical figures for each of the three financial years ended 31 December 2005, 2006 and 2007 are set out below:

Type of transaction	Historical figures for		
	2005 <i>(approximately RMB'000)</i>	2006 <i>(approximately RMB'000)</i>	2007 <i>(approximately RMB'000)</i>
Processing, testing and assembling services and purchase of raw materials and modules			
– Annual service charges paid by Hua Da			
Electronics	223,464	515,850	375,198
Sales of products			
– Annual charges received by Hua Da			
Electronics	34,336	42,991	46,886
Canteen services			
– Annual service charges paid by Hua Da			
Electronics	494	459	599

Proposed annual caps

It is expected that for the period commencing from the completion of the China Hua Da Acquisition until 31 December 2008 and the two financial years ending 31 December 2009 and 2010, the amount of consideration payable by Hua Da Electronics to the CEC Group for the provision of processing, testing and assembling services by the CEC Group and the purchase of raw materials and modules from the CEC Group, the amount of consideration receivable by Hua Da Electronics from the CEC Group for the sales of products and the amount of consideration payable by Hua Da Electronics to the CEC Group for the provision of canteen services will not exceed the amounts set out in the following table. Accordingly, these amounts have been set as the proposed annual caps for the relevant continuing connected transactions.

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Type of transaction	For the period commencing from the completion of the China Hua Da Acquisition until 31 December	For the year ending 31 December	For the year ending 31 December
	2008 (RMB'000)	2009 (RMB'000)	2010 (RMB'000)
Processing, testing and assembling services and purchase of raw materials and modules			
– Annual service charges payable by Hua Da Electronics	284,640	293,310	421,140
Canteen services			
– Annual service charges payable by Hua Da Electronics	550	1,120	1,160
<i>Total annual service charges payable by Hua Da Electronics</i>	<u>285,190</u>	<u>294,430</u>	<u>422,300</u>
Sales of products			
– Annual charges receivable by Hua Da Electronics	19,620	36,000	43,200

In arriving at the above annual caps for the provision of processing, testing and assembling services by the CEC Group and the purchase of raw materials and modules from the CEC Group, the Company has made reference to the historical service fees paid by Hua Da Electronics and the historical purchase volume of raw materials and modules from the CEC Group and has taken into account the expected demand of the products of Hua Da Electronics, the production plan of Hua Da Electronics and the costs of providing such services, raw materials and modules.

In arriving at the above annual caps for the sales of products to the CEC Group, the Company has made reference to the historical sales volume, the expected demand of Hua Da Electronics' products by the CEC Group and the order status of the products.

In arriving at the above annual caps for the provision of canteen services by the CEC Group to Hua Da Electronics, the Company has taken into account the historical consumption volume by Hua Da Electronics, the anticipated increase in headcount of Hua Da Electronics and the anticipated inflation rate over the period.

(2) Hua Da Deposit Services Agreement

Hua Da Electronics and CEC Finance entered into the Hua Da Deposit Services Agreement on 20 June 2008 after trading hours. CEC Finance is a subsidiary of CEC and therefore an connected person of the Company. CEC Finance is a non-bank financial institution approved and regulated by the People's Bank of China and China Banking Regulatory Commission. CEC Finance was established for the purpose of enhancing the centralised management of funds among members of the CEC Group and for improving the fund utilisation efficiency of the CEC Group as a whole. As an intra-group service provider, CEC Finance generally has a better and more efficient communication with Hua Da Electronics which will allow expedient and efficient service provision by CEC Finance.

The Hua Da Deposit Services Agreement does not create any obligation on the part of Hua Da Electronics to utilise any particular services of CEC Finance. Other than the fixed deposits which have specified deposit terms, Hua Da Electronics may at any time withdraw the funds deposited with CEC Finance without incurring any penalty. CEC Finance is one of the financial institutions which provide deposit services to Hua Da Electronics. Hua Da Electronics may obtain deposit services available from any other financial institutions in addition to or instead of CEC Finance, as it sees fit.

The interest rates for deposit shall be the standard rates promulgated by the People's Bank of China for the same type of deposits. Such interest rates will not be less than the rates offered to Hua Da Electronics by normal commercial banks in the PRC for comparable deposits.

The Hua Da Deposit Services Agreement takes effect from the date of completion of the China Hua Da Acquisition and will be valid until 31 December 2010. Upon expiry of the initial term of the Hua Da Deposit Services Agreement, the agreement may be renewed for further terms of three years automatically unless either party objects by giving a written notice at least one month prior to the expiry of the Hua Da Deposit Services Agreement.

The Company proposed that for the period commencing from the completion of the China Hua Da Acquisition until 31 December 2010, the maximum balance of deposits (including the interests accrued thereon) maintained by Hua Da Electronics with CEC Finance shall not exceed RMB10 million on any given day. In determining the above proposed cap, the Company has taken into account the cashflow position of Hua Da Electronics and the treasury policy of the Group.

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(3) Hua Da Tenancy Agreement

On 20 June 2008 after trading hours, Hua Da Electronics and Beijing Huada Zhibao entered into the Hua Da Tenancy Agreement pursuant to which Beijing Huada Zhibao agreed to lease to Hua Da Electronics the premises which is situated in Gaojiayuan, Beijing, PRC.

Details of the Hua Da Tenancy Agreement is set out below:

Date:	20 June 2008
Landlord:	Beijing Huada Zhibao
Tenant:	Hua Da Electronics
Premises:	Levels 1 to 3 and Level 5 of the building located at No. 1 Gaojiayuan, Chaoyang District, Beijing, PRC.
Term:	One (1) year commencing from 1 July 2008 and expiring on 30 June 2009 (both days inclusive).

Hua Da Electronics has the right to request for the renewal of the Hua Da Tenancy Agreement by giving a written notice to Beijing Huada Zhibao three months prior to the expiry of the Hua Da Tenancy Agreement. Hua Da Electronics shall have priority over the others to lease the premises.

Gross floor area	approximately 3,960 square metres
Rental:	RMB2,082,544 per annum (which is exclusive of utilities charges which shall be borne by Hua Da Electronics).
Usage	Research and development and offices purposes

The aggregate rentals payable by Hua Da Electronics to Beijing Huada Zhibao under the Hua Da Tenancy Agreement for the period commencing from the completion of the China Hua Da Acquisition until 31 December 2008 and for the six months ending 30 June 2009 will not exceed RMB960,000 and RMB1,041,272, respectively. The annual caps for the transactions contemplated under the Hua Da Tenancy Agreement for the period commencing from the completion of the China Hua Da Acquisition until 31 December 2008 and for the six months ending 30 June 2009 are therefore set at such amounts accordingly.

LETTER FROM THE BOARD

Hua Da Electronics is currently occupying the premises as its research and development centre and offices. Since the old tenancy agreement in respect of the premises will expire in June 2008, Hua Da Electronics and Beijing Huada Zhibao entered into the Hua Da Tenancy Agreement to renew the tenancy. The terms of the Hua Da Tenancy Agreement have been arrived at after arm's length negotiations between the parties and with reference to open market rent of properties of comparable size, use and location which is publicly available in the market.

Beijing Huadao Zhibao is a subsidiary of CEC and therefore a connected person of the Company. Beijing Huada Zhibao is principally engaged in the design, research and development, manufacture and sale of integrated circuits and electronics system software and the provision of system integration services.

Listing Rules implications

Apart from the Hua Da Business Services Agreement, Sang Fei, the principal operating subsidiary of the Company, has also entered into the Business Services Agreement with CEC to set out the framework for the ongoing business relationship between the CEC Group and Sang Fei. Details of the Business Services Agreement between Sang Fei and CEC are set out in the announcements of the Company dated 18 June 2004, 21 December 2006 and 8 August 2007.

Apart from the Hua Da Deposit Services Agreement, Sang Fei has also entered into the Deposit Services Agreement with CEC Finance, pursuant to which Sang Fei will utilise the deposit services offered by CEC Finance. Details of the Deposit Services Agreement between Sang Fei and CEC are set out in the announcement of the Company dated 20 September 2007.

Apart from the transactions contemplated under the Hua Da Tenancy Agreement, the Group has also been leasing and licensing certain properties from members of the CEC Group through the Sang Da Tenancy Agreement, the Great Wall Tenancy Agreement and other rental arrangements. Details of the Sang Da Tenancy Agreement, the Great Wall Tenancy Agreement and the other rental arrangements are set out in the announcements of the Company dated 9 April 2008, 15 September 2006 and 18 June 2004, respectively.

Under the Listing Rules, the transactions under the Hua Da Business Services Agreement and the Business Services Agreement, the transactions under the Hua Da Deposit Services Agreement and the Deposit Services Agreement, the transactions under the Hua Da Tenancy Agreement, the Sang Da Tenancy Agreement, the Great Wall Tenancy Agreement and other rental arrangements, will in each case be aggregated and treated as if they were one transaction. Other than the above, there are no other prior continuing connected transactions between the Group and the counterparties of the continuing connected transactions which would require aggregation under the Listing Rules.

LETTER FROM THE BOARD

Since the applicable percentage ratios set out in Rule 14.07 of the Listing Rules in respect of the transactions under the Hua Da Business Services Agreement and the Business Services Agreement, as aggregated, are more than 2.5%, the Hua Da Business Services Agreement is, pursuant to Rule 14A.35 of the Listing Rules, subject to the reporting, announcement and independent shareholders' approval requirements.

Since the applicable percentage ratios set out in Rule 14.07 of the Listing Rules in respect of the transactions under the Hua Da Deposit Services Agreement and the Deposit Services Agreement, as aggregated, are less than 2.5%, the Hua Da Deposit Services Agreement is, pursuant to Rule 14A.34 of the Listing Rules, only subject to the reporting and announcement requirements and is exempt from the independent shareholders' approval requirements.

Since the applicable percentage ratios set out in Rule 14.07 of the Listing Rules in respect of the transactions under the Hua Da Tenancy Agreement, the Sang Da Tenancy Agreement, the Great Wall Tenancy Agreement and other rental arrangements, as aggregated, are less than 2.5%, the Hua Da Tenancy Agreement is, pursuant to Rule 14A.34 of the Listing Rules, only subject to the reporting and announcement requirements and is exempt from the independent shareholders' approval requirements.

The Directors are of the view that the continuing connected transactions described above will be carried out in the ordinary and usual course of business of Hua Da Electronics and on normal commercial terms and that these continuing connected transactions and the proposed caps are fair and reasonable and in the interests of the Company and its shareholders as a whole.

SGM

A notice convening the SGM to be held at Plaza I-III, Lower Lobby, Novotel Century Hong Kong, 238 Jaffe Road, Wanchai, Hong Kong on Monday, 21 July 2008 at 3:00 p.m. is set out on pages 158 to 160 of this circular. At the SGM, ordinary resolutions will be proposed to approve the China Hua Da Acquisition, the Beijing Shoufa Xinan Acquisition and the Other Vendors Acquisition and the Non-exempt Continuing Connected Transactions. The vote of the Independent Shareholders at the SGM shall be taken by poll.

In accordance with the Listing Rules, CEC, the Company's ultimate controlling Shareholder holding 74.98% interest in the Company as at the Latest Practicable Date, and its associates, will abstain from voting on the ordinary resolutions approving the China Hua Da Acquisition, the Beijing Shoufa Xinan Acquisition and the Other Vendors Acquisition and the Non-exempt Continuing Connected Transactions at the SGM.

LETTER FROM THE BOARD

A form of proxy for use at the SGM is enclosed with this circular. Whether or not you are able to attend the SGM, you are requested to complete the accompanying form of proxy in accordance with the instructions printed thereon and return the same to the Company's branch share registrar in Hong Kong, Tricor Abacus Limited at 26th Floor, Tesbury Centre, 28 Queen's Road East, Wanchai, Hong Kong, as soon as possible and in any event not less than 48 hours before the time appointed for holding the SGM or any adjournment thereof. Completion and return of the form of proxy will not preclude you from attending and voting in person at the SGM or any adjournment thereof should you so wish.

RECOMMENDATION

Altus has been retained as the independent financial adviser to advise the Independent Board Committee and the Independent Shareholders in respect of the terms of the Acquisition and the terms of the Non-exempt Continuing Connected Transactions. Altus considers that the terms of the Acquisition are on normal commercial terms, and that the terms of the Non-exempt Continuing Connected Transactions are on normal commercial terms and are conducted in the ordinary and usual course of business of the Group. Furthermore, Altus considers that the terms of the Acquisition and the terms of the Non-exempt Continuing Connected Transactions to be fair and reasonable and are in the interests of the Company and the Shareholders as a whole. Accordingly, Altus advises the Independent Shareholders, as well as the Independent Board Committee to recommend the Independent Shareholders, to vote in favour of the ordinary resolutions to be proposed at the SGM to approve the Acquisition and the Non-exempt Continuing Connected Transactions. The text of the letter from Altus containing its advice and the principal factors and reasons it has taken into consideration in arriving at its advice is set out on pages 36 to 53 of this circular.

The Independent Board Committee, after considering the advice from Altus, concurs with the views of Altus and considers that the terms of the Acquisition and the terms of the Non-exempt Continuing Connected Transactions are fair and reasonable and in the interests of the Company and the Shareholders as a whole. Accordingly, the Independent Board Committee recommends the Independent Shareholders to vote in favour of the ordinary resolutions to be proposed at the SGM to approve the Acquisition and the Non-exempt Continuing Connected Transactions. The text of the letter from the Independent Board Committee is set out on pages 34 to 35 of this circular.

LETTER FROM THE BOARD

FURTHER INFORMATION

Your attention is also drawn to the letter from the Independent Board Committee which sets out its recommendation to the Independent Shareholders, the letter from Altus which contains its advice to the Independent Board Committee and the Independent Shareholders, and the additional information set out in the appendices to this circular.

Yours faithfully

For and on behalf of the Board

China Electronics Corporation Holdings Company Limited

Xiong Qunli

Chairman



CHINA ELECTRONICS CORPORATION HOLDINGS COMPANY LIMITED

中國電子集團控股有限公司*

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

(Stock Code: 00085)

30 June 2008

To the Independent Shareholders

Dear Sir or Madam,

**MAJOR TRANSACTION,
CONNECTED TRANSACTION
AND
CONTINUING CONNECTED TRANSACTIONS**

We refer to the circular (the “**Circular**”) dated 30 June 2008 issued by the Company to its Shareholders of which this letter forms part. The terms defined in the Circular shall have the same meanings when used in this letter, unless the context otherwise requires.

On 20 June 2008, the Board announced that the Company has, on the same date, entered into the China Hua Da Agreement, the Beijing Shoufa Xinan Agreement and the Other Vendors Agreement in respect of the China Hua Da Acquisition, the Beijing Shoufa Xinan Acquisition and the Other Vendors Acquisition, respectively.

We have been appointed by the Board to advise you as to whether the terms of the Acquisition and the terms of the Non-exempt Continuing Connected Transactions are fair and reasonable and in the interests of the Company and the Shareholders as a whole. Details of the Acquisition and the Non-exempt Continuing Connected Transactions are set out in the section headed “Letter from the Board” of the Circular.

Altus has been retained as independent financial adviser to advise the Independent Board Committee and the Independent Shareholders in respect of the terms of the Acquisition and the terms of the Non-exempt Continuing Connected Transactions. The text of the letter of advice from Altus containing its advice and the principal factors and reasons it has taken into consideration in arriving at its advice is set out on pages 36 to 53 of the Circular.

* For identification purpose only

LETTER FROM THE INDEPENDENT BOARD COMMITTEE

We, after considering the advice from Altus, concur with the views of Altus and consider that the terms of the Acquisition and the terms of the Non-exempt Continuing Connected Transactions are fair and reasonable and in the interests of the Company and the Shareholders as a whole. Accordingly, we recommend the Independent Shareholders to vote in favour of the ordinary resolutions to be proposed at the SGM to approve the Acquisition and the Non-exempt Continuing Connected Transactions, as detailed in the notice of the SGM set out at the end of the Circular.

Yours faithfully

Independent Board Committee

Chan Kay Cheung

Wong Po Yan

Yin Yongli

LETTER FROM ALTUS

The following is the text of a letter of advice from Altus to the Independent Board Committee and the Independent Shareholders in respect of the Acquisition and the Non-exempt Continuing Connected Transactions which have been prepared for the purpose of inclusion in this circular.

ALTUS CAPITAL LIMITED

8th Floor, Hong Kong Diamond Exchange Building
8 Duddell Street, Central
Hong Kong

30 June 2008

The Independent Board Committee and the Independent Shareholders

China Electronics Corporation Holdings Company Limited

Room 3503, 35th Floor
China Resources Building
26 Harbour Road
Wanchai, Hong Kong

Dear Sirs,

**MAJOR AND CONNECTED TRANSACTION
ACQUISITION OF 100% EQUITY INTERESTS**

**IN HUA DA ELECTRONICS
NON-EXEMPT CONTINUING CONNECTED TRANSACTIONS**

INTRODUCTION

We refer to our appointment as independent financial adviser to advise the Independent Board Committee and Independent Shareholders in respect of the Acquisition and the Non-exempt Continuing Connected Transactions. Their details are set out in the letter from the Board contained in the circular of the Company dated 30 June 2008 (“**Circular**”) to the Shareholders, of which this letter forms part. Terms used in this letter shall have the same meanings as those defined in the Circular unless the context requires otherwise.

The Acquisition constitutes a major transaction of the Company under the Listing Rules as the applicable percentage ratios calculated per Rule 14.07 of the Listing Rules exceed 25% but are less than 100%. As at the Latest Practicable Date, CEC was the ultimate controlling shareholder of the Company with shareholding of approximately 74.98%. One of the vendors of the Acquisition, China Hua Da is owned as to 50% by CEC and is therefore a connected person of the Company. On this basis, the China Hua Da Acquisition constitutes a connected transaction of the Company.

CEC, which is interested in the China Hua Da Acquisition, is also considered to have a material interest in the Beijing Shoufa Xinan Acquisition and the Other Vendors Acquisition. Consequently, CEC and its associates are required to abstain from voting on the proposed resolutions approving the Acquisition.

Upon completion of the Acquisition, the transactions contemplated under the Hua Da Business Services Agreement, when aggregated with the Business Service Agreement, will constitute non-exempt continuing connected transactions which require reporting, announcement and independent shareholders' approval requirements under the Listing Rules. CEC and its associates are accordingly required to abstain from voting on the relevant resolution approving the Non-exempt Continuing Connected Transactions.

The Independent Board Committee has been established to advise whether the Acquisition and the Non-exempt Continuing Connected Transactions are fair and reasonable and in the interests of the Company and the Shareholders as a whole, and to advise the Independent Shareholders on how to voting. The Independent Board Committee comprises Messrs. Chan Kay Cheung, Wong Po Yan and Yin Yongli, all being independent non-executive Directors.

BASIS OF OUR ADVICE

In formulating our opinion, we have relied on the information, facts and representations contained or referred to in the Circular and the information, facts and representations provided by, and the opinions expressed by the Directors, the Company and its management. We have assumed that all statements, information, facts, opinions and representations made or referred to in the Circular were true, accurate and complete at the time they were made and continued to be true, accurate and complete as at the date of the Circular. We have no reason to doubt the truth, accuracy and completeness of the statements, information, facts, opinions and representations provided to us by the Directors, the Company and its management. The Directors have confirmed to us that no material facts have been omitted from the information supplied and opinions expressed; thus we have no reason to doubt that any relevant material facts have been withheld or omitted from the information provided and referred to in the Circular, or the reasonableness of the opinions and representations provided to us by them.

All the Directors jointly and severally accept full responsibility for the accuracy of the information contained in the Circular and confirm, having made all reasonable enquiries, that, to the best of their knowledge, opinions expressed in the Circular have been arrived at after due and careful consideration and that there are no other facts not contained in the Circular the omission of which would make any statement in the Circular misleading. We have relied on such information and opinions and have not however, conducted any independent investigation into the business, financial conditions and affairs or the future prospects of the Group and Hua Da Electronics.

PRINCIPAL FACTORS TAKEN INTO CONSIDERATION

I. THE ACQUISITION

In formulating our opinion on the Acquisition, we have taken into consideration the following principal factors and reasons:

1. Background of the transaction

As at the Latest Practicable Date, Hua Da Electronics was owned as to 64.75%, 7.50% and 27.75% by China Hua Da, Beijing Shoufa Xinan and the Other Vendors respectively.

The Company has on 20 June 2008 entered into the China Hua Da Agreement, the Beijing Shoufa Xinan Agreement and the Other Vendors Agreement in respect of the Acquisition. Under the Acquisition, the Company will acquire the entire equity interests of Hua Da Electronics for a total consideration of HK\$1,520 million, which is payable to China Hua Da, Beijing Shoufa Xinan and the Other Vendors in the proportion of their stakes in Hua Da Electronics. The consideration is to be satisfied by the allotment and issuance of an aggregate of 608,000,000 Consideration Shares at the Issue Price of HK\$2.50 to China Hua Da, Beijing Shoufa Xinan and the Other Vendors respectively.

It is noted that the completions of each of the China Hua Da Agreement, the Beijing Shoufa Xinan Agreement and the Other Vendors Agreement are not conditional upon each other. Hence, while the Company's intention is to acquire the entire interests of Hua Da Electronics, its eventual shareholding is dependent on the outcome of each of the China Hua Da Agreement, the Beijing Shoufa Xinan Agreement and the Other Vendors Agreement.

2. Hua Da Electronics

The business

Hua Da Electronics, a company established under the laws of the PRC, is principally engaged in the design and sale of integrated circuits ("IC"), and the research and development of electronic design automation tools. According to the Directors, China Hua Da group of companies is one of the first IC design companies established in the PRC. It is also one of the first authorised suppliers to be recognised by several PRC government departments for supply of ICs for various applications.

The ICs designed by Hua Da Electronics are used in a wide range of products including Smart chips for personal identity cards and petrol cards and Subscriber Identity Module (SIM) cards. Its major customers include government agencies responsible for identity card issuance, petrol companies and petrol station operators.

Compared with the Group's existing business of manufacturing and sales of mobile handsets and other portable electronic products, the businesses of Hua Da Electronics represent a high-technology area which offers higher profit margins. The Acquisition enables the Group to acquire a leading company in the PRC market and allows the Group to expand its business scope and diversify its sources of revenue as the wide ranging IC applications enable the Group to expand its range of products.

Industry background and prospects

Since its initial development in the middle of 20th century, ICs have become the basis for information delivery, management and storage; and is an integral part for the areas of consumer electronics, internet and telecommunications, computing and home network, transportation and manufacturing activities.

According to CCID Consulting¹, the IC market in the PRC has grown from RMB380 billion in 2005 to about RMB560 billion in 2007. It expects the IC market to continue to grow in the next few years, reaching approximately RMB1.1 trillion in 2011. The demand is expected to be spurred by the advent of new areas of applications of ICs. Meanwhile, for the specific area of IC design, CCID Consulting¹ expects annual growth of more than 20% in the next few years.

Note 1: CCID Consulting is a market research consulting company established under the supervision of the China Center of Information Industry Development of the Ministry of Information Industry.

Based on the information above, Hua Da Electronics operates in a high growth albeit highly competitive market. Having considered Hua Da Electronics' leading position in the PRC market, we are of the view that the Acquisition allows the Group an opportunity to participate in this high growth area of business.

LETTER FROM ALTUS

Financial performance

The financial performance of Hua Da Group (including the Excluded Assets) in the past three years are summarised below:

	Year ended 31 December (“FY”)		
	2005 (HK\$'000)	2006 (HK\$'000)	2007 (HK\$'000)
Income statements			
Revenue	295,524	508,717	652,767
Cost of sales	(215,823)	(327,554)	(399,877)
Gross profit	79,701	181,163	252,890
Operating and financing expenses	(60,699)	(73,339)	(130,428)
Other income and gains	22,814	20,892	9,601
Profit before income tax	41,816	128,716	132,063
Income tax	(2,383)	(8,690)	(4,756)
Profit after income tax	39,433	120,026	127,307
Minority interests	919	176	136
Profit attributable to shareholders	40,352	120,202	127,443

The revenue of Hua Da Group has increased by more than 120% between FY2005 and FY2007. Over the same period, gross profit increased by a higher rate about 217% with the improvement of gross margins due to higher efficiency achieved in product design as well as economies of scale achieved in outsourcing. Between FY2005 and FY2007, operating and financing expenses rose by approximately 115%, in line with the increase in revenue. Other income and gains consist of mainly grants from government which amounted to HK\$22.5 million, HK\$19.0 million and HK\$7.5 million respectively. The government grants are subject to the qualification of each of the project undertaken by Hua Da Group. Hence, the amount of grants receivable in the future will depend on the nature of each projects.

In line with the substantial increase in gross profit, profit after income tax rose by more than 220% between FY2005 and FY2007, notwithstanding the decrease in government grant over the same period.

LETTER FROM ALTUS

In summary, Hua Da Group has experienced substantial revenue growth and improved profitability in the past few years. The Acquisition will therefore enhance the profitability of the Group if such trend continues, in line with the positive outlook of the IC industry and markets.

Financial position

The financial position of Hua Da Group (including the Excluded Assets) as at 31 December 2007 is summarised below:

	As at 31 December 2007 (HK\$'000)
Balance sheet	
Non-current assets	40,794
Current assets	<u>574,528</u>
Total assets	615,322
Total liabilities	<u>(312,686)</u>
Net assets	<u><u>302,636</u></u>

Consistent with the nature of its business of design, research and development, Hua Da Group maintained relatively small investments in plants and equipment and hence has relatively small non-current assets. Of the current assets, it maintained cash and cash equivalent of about HK\$188.9 million as at 31 December 2007. The liabilities of Hua Da Group comprised mainly trade and other payables. It has short-term bank borrowing of HK\$64.5 million as at 31 December 2007 and has no long-term borrowings. The net assets of Hua Da Group amounted to approximately HK\$302.6 million as at 31 December 2007.

The shareholders of Hua Da Electronics had approved the payment of the final dividend for the year ended 31 December 2007 in an aggregate amount of approximately HK\$148.8 million and it will not have any other distributions before the completion of the Acquisition. The payment of this final dividend will reduce the net asset value of Hua Da Group. The effects of this final dividend on the net asset value based on the unaudited pro forma consolidated statement of assets and liabilities of the Enlarged Group as if the Acquisition has been taken place on 31 December 2007 will be further discussed in Section 7 below. Hua Da Group has net current assets of approximately HK\$261.8 million and cash balance of approximately HK\$188.9 million as at 31 December 2007. Based on the above, we believe Hua Da Electronics has the ability to make the aforesaid dividend payment without having material adverse effect on its working capital position.

Based on the balance sheet above, we are of the view that Hua Da Group has a healthy financial position.

Having considered Hua Da Group's principal businesses and prospects, its past financial performance and financial position as discussed above, we are of the view that the Acquisition is in the interests of the Company and the Shareholders from the business development point of view.

3. The Group's business and development strategy

The Company is an investment holding company. Sang Fei, its principal operating subsidiary, is primarily engaged in the manufacturing and sales of mobile handsets and other portable electronic products.

It is the management's strategy to progressively transform the Group's businesses from the lower-end OEM manufacturing, to the mid-and-high end value chain, thereby becoming a comprehensive business solution provider in the long run. To this end, the Group has been exploring merger and acquisition opportunities of new businesses at the upstream of the information technology ("IT") industry value chain. Recognising that CEC is one of the leading enterprises in the IT industry in the PRC, it has been the intention of the management to leverage on the Company's relationship with CEC for this development. The Acquisition is therefore consistent with business development strategy of the Company.

4. Valuation of the Acquisition

We have attempted to identify companies which are engaged in similar business with Hua Da Electronics. As far as we are aware, we have identified Shanghai Fudan Microelectronics Company Limited ("Shanghai Fudan") which is listed on the Stock Exchange and several companies listed on the New York Stock Exchange/Nasdaq, being Atmel Corporation ("Atmel"), Infineon Technologies AG ("Infineon") and Atheros Communications Inc. ("Atheros"). When analysing the reasonableness of the valuation of the Acquisition, we have made comparisons with the aforesaid companies (the "Comparables"). We wish to highlight that these Comparables may differ from Hua Da Electronics in terms of size, and their scope of business activities may not be identical to that of Hua Da Electronics.

LETTER FROM ALTUS

(a) Price-to-earnings ratio

The total consideration for the Acquisition of HK\$1,520 million was arrived at after arm’s length negotiations among the relevant parties with reference to, inter alia, the historical earnings of Hua Da Electronics. Price-to-earnings ratio (“PER”) is a commonly used reference for valuing an entity and we believe it is an acceptable method to value Hua Da Electronics in this case as it has a profitable track record and is not an asset-based company. In this regard, we have compared it with the PERs of the Comparables, based on their share prices as at the Latest Practicable Date as follows:

Company	Principal activities	Principal stock exchange	Forecast PER (times)	Historical PER (times)	Revenue (HK\$ billion)	Gross Profit (HK\$ billion)	Market capitalisation (HK\$ billion)
Shanghai Fudan	Designs, develops & sells IC products & provision of testing services for IC products	Stock Exchange	n/a	10.6	0.3	0.1	0.2
Atmel	Designs, develops, manufactures, & markets semiconductors	Nasdaq	16.9 ¹	76.7	12.9	4.5	12.5
Infineon	Designs, develops, manufactures, & markets semiconductors & system solutions used in various microelectronics applications	New York	48.6 ²	n/a	96.3	17.7	52.6
Atheros	Develops integrated semiconductor system solutions for communication IC products	Nasdaq	21.1 ³	55.0	3.4	1.6	13.4
Hua Da Electronics	Designs & sells IC & research & develops electronic design automation tools	Unlisted	n/a	11.9	0.7	0.3	1.5

Source: Yahoo Finance website

Notes:

1. For the financial year ending 31 December 2009, by Thomson Group, a financial information company
2. For the financial year ending 30 September 2009, by Thomson Group, a financial information company
3. For the financial year ending 31 December 2009, by Thomson Group, a financial information company

Compared with Hua Da Electronics, it is noted that the market capitalisation and revenue of Infineon, Atmel and Atheros are substantially larger, while Shanghai Fudan is smaller. For the larger Comparables, it is noted that Infineon has incurred losses in the past financial year and as a result, historical PER is not applicable. The historical PERs of Atmel and Atheros are 76.7 times and 55.0 times respectively. For the smaller Comparable, the historical PER of Shanghai Fudan is 10.6 times. Hua Da Electronics has been profitable in the past year and the historical PER based on its valuation under the Acquisition is 11.9 times. Profit projections of Hua Da Electronics and Shanghai Fudan are not available while the forecast PERs of the larger Comparables range from 16.9 times to 48.6 times. It is noted that the forecast PERs relate to financial years ending in 2009 and 2010.

Given their larger scale of operations, the market may accord the larger Comparables with higher PERs. Notwithstanding, in this case, the PERs of the larger Comparables are substantially higher. Meanwhile, the historical PER based on the valuation under the Acquisition is comparable to the current PER of the smaller Comparable. Having considered the above, we are of the view that the valuation of Hua Da Electronics is fair and reasonable when compared with the Comparables.

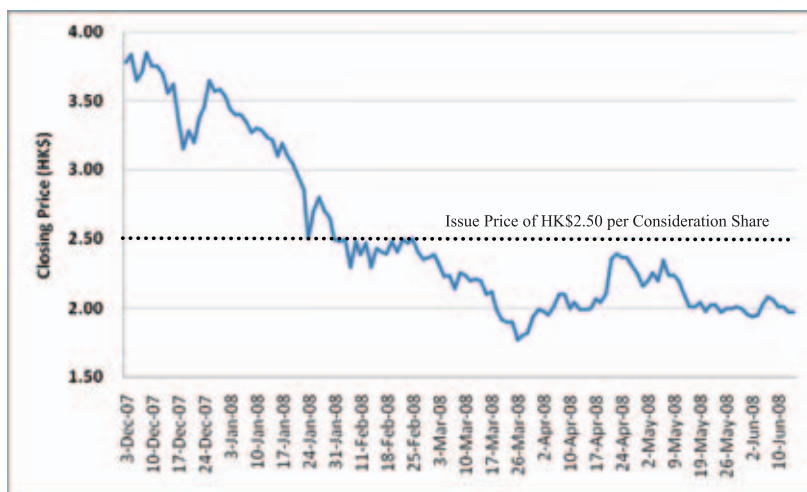
5. Issue price of the Consideration Shares

To satisfy the consideration of HK\$1,520 million for the Acquisition, 608,000,000 Consideration Shares will be issued at an issue price of HK\$2.50 per Consideration Share. This issue price represents:

- (a) a premium of approximately 28.87% over the closing price of HK\$1.94 per Share as quoted on the Stock Exchange on the Last Trading Day;
- (b) a premium of approximately 25.38% over the average closing price of approximately HK\$1.994 per Share as quoted on the Stock Exchange for the last five consecutive trading days up to and including the Last Trading Day;
- (c) a premium of approximately 25.06% over the average closing price of approximately HK\$1.999 per Share as quoted on the Stock Exchange for the last 10 consecutive trading days up to and including the Last Trading Day; and
- (d) a premium of approximately 20.19% over the closing price of approximately HK\$2.08 per Share as quoted on the Stock Exchange on the Latest Practicable Date.

LETTER FROM ALTUS

In the past three months, the Shares have been trading at below the issue price of the Consideration Shares, at within the range of HK\$1.94 and HK\$2.39 per Share as shown below.



The issue price of the Consideration Shares represents a premium of approximately 5.74 times over the underlying net asset value per Share attributable to equity holders of the Company of approximately HK\$0.435 per Share as at 31 December 2007. Based on the Company's earnings per Share of HK\$0.0075 for the financial year ended 31 December 2007, the issue price represents a price-to-earnings ratio of more than 300 times. This compares favourably with the valuation of the Acquisition as discussed in the preceding paragraph and on this basis, we are of the view that the issue price of the Consideration Shares are fair and reasonable.

6. Effects on shareholding of existing Shareholders

As consideration for the Acquisition, 608,000,000 Consideration Shares will be issued. The Consideration Shares represent approximately 56.1% of the existing issued share capital and approximately 35.9% of the enlarged share capital of the Company. The table below sets out the shareholding structure of the Company as at the Latest Practicable Date and immediately after issuance of the Consideration Shares for the Acquisition.

Shareholder	As at the Latest Practicable Date		Immediately after issuance of the Consideration Shares for the Acquisition	
CEC Group	812,500,000	74.98%	1,206,180,000	71.30%
– CEC	812,500,000	74.98%	812,500,000	48.03%
– China Hua Da			393,680,000	23.27%
Beijing Shoufa Xinan	–	–	45,600,000	2.70%
Other Vendors	–	–	168,720,000	9.97%
Existing public Shareholders	271,060,000	25.02%	271,060,000	16.03%
	<u>1,083,560,000</u>	<u>100.00%</u>	<u>1,691,560,000</u>	<u>100.00%</u>

As shown above, the percentage shareholding interests of the existing public Shareholders in the Company will be diluted from about 25.02% as at the Latest Practicable Date to approximately 16.03% upon issuance of the Consideration Shares. Notwithstanding the dilution, it is noted that (i) the economic benefits accruing to Shareholders in terms of earnings per Share will improve after the Acquisition as further discussed in “Financial effects of the Acquisition” below; and (ii) the Issue Price represents a premium to the historical trading prices of the Shares in the past three months. We are therefore of the view that the dilution effects of the Acquisition on the shareholding of existing Shareholders while in itself is not favourable, is acceptable.

It is also noted that upon completion of the Acquisition, CEC together with China Hua Da, will have shareholding of about 71.3% in the Company. Consequently, there will be no change in the ultimate controlling shareholder of the Company after the Acquisition.

7. Financial effects of the Acquisition

Profit and loss accounts and earnings per Share

The Group recorded net profit attributable to Shareholders of HK\$8.07 million for the financial year ended 31 December 2007. Based on 1,083,560,000 Shares in issue as at the Latest Practicable Date, this translates into earnings per Share of HK\$0.0075.

Upon the Completion, Hua Da Electronics will become a wholly-owned subsidiary of the Company and its financial results will be consolidated into the Group. Hua Da Group has recorded a profit attributable to the equity holders for the year ended 31 December 2007 of HK\$127.4 million, as set out in Appendix I to this Circular. Without taking into account the nominal impact of the Excluded Assets¹, the Group’s total profit attributable to Shareholders for the financial year ended 31 December 2007 (assuming the Acquisition has taken place on 1 January 2007 and the profit contribution of Hua Da Group is added to the Group’s profit) will therefore be HK\$135.5 million. Based on the enlarged issued share capital of 1,691,560,000 Shares after the Completion, this result in earnings per Share of HK\$0.08. The Acquisition will therefore enhance the earnings per Share of the Company and is favourable to the Shareholders.

Note 1: Based on their respective unaudited management accounts, the Excluded Assets have an unaudited net asset value of an aggregate amount of approximately HK\$3.0 million as at 31 December 2007 and have incurred a net loss of an aggregate amount of HK\$1.75 million for the year ended 31 December 2007.

LETTER FROM ALTUS

The following table sets forth:

- (i) the net asset value and net assets value per share of the Group; and
- (ii) the net asset value and net assets value per share of the Enlarged Group as further adjusted to give effect to the dividend declared and paid by Hua Da Electronics after 31 December 2007.

The net assets before dividend payment of the Enlarged Group as shown in the following table is determined using the information contained in the unaudited pro forma consolidated statement of assets and liabilities of the Enlarged Group as set out in Appendix IV to this Circular.

	The Group (HK\$'000)	The Enlarged Group (HK\$'000)
Non-current assets	103,882	144,676
Current assets	1,713,080	2,281,625
Total assets	1,816,962	2,426,301
Current liabilities	(1,216,126)	(1,528,812)
Net assets before dividend payment	600,836	897,489
Dividend	—	(148,794)
Net assets after dividend payment	<u>600,836</u>	<u>748,695</u>
Number of Shares outstanding	1,083,560,000	1,691,560,000
Net asset value per Share	HK\$0.55	HK\$0.44

After the Acquisition, the net asset value of the Group will increase from HK\$600.8 million as at 31 December 2007 to approximately HK\$897.5 million of the Enlarged Group. However, after taking into account the total amount of dividend declared for the year ended 31 December 2007 of approximately HK\$148.8 million, net asset value of the Enlarged Group will be approximately HK\$748.7 million. Net asset value per Share will decline to HK\$0.44 compared with HK\$0.55 prior to the Acquisition.

The Acquisition will therefore enlarge the financial position of the Group, but will result in dilution of net asset value per Share. Notwithstanding the dilution to the net asset value per Share, the dividend payment will not have material adverse effect on the operation and the working capital position of Hua Da Electronics having taking into consideration its financial position as at 31 December 2007.

Working capital position

The consideration for the Acquisition will be fully satisfied by the allotment and issuance of the Consideration Shares. Consequently, the liquidity and working capital position of the Group will not be affected by the Acquisition.

II. THE NON-EXEMPT CONTINUING CONNECTED TRANSACTIONS

In formulating our opinion on the Non-exempt Continuing Connected Transactions, we have taken into consideration the following principal factors and reasons:

1. Background

Hua Da Electronics has had close relationship with the CEC Group where it has on-going business transactions with members of the CEC Group in its ordinary and usual course of business. These transactions can be categorised as follows:

- (i) provision of processing, testing and assembling services by CEC Group and purchase of raw materials and modules from CEC Group (“Outsourcing and Purchase Transactions”);
- (ii) sales of IC cards and smart card modules, chips and EDA tools to CEC Group (“Sale Transactions”); and
- (iii) provision of canteen services by CEC Group to Hua Da Electronics (“Canteen Transactions”).

To regulate such continuing relationship between Hua Da Electronics and members of the CEC Group and to set out the framework for future transactions, the Hua Da Business Services Agreement has been entered into on 20 June 2008. This agreement will take effect from the date of completion of the China Hua Da Acquisition and expires on 31 December 2010.

2. Reasons for the Non-exempt Continuing Connected Transactions

Outsourcing and Purchase Transactions

Hua Da Electronics focuses on the design of ICs and research and development of new technology. It does not own facilities for conducting processing, testing and assembling procedures on IC products as these are not considered its core businesses. Consequently, these procedures have been outsourced to the relevant service providers and they include certain members of the CEC Group.

CEC Group is a nationwide electronics and information technology conglomerate established in 1989 in the PRC with the approval of the PRC State Council and is under the direct administration of the central government of the PRC. It actively focuses on and has made substantial investments in the communication/consumer electronics, semi-conductor and software sectors. Consequently, members of the CEC Group have established themselves as reliable and competitive providers of processing, testing and assembling services to IC design companies such as Hua Da Electronics.

In the past three years, the Outsourcing and Purchase Transactions with members of the CEC Group constituted more than 90% of Hua Da Electronics' total outsourcing and purchase requirements, with the balance being procured and purchased from independent third party suppliers.

According to the Directors, for projects undertaken by Hua Da Electronics, the customers typically dictates the panel of outsourcing service providers and suppliers. CEC Group, being a leading conglomerate in this field in the PRC, has regularly been part of the panel of suppliers and service providers identified by the customers. The management of Hua Da Electronics has confirmed that members of the CEC Group have been providing high quality services at competitive prices.

Sale Transactions

Hua Da Electronics sells its products such as IC cards and smart card modules, chips and EDA tools to members of the CEC Group. The major products under the Sale Transactions are petrol cards to a member of CEC Group and this company is the sole distributor of petrol cards for a major petroleum company. Hua Da Electronics also supplies USB keys and smart card modules to members of the CEC Group which are major distributors of bank cards of financial institutions and so forth. Consequently, if Hua Da Electronics is to participate in the relevant projects, these members of CEC Group will be the major channels.

Canteen Transactions

Under the Canteen Transactions, members of the CEC Group have been engaged to provide canteen facilities and meals to staff of Hua Da Electronics as its management believes such services to staff are ancillary activities. The aforesaid canteen service provider is located in close proximity to its office and has large canteen operations with economies of scale, thereby able to provide such services at comparatively lower costs than if Hua Da Electronics is to operate its own canteen.

We are of the view that the Non-exempt Continuing Connected Transactions are entered into for commercial reasons such as (i) procuring services of designated suppliers of Hua Da Electronics' customers under the Outsourcing and Purchase Transactions; (ii) expanding the source of revenue of Hua Da Electronics by working with designated distributors of major companies under the Sale Transactions; and (iii) sub-contracting ancillary activities which are not Hua Da Electronics' core businesses under the Canteen Transactions. On this basis, we are of the view that it is fair and reasonable to enter into the Non-exempt Continuing Connected Transactions.

3. Historical and future transaction amount

Outsourcing and Purchase Transactions

The historical figures and the proposed annual caps for the Outsourcing and Purchase Transactions are summarised below:

	Historical figures for			Proposed annual caps for		
	2005	2006	2007	2008¹	2009	2010
	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>
Annual service charges paid/						
to be paid	223,464	515,850	375,198	284,640	293,310	421,140

1. For the period commencing from the Completion to 31 December 2008

Between 2005 and 2007, the amount of service charges paid had increased, in line with the growth of Hua Da Electronics' business. The proposed annual caps for 2008, 2009 and 2010 are estimated based on the amount of outsourcing and purchase of raw materials Hua Da Electronics will require for its projects on-hand and future projects. For each of its project, the panel of outsourcing service providers and suppliers are normally identified at the outset and consequently, the amount of service charges payable may be estimated based on the forecast revenue for each project. Notwithstanding, Hua Da Electronics is not obligated nor committed to purchasing only from members of CEC Group if their prices are not competitive, and is able to engage other third party suppliers.

For the remaining year of 2008, the annual service charges are estimated to increase due to increased sale in an ongoing project which a member of the CEC Group has been designated as outsourcing service provider. The amount of service charges are expected to reduce in 2009 as current projects on hand expected to be launched next year involve fewer suppliers which are members of the CEC Group. We believe the above is a reasonable basis to arrive at the proposed annual caps.

The service charges by members of the CEC Group will be determined based on arm's length negotiations with reference to market rates of similar services and products. We have reviewed the prices charged by members of the CEC Group in the past and found that they are comparable to the prices offered by independent third party service providers for similar services and products.

LETTER FROM ALTUS

Sale Transactions

The historical figures and the proposed annual caps for the Sale Transactions are summarised below:

	Historical figures for			Proposed annual caps for		
	2005	2006	2007	2008 ¹	2009	2010
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Payment for sales received/to be received	34,336	42,991	46,886	19,620	36,000	43,200

1. For the period commencing from the Completion to 31 December 2008

The amount of sales to members of the CEC Group has increased between 2005 and 2007 due to the increase in Hua Da Electronics' range of products, which in turn resulted in more projects undertaken with members of the CEC Group. The proposed annual caps for the remaining year of 2008 and in 2009 and 2010 are expected to decrease as certain current projects with members of the CEC Group are expected to end while launches for new products have yet to be confirmed. We believe the above is a reasonable basis to arrive at the proposed annual caps.

The sale prices to members of the CEC Group will be determined based on arm's length negotiations with reference to market rates of similar products. We have reviewed the sale prices charged to members of the CEC Group in the past and found that they are comparable to the sale prices to independent third party customers for similar products.

Canteen Transactions

The historical figures and the proposed annual caps for the Canteen Transactions are summarised below:

	Historical figures for			Proposed annual caps for		
	2005	2006	2007	2008 ¹	2009	2010
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Service fees paid/to be paid	494	459	599	550	1,120	1,160

1. For the period commencing from the Completion to 31 December 2008

The amount of canteen service fees paid to members of the CEC Group will be dependent on the number of Hua Da Electronics' staff using such services and the rates charged for such services. The number of Hua Da Electronic staff has increased since 2005. Consequently, the amount of service fees paid has increased between 2005 and 2007.

The proposed annual caps for the remaining year of 2008 and in 2009 and 2010 are expected to increase substantially. The management explained that this is due to the revision of service fees per meal in 2008 by more than 30%, which is negotiated as a result of high rate of inflation in recent months. Based on our discussion with the management, notwithstanding the increase in service fees, they remain lower than the costs Hua Da Electronics will have to incur if it is to operate the canteen facilities itself. In addition, the revised service fees are competitive compared with other third party suppliers. Another major consideration in the Canteen Transactions is the proximity of Hua Da Electronics' premise to the canteen facilities of the member of CEC Group.

Based on the above, the annual caps have been determined on a reasonable basis with reference to the current projects and expected projects that will be undertaken with members of the CEC Group. The basis for determining the prices for the Non-exempt Continuing Connected Transactions are also fair and reasonable as they will be made with reference to market rates for similar services and products.

RECOMMENDATIONS

The Acquisition

We are of the view that the terms of the Acquisition are on normal commercial terms. Notwithstanding that the Acquisition will result in a dilution of net asset value per Share, having considered the overall benefits of the Acquisition, we believe it is in the interest of the Company and the Shareholders as a whole. We are also of the view that the terms of the agreements relating to the Acquisition are fair and reasonable as far as the Independent Shareholders are concerned.

Based on the above, we recommend the Independent Board Committee and the Independent Shareholders to vote in favour of the proposed resolution approving the Acquisition at the SGM.

The Non-exempt Continuing Connected Transactions

Having considered the principal factors discussed above, we are of the view that the Non-exempt Continuing Connected Transactions with the CEC Group are conducted in the ordinary and usual course of business of the Group. The terms and conditions of the Non-exempt Continuing Connected Transactions, including the proposed annual caps for the Outsourcing and Purchase Transactions, the Sales Transactions and the Canteen Transactions are on normal commercial terms, fair and reasonable and are in the interest of the Group and the Shareholders as a whole. We would therefore advise the Independent Shareholders and the Independent Board Committee to recommend the Independent Shareholders to vote in favour of the resolutions to be proposed at the SGM.

Yours faithfully,
For and on behalf of
Altus Capital Limited
Arnold Ip
Executive Director

The following is the text of a report received from the Company's reporting accountant, PricewaterhouseCoopers, Certified Public Accountants, Hong Kong, for the purpose of incorporation in this circular.



羅兵咸永道會計師事務所

PricewaterhouseCoopers
22/F, Prince's Building
Central, Hong Kong

30 June 2008

The Directors
China Electronics Corporation Holdings Company Limited

Dear Sirs,

We set out below our report on the financial information (the “Financial Information”) of 北京中電華大電子設計有限責任公司 (CEC Huada Electronic Design Co., Ltd.) (the “Target Company”) and its subsidiaries (together, the “Target Group”) set out in Section I to III below, for inclusion in the circular of China Electronics Corporation Holdings Company Limited (the “Company” or “CEC Holdings”) dated 30 June 2008 (the “Circular”) in connection with the proposed acquisition of the Target Group by the Company (the “Proposed Acquisition”). The Financial Information comprises the consolidated balance sheets of the Target Group and the balance sheets of the Target Company as at 31 December 2005, 2006 and 2007, and the consolidated income statements, the consolidated statements of changes in equity and the consolidated cash flow statements of the Target Group for each of the years ended 31 December 2005, 2006 and 2007 (the “Relevant Periods”), and a summary of significant accounting policies and other explanatory notes.

The Target Company was established in the People's Republic of China (the “PRC”) on 6 June 2002 as a company with limited liability under the Company Law of the PRC.

At the date of this report, the Target Company has direct interests in the subsidiaries as set out in Note 7 of Section II. All companies comprising the Target Group are private companies and have adopted 31 December as their financial year end date for statutory reporting and/or management reporting purpose.

The consolidated financial statements of the Target Group for each of the years ended 31 December 2005, 2006 and 2007 which have been prepared in accordance with the Accounting System for Business Enterprise and the Accounting Standards for Business Enterprises (“PRC GAAP”) were audited by 利安達信隆會計師事務所 (Reanda Certified Public Accountants).

The Financial Information has been prepared based on the audited consolidated financial statements of the Target Group prepared in accordance with PRC GAAP, after making such adjustments as are appropriate.

RESPONSIBILITY OF DIRECTORS

The directors of the Target Company during the Relevant Periods are responsible for the preparation and the fair presentation of the consolidated financial statements of the Target Group in accordance with PRC GAAP. The directors of the Company and the Target Company are responsible for the preparation and the true and fair presentation of the Financial Information in accordance with Hong Kong Financial Reporting Standards (“HKFRS”) issued by the Hong Kong Institute of Certified Public Accountants (the “HKICPA”). This responsibility includes designing, implementing and maintaining internal control relevant to the preparation and the true and fair presentation of Financial Information that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

RESPONSIBILITY OF REPORTING ACCOUNTANT

Our responsibility is to express an opinion on the Financial Information based on our examination and to report our opinion to you. We examined the audited consolidated financial statements of the Target Group prepared in accordance with PRC GAAP for the Relevant Periods and the related adjustments made in preparing the Financial Information, and carried out such additional procedures as we considered necessary in accordance with Auditing Guideline 3.340 “Prospectuses and the Reporting Accountant” issued by HKICPA.

OPINION

In our opinion, the Financial Information, for the purpose of this report, gives a true and fair view of the state of affairs of the Target Company and of the Target Group as at 31 December 2005, 2006 and 2007 and of the Target Group’s results and cash flows for the Relevant Periods.

I. FINANCIAL INFORMATION

The following is the Financial Information of the Target Group as at 31 December 2005, 2006 and 2007 and for each of the years ended 31 December 2005, 2006 and 2007.

Consolidated Balance Sheets

	<i>Note</i>	As at 31 December		
		2005	2006	2007
		<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
ASSETS				
Non-current assets				
Property, plant and equipment	5	5,195	7,199	22,296
Intangible assets	6	8,377	9,825	5,333
Deferred income tax assets	22(d)	1,468	1,625	8,865
Investment in an associate	8	2,504	–	–
Available-for-sale financial assets	9	3,845	4,000	4,300
		<u>21,389</u>	<u>22,649</u>	<u>40,794</u>
Current assets				
Inventories	10	28,024	180,992	158,059
Trade and other receivables	11	173,162	270,260	227,567
Cash and cash equivalents	12	24,766	87,952	188,902
		<u>225,952</u>	<u>539,204</u>	<u>574,528</u>
Total assets		<u><u>247,341</u></u>	<u><u>561,853</u></u>	<u><u>615,322</u></u>
EQUITY				
Capital and reserves attributable to the Target Company's equity holders				
Paid-in capital	13	32,642	32,642	32,642
Reserves	14	11,410	25,968	48,025
Retained earnings				
– Proposed final dividend	24	13,435	45,045	148,794
– Others		30,483	97,850	72,219
		<u>87,970</u>	<u>201,505</u>	<u>301,680</u>
Minority interests		<u>1,157</u>	<u>1,065</u>	<u>956</u>
Total equity		<u><u>89,127</u></u>	<u><u>202,570</u></u>	<u><u>302,636</u></u>
LIABILITIES				
Current liabilities				
Trade and other payables	15	127,665	336,165	239,822
Current income tax liabilities		1,703	3,118	8,348
Short term bank loans	16	28,846	20,000	64,516
Total liabilities		<u>158,214</u>	<u>359,283</u>	<u>312,686</u>
Total equity and liabilities		<u><u>247,341</u></u>	<u><u>561,853</u></u>	<u><u>615,322</u></u>
Net current assets		<u><u>67,738</u></u>	<u><u>179,921</u></u>	<u><u>261,842</u></u>
Total assets less current liabilities		<u><u>89,127</u></u>	<u><u>202,570</u></u>	<u><u>302,636</u></u>

Balance Sheets – Target Company

		As at 31 December		
		2005	2006	2007
	Note	HK\$'000	HK\$'000	HK\$'000
ASSETS				
Non-current assets				
Property, plant and equipment	5	4,966	6,454	21,569
Intangible assets	6	3,670	6,287	2,644
Deferred income tax assets	22(d)	1,468	1,625	8,865
Investments in subsidiaries	7	4,808	12,715	8,347
Investment in an associate	8	2,885	–	–
Available-for-sale financial assets	9	3,845	4,000	4,300
		21,642	31,081	45,725
Current assets				
Inventories	10	27,031	180,453	157,087
Trade and other receivables	11	176,554	271,431	219,775
Cash and cash equivalents	12	19,462	76,674	183,799
		223,047	528,558	560,661
Total assets		244,689	559,639	606,386
EQUITY				
Capital and reserves attributable to the Target Company's equity holders				
Paid-in capital	13	32,642	32,642	32,642
Reserves	14	11,333	25,892	48,171
Retained earnings				
– Proposed final dividend	24	13,435	45,045	148,794
– Others		30,684	99,439	75,688
Total equity		88,094	203,018	305,295
LIABILITIES				
Current liabilities				
Trade and other payables	15	126,046	333,503	228,227
Current income tax liabilities		1,703	3,118	8,348
Short term bank loans	16	28,846	20,000	64,516
Total liabilities		156,595	356,621	301,091
Total equity and liabilities		244,689	559,639	606,386
Net current assets		66,452	171,937	259,570
Total assets less current liabilities		88,094	203,018	305,295

Consolidated Income Statements

		Year ended 31 December		
		2005	2006	2007
	<i>Note</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Revenue		295,524	508,717	652,767
Cost of sales	17	<u>(215,823)</u>	<u>(327,554)</u>	<u>(399,877)</u>
Gross profit		79,701	181,163	252,890
Selling and marketing costs	17	(8,525)	(11,741)	(15,928)
Administrative expenses	17	(50,000)	(59,974)	(111,905)
Other gains – net	19	<u>22,316</u>	<u>19,900</u>	<u>8,457</u>
Operating profit		43,492	129,348	133,514
Finance income		498	992	1,144
Finance costs		<u>(2,174)</u>	<u>(1,624)</u>	<u>(2,595)</u>
Finance costs – net	21	<u>(1,676)</u>	<u>(632)</u>	<u>(1,451)</u>
Profit before income tax		41,816	128,716	132,063
Income tax expense	22(a)	<u>(2,383)</u>	<u>(8,690)</u>	<u>(4,756)</u>
Profit for the year		<u>39,433</u>	<u>120,026</u>	<u>127,307</u>
Attributable to:				
Equity holders of the Target Company	23	40,352	120,202	127,443
Minority interests		<u>(919)</u>	<u>(176)</u>	<u>(136)</u>
		<u>39,433</u>	<u>120,026</u>	<u>127,307</u>
Dividends	24	<u>13,435</u>	<u>45,045</u>	<u>148,794</u>

Consolidated Statements of Changes in Equity

		Attributable to equity holders of the Target Company					
	Note	Paid-in capital HK\$'000 (Note 13)	Reserves HK\$'000 (Note 14)	Retained earnings HK\$'000	Total HK\$'000	Minority interests HK\$'000	Total equity HK\$'000
Balance at 1 January 2005		30,154	1,996	9,390	41,540	–	41,540
Currency translation differences		–	1,240	–	1,240	11	1,251
Net income recognised directly in equity		–	1,240	–	1,240	11	1,251
Profit for the year		–	–	40,352	40,352	(919)	39,433
Total recognised income and expense for the year		–	1,240	40,352	41,592	(908)	40,684
Capital injection from shareholders		2,488	2,350	–	4,838	–	4,838
Acquisition of subsidiaries		–	–	–	–	2,065	2,065
Appropriation to other reserves		–	5,824	(5,824)	–	–	–
Balance at 31 December 2005		32,642	11,410	43,918	87,970	1,157	89,127
Balance at 1 January 2006		32,642	11,410	43,918	87,970	1,157	89,127
Currency translation differences		–	6,768	–	6,768	42	6,810
Net income recognised directly in equity		–	6,768	–	6,768	42	6,810
Profit for the year		–	–	120,202	120,202	(176)	120,026
Total recognised income and expense for the year		–	6,768	120,202	126,970	(134)	126,836
Dividends related to 2005		–	–	(13,435)	(13,435)	–	(13,435)
Acquisition of subsidiaries		–	–	–	–	42	42
Appropriation to other reserves		–	7,790	(7,790)	–	–	–
Balance at 31 December 2006		32,642	25,968	142,895	201,505	1,065	202,570
Balance at 1 January 2007		32,642	25,968	142,895	201,505	1,065	202,570
Currency translation differences		–	17,777	–	17,777	74	17,851
Net income recognised directly in equity		–	17,777	–	17,777	74	17,851
Profit for the year		–	–	127,443	127,443	(136)	127,307
Total recognised income and expense for the year		–	17,777	127,443	145,220	(62)	145,158
Dividends related to 2006		–	–	(45,045)	(45,045)	–	(45,045)
Acquisition of additional interest in subsidiaries		–	–	–	–	(47)	(47)
Appropriation to other reserves		–	4,280	(4,280)	–	–	–
Balance at 31 December 2007		32,642	48,025	221,013	301,680	956	302,636

Consolidated Cash Flow Statements

		Year ended 31 December		
		2005	2006	2007
	<i>Note</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Cash flows from operating activities				
Cash (used in)/generated				
from operations	25	(20,881)	98,070	121,387
Interest paid		(2,174)	(1,624)	(2,595)
Income tax paid		(1,310)	(7,564)	(7,933)
Net cash (used in)/generated				
from operating activities		(24,365)	88,882	110,859
Cash flows from investing activities				
Interest received		498	992	1,144
Purchase of property, plant and				
equipment and intangible assets		(2,255)	(8,924)	(17,606)
Proceeds on disposal of property,				
plant and equipment	25(a)	–	–	81
Dividend received		–	–	376
Net cash (paid)/received for				
acquisition of subsidiaries	7(d)	(3,603)	2,433	(47)
Net cash used in investing activities		(5,360)	(5,499)	(16,052)
Cash flows from financing activities				
Dividend paid	24	–	(13,435)	(45,045)
Proceeds from bank loans		47,618	33,980	83,333
Repayment of bank loans		(33,333)	(43,689)	(41,667)
Capital received		4,838	–	–
Net cash generated from/(used in)				
financing activities		19,123	(23,144)	(3,379)
Effects of exchange rate changes				
on cash and cash equivalents				
		614	2,947	9,522
Net (decrease)/increase in cash and				
cash equivalents				
		(9,988)	63,186	100,950
Cash and cash equivalents				
at beginning of the year		34,754	24,766	87,952
Cash and cash equivalents				
at end of the year		24,766	87,952	188,902

II. NOTES TO THE FINANCIAL INFORMATION

1. BACKGROUND OF THE TARGET GROUP

The Target Company was established in the PRC on 6 June 2002 as a limited liability company under the Company Law of the PRC. The Target Group is engaged in design and sale of integrated circuit. The address of the Target Company's registered office is No.1. Gaojiayuan, Chaoyang District, Beijing, the People's Republic of China.

The Target Company is controlled by China Huada Integrated Circuit Design (Group) Co., Ltd. ("CIDC") which owns 64.75% of the Target Company's interests. CIDC is jointly owned and controlled by China Electronics Corporation ("CEC") and State Development & Investment Corp. ("SDIC"). Both CEC and SDIC are state-owned enterprises established in the PRC.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies applied in the preparation of the Financial Information are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

2.1 Basis of preparation

The Financial Information of the Target Group have been prepared in accordance with HKFRS issued by the HKICPA. The Financial Information has been prepared under the historical cost convention.

The preparation of Financial Information in conformity with HKFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Target Group's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the Financial Information, are disclosed in Note 4.

The Financial Information is the first set of the Target Group's financial statements prepared in accordance with HKFRS. The Financial Information has been prepared in accordance with disclosure requirements for the first time adoption of HKFRS. HKFRS 1, "First-time Adoption of Hong Kong Financial Reporting Standards", has been applied in preparing this Financial Information.

In preparing these Financial Information in accordance with HKFRS 1, the Target Group has applied one optional exemptions from full retrospective application of HKFRS 2, "Share-based Payment". It applied HKFRS 2 from 1 January 2005 to those share that were granted after 7 November 2002.

The directors of the Target Company have prepared the consolidated financial statements of the Target Group for each of the years ended 31 December 2005, 2006 and 2007 in accordance with PRC GAAP. PRC GAAP differs in certain aspects from HKFRS. Reconciliations and descriptions of the effect of the conversion from PRC GAAP to HKFRS on the Target Group's total equity and profit for the year are as follows:

	Total equity as at 1 January 2005 HK\$'000	Total equity as at 31 December 2007 HK\$'000	Profit for the year ended 31 December 2007 HK\$'000
Amounts per PRC GAAP	39,107	252,921	99,052
GAAP Adjustments:			
To write back the over-accrual of welfare according to the HKFRS	1,597	499	(3,694)
Deferred tax assets	834	8,865	6,895
Other retrospective adjustments:			
Revenue cut-off adjustment and related tax impact	1,448	25,480	22,822
Reversal of over-accrual of cost of sales and related tax impact	1,495	13,215	(1,548)
Provision of inventory impairment to write down carrying value of certain inventories to their net realizable value and related tax impact	–	(942)	(912)
Cut-off adjustment to recognise expenses/income relating to government grants and related tax impact	(3,171)	4,355	5,550
Provision of additional income tax liabilities based on taxable income for the year	–	(2,304)	(283)
Others	230	547	(575)
Amount per HKFRS	41,540	302,636	127,307

- (a) *Standards, amendments and interpretations to existing standards that are not yet effective and have not been early adopted.*

The following standards, amendments and interpretations to existing standards have been published and are mandatory for the Target Group's accounting periods beginning on or after 1 January 2008 or later periods, and the Target Group has not early adopted them:

HKAS 1 (Revised), 'Presentation of Financial Statements' (effective from 1 January 2009). HKAS 1 (Revised) requires all owner changes in equity to be presented in a statement of changes in equity. All comprehensive income is presented in one statement of comprehensive income or in two statements (a separate income statement and a statement of comprehensive income). It requires presenting a statement of financial position as at the beginning of the earliest comparative period in a complete set of financial statements when there are retrospective adjustments or reclassification adjustments. However, it does not change the recognition, measurement or disclosure of specific transactions and other events required by other HKFRS. The Target Group will apply HKAS 1 (Revised) from 1 January 2009. The directors of the Target Group are assessing the impact.

HKAS 23 (Revised), 'Borrowing costs' (effective from 1 January 2009). The amendment requires an entity to capitalise borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset (one that takes a substantial period of time to get ready for use or sale) as part of the cost of that asset. The option of immediately expensing those borrowing costs will be removed. The Target Group will apply HKAS 23 (Revised) from 1 January 2009 which is not expected to have any impact on the Target Group's financial statements.

HKFRS 8, 'Operating segments' (effective from 1 January 2009). HKFRS 8 replaces HKAS 14 and aligns segment reporting with the requirements of the US standard SFAS 131, 'Disclosures about segments of an enterprise and related information'. The new standard requires a 'management approach', under which segment information is presented on the same basis as that used for internal reporting purposes. The Target Group will apply HKFRS 8 from 1 January 2009. The directors of the Target Group are assessing the impact.

HK(IFRIC) – Int 11, 'HKFRS 2 – Group and treasury share transactions', (effective from 1 March 2007). HK(IFRIC) – Int 11 provides guidance on whether share-based transactions involving treasury shares or involving Group entities (for example, options over a parent's shares) should be accounted for as equity-settled or cash-settled share-based payment transactions in the stand-alone accounts of the parent and group companies. This interpretation does not have an impact on the Target Group's financial statements.

HK(IFRIC) – Int 12, 'Service concession arrangements' (effective from 1 January 2008). HK(IFRIC) – Int 12 applies to contractual arrangements whereby a private sector operator participates in the development, financing, operation and maintenance of infrastructure for public sector services. HK(IFRIC) – Int 12 is not relevant to the Target Group's operations because none of the Target Group's companies provide public sector services.

HK(IFRIC) – Int 13, 'Customer loyalty programmes' (effective from 1 July 2008). HK(IFRIC) – Int 13 clarifies that where goods or services are sold together with a customer loyalty incentive (for example, loyalty points or free products), the arrangement is a multiple-element arrangement and the consideration receivable from the customer is allocated between the components of the arrangement using fair values. HK(IFRIC) – Int 13 is not relevant to the Target Group's operations because none of the Target Group's companies operate any loyalty programmes.

HKAS 27 (Revised) 'Consolidated and Separate Financial Statements' (effective from annual period beginning on or after 1 July 2009). The amendment requires non-controlling interests (i.e. minority interests) to be presented in the consolidated statement of financial position within equity, separately from the equity of the owners of the parent. Total comprehensive income must be attributed to the owners of the parent and to the non-controlling interests even if this results in the non-controlling interests having a deficit balance. Changes in a parent's ownership interest in a subsidiary that do not result in the loss of control are accounted for within equity. When control of a subsidiary is lost, the assets and liabilities and related equity components of the former subsidiary are derecognised. Any gain or loss is recognised in profit or loss. Any investment retained in the former subsidiary is measured at its fair value at the date when control is lost. The Target Group will apply HKAS 27 (Revised) from 1 January 2010. The directors of the Target Group are assessing the impact.

HKFRS 3 (Revised) 'Business Combination' (effective for business combinations with acquisition date on or after the beginning of the first annual reporting period beginning on or after 1 July 2009). The amendment may bring more transactions into acquisition accounting as combinations by contract alone and combinations of mutual entities are brought into the scope of the standard and the definition of a business has been amended slightly. It now states that the elements are 'capable of being conducted' rather than 'are conducted and managed'. It requires considerations (including contingent consideration), each identifiable asset and liability to be measured at its acquisition-date fair value, except leases and insurance contracts, reacquired right, indemnification assets as well as some assets and liabilities required to be measured in accordance with other HKFRS. They are income taxes, employee benefits, share-based payment and non current assets held for sale and discontinued operations. Any non-controlling interest in an acquiree is measured either at fair value or at the non-controlling interest's proportionate share of the acquiree's net identifiable assets. The Target Group will apply HKFRS 3 (Revised) from 1 January 2010. The directors of the Target Group are assessing the impact.

HKFRS 2 Amendment 'Share-based Payment Vesting Conditions and Cancellations' (effective from 1 January 2009). The amendment clarifies the definition of 'vesting conditions' and specifies the accounting treatment of "cancellations" by the counterparty to a share-based payment arrangement. Vesting conditions are service conditions (which require a counterparty to complete a specified period of service) and performance conditions (which require a specified period of service and specified performance targets to be met) only. All 'non-vesting conditions' and vesting conditions that are market conditions shall be taken into account when estimating the fair value of the equity instruments granted. All cancellations are accounted for as an acceleration of vesting and the amount that would otherwise have been recognised over the remainder of the vesting period is recognised immediately. The Target Group will apply HKFRS 2 Amendment from 1 January 2009 which it is not expected to have any impact on the Target Group's financial statements.

2.2 Consolidation

(a) Subsidiaries

Subsidiaries are all entities over which the Target Group has the power to govern the financial and operating policies generally accompanying a shareholding of more than one half of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Target Group controls another entity.

Subsidiaries are fully consolidated from the date on which control is transferred to the Target Group. They are de-consolidated from the date that control ceases.

The purchase method of accounting is used to account for the acquisition of subsidiaries by the Target Group. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any minority interest. The excess of the cost of acquisition over the fair value of the Target Group's share of the identifiable net assets acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognised directly in the income statement.

Inter-company transactions, balances and unrealised gains on transactions between group companies are eliminated. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Target Group.

In the Target Company's balance sheet the investments in subsidiaries are stated at cost less provision for impairment losses (Note 2.7). The results of subsidiaries are accounted for by the Target Company on the basis of dividend received and receivable.

(b) Associates

Associates are all entities over which the Target Group has significant influence but not control, generally accompanying a shareholding of between 20% and 50% of the voting rights. Investments in associates are accounted for using the equity method of accounting and are initially recognised at cost. The Target Group's investment in associates includes goodwill (net of any accumulated impairment loss) identified on acquisition (Note 2.6).

The Target Group's share of its associates' post-acquisition profits or losses is recognised in the income statement, and its share of post-acquisition movements in reserves is recognised in reserves. The cumulative post-acquisition movements are adjusted against the carrying amount of the investment. When the Target Group's share of losses in an associate equals or exceeds its interest in the associate, including any other unsecured receivables, the Target Group does not recognise further losses, unless it has incurred obligations or made payments on behalf of the associate.

Unrealised gains on transactions between the Target Group and its associates are eliminated to the extent of the Target Group's interest in the associates. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of associates have been changed where necessary to ensure consistency with the policies adopted by the Target Group.

Dilution gains and losses in associates are recognised in the consolidated income statement.

In the Target Company's balance sheet the investments in associated companies are stated at cost less provision for impairment losses (Note 2.7). The results of associated companies are accounted for by the Company on the basis of dividend received and receivable.

2.3 Foreign currency translation

(a) *Functional and presentation currency*

Items included in the financial statements of each of the Target Group's entities are measured using the currency of the primary economic environment in which the entity operates (the "functional currency"). The Financial Information are presented in Hong Kong dollar ("HK dollar"), which is different from the Target Company's functional currency of Renminbi. The Directors of the Company consider that presentation of Financial Information in Hong Kong dollars will facilitate analysis of Financial Information of the Target Group.

(b) *Transactions and balances*

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement.

(c) *Group companies*

The results and financial position of all the Target Group entities (none of which has the currency of a hyperinflationary economy) that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

- assets and liabilities for each balance sheet presented are translated at the closing rate at the date of that balance sheet;
- income and expenses for each income statement are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the dates of the transactions); and
- all resulting exchange differences are recognised as a separate component of equity.

When a foreign operation is partially disposed of or sold, such exchange differences that were recorded in equity are recognised in the income statement as part of the gain or loss on sale.

2.4 Segment reporting

The Target Group operates and manages its business as a single segment. The Target Group also operates within one geographical segment because its revenues are generated in the PRC and its assets are located in the PRC. Accordingly, no geographical segment data is presented.

2.5 Property, plant and equipment

Property, plant and equipment are stated at historical cost less depreciation and impairment losses. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Target Group and the cost of the item can be measured reliably. The carrying amount of the replaced part is derecognised. All other repairs and maintenance are expensed in the income statement during the financial period in which they are incurred.

Depreciation of property, plant and equipment is calculated using the straight-line method to allocate cost to their residual values over their estimated useful lives, as follows:

– Machinery	5-10 years
– Motor vehicles	10 years
– Furniture and fixtures	3 years

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount (Note 2.7).

Gains and losses on disposals are determined by comparing the proceeds with the carrying amount and are recognised in the income statement.

2.6 Intangible assets

(a) Goodwill

Goodwill represents the excess of the cost of an acquisition over the fair value of the Target Group's share of the net identifiable assets of the acquired subsidiary at the date of acquisition. Goodwill on acquisition of subsidiaries is included in intangible assets. Goodwill is tested annually for impairment and carried at cost less accumulated impairment losses. Impairment losses on goodwill are not reversed. Gains and losses on the disposal of an entity include the carrying amount of goodwill relating to the entity sold.

Goodwill is allocated to cash-generating units for the purpose of impairment testing. The allocation is made to those cash-generating units or groups of cash-generating units that are expected to benefit from the business combination in which the goodwill arose.

(b) Computer software

Acquired computer software licences are capitalised on the basis of the costs incurred to acquire and bring to use the specific software. These costs are amortised over their estimated useful lives (four to five years).

Costs associated with developing or maintaining computer software programmes are recognised as an expense as incurred. Costs that are directly associated with the development of identifiable and unique software products controlled by the Target Group, and that will probably generate economic benefits exceeding costs beyond one year, are recognised as intangible assets. Direct costs include the employee costs incurred as a result of developing software and an appropriate portion of relevant overheads.

Computer software development costs recognised as assets are amortised over their estimated useful lives.

2.7 Impairment of investments in subsidiaries, associate and non-financial assets

Assets that have an indefinite useful life or have not yet available for use are not subject to amortisation and are tested annually for impairment. Assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). Non-financial assets other than goodwill that suffered an impairment are reviewed for possible reversal of the impairment at each reporting date.

2.8 Financial assets

The Target Group classifies its financial assets in the following categories: loans and receivables, and available-for-sale financial assets. The classification depends on the purpose for which the financial assets were acquired. Management determines the classification of its financial assets at initial recognition.

(a) *Loans and receivables*

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are included in current assets, except for maturities greater than 12 months after the balance sheet date. These are classified as non-current assets. Loans and receivables are classified as trade and other receivables in the balance sheet (Note 2.10).

(b) *Available-for-sale financial assets*

Available-for-sale financial assets are non-derivatives that are either designated in this category or not classified in any of the other categories. They are included in non-current assets unless management intends to dispose of the investment within 12 months of the balance sheet date.

Regular purchases and sales of financial assets are recognised on trade-date – the date on which the Target Group commits to purchase or sell the asset. Financial assets are derecognised when the rights to receive cash flows from the investments have expired or have been transferred and the Target Group has transferred substantially all risks and rewards of ownership. However, the available-for-sale financial assets that do not have a quoted market price, the range of reasonable fair value estimates is significant and the possibilities of the various estimates can not be reasonably assessed, is measured at cost. Loans and receivables are carried at amortised cost using the effective interest method.

When securities classified as available for sale are sold or impaired, the accumulated fair value adjustments recognised in equity are included in the income statement.

Interest on available-for-sale securities calculated using the effective interest method is recognised in the income statement as part of other income. Dividends on available-for-sale equity instruments are recognised in the income statement as part of other income when the Target Group's right to receive payments is established.

The Target Group assesses at each balance sheet date whether there is objective evidence that a financial asset or a group of financial assets is impaired. In the case of equity securities classified as available for sale, a significant or prolonged decline in the fair value of the security below its cost is considered as an indicator that the securities are impaired. If any such evidence exists for available-for-sale financial assets, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in profit or loss – is removed from equity and recognised in the income statement. Impairment losses recognised in the income statement on equity instruments are not reversed through the income statement. Impairment testing of trade receivables is described in Note 2.10.

2.9 Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is determined using the weighted average method. The cost of finished goods and work in progress comprises raw material, manufacturing cost of subcontractors, testing and packaging. It excludes borrowing costs. Net realisable value is the estimated selling price in the ordinary course of business, less applicable variable selling expenses.

2.10 Trade and other receivables

Trade and other receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less provision for impairment. A provision for impairment of trade and other receivables is established when there is objective evidence that the Target Group will not be able to collect all amounts due according to the original terms of receivables. Significant financial difficulties of the debtor, probability that the debtor will enter bankruptcy or financial reorganisation, and default or delinquency in payments are considered indicators that the trade receivable is impaired. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account, and the amount of the loss is recognised in the income statement within administrative expenses. Where evidence exists that a receivable can not be collected, either due to long time overdue or the customer is liquidated or dissolved, the receivable is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited against administrative expenses in the income statement.

2.11 Cash and cash equivalents

Cash and cash equivalents include cash in hand, deposits held at call with banks, financial institutions and entities, other short-term highly liquid investments with original maturities of three months or less.

2.12 Paid-in capital

Paid-in capital represents contributions made by investors in accordance with the amount specified in the contracts, agreements or the enterprise's application document for incorporation.

2.13 Government grants

Government grants are recognised at their fair values where there is a reasonable assurance that the grant will be received and the Target Group will comply with all attached conditions. Grants relating to assets are included in non-current liabilities, which are credited to the income statement on a straight-line basis over the expected lives of the related assets. Grants relating to costs are deferred and recognised in the income statement over the period necessary to match them with the costs that they are intended to compensate.

2.14 Trade payables

Trade payables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method.

2.15 Borrowings

Borrowings are recognised initially at fair value, net of transaction costs incurred. Borrowings are subsequently stated at amortised cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognised in the income statement over the period of the borrowings using the effective interest method.

Borrowings are classified as current liabilities unless the Target Group has an unconditional right to defer settlement of the liability for at least 12 months after the balance sheet date.

2.16 Current and deferred income tax

The current income tax charge is calculated on the basis of the tax laws enacted or substantively enacted at the balance sheet date in the countries where the Target Company and its subsidiaries and associates operate and generate taxable income. Management of the Target Company periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation and establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

Deferred income tax 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 Financial Information. However the deferred income tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

Deferred income 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.

Deferred income tax is provided on temporary differences arising on investments in subsidiaries, except where the timing of the reversal of the temporary difference is controlled by the Target Group and it is probable that the temporary difference will not reverse in the foreseeable future.

2.17 Provision

Provisions are recognised when: the Target 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 the amount has been reliably estimated. Provisions are not recognised for future operating losses.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognised even if the likelihood of an outflow with respect to any one item included in the same class of obligations may be small.

Provisions are measured at the present value of expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to passage of time is recognised as interest expense.

2.18 Employee benefits

(a) Pension obligations

The Target Group's subsidiaries operating in the People's Republic of China (the "PRC") have 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 income statement as and when incurred.

Full time employees in Mainland China are covered by a state-sponsored defined contribution pension scheme under which the employees are entitled to an annual pension equal to a fixed proportion of their basic salaries at their retirement dates. The PRC government is responsible for the pension liability to these retired employees. The Target Group was required to make defined contributions to the pension scheme at the rate of 20% of the employees' basic salaries for each of the years ended 31 December 2005, 2006 and 2007. Under this scheme, the Target Group has no obligation for post-retirement benefits beyond the annual contributions.

(b) 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.

(c) Bonus plans

The expected cost of bonus payments are recognised as a liability when the Target 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 bonus plans are expected to be settled within 12 months and are measured at the amounts expected to be paid when they are settled.

2.19 Contingent liabilities

A contingent liability is a possible obligation that arises from past events and whose existence will only be confirmed by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the Target 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.

2.20 Revenue recognition

Revenue comprises the fair value of the consideration received or receivable for the sale of goods, net of value-added tax, and returns. Revenue is recognised when the goods are delivered to customers, the customers have accepted the goods or the product quality inspection time period has elapsed and collectability of the related receivables is reasonably assured.

Interest income is recognised on a time-proportion basis using the effective interest method. When a receivable is impaired, the Target Group reduces the carrying amount to its recoverable amount, being the estimated future cash flow discounted at original effective interest rate of the instrument, and continues unwinding the discount as interest income.

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

2.21 Operating leases (as the lessee for operating leases)

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are charged to the income statement on a straight-line basis over the period of the lease.

2.22 Research and development

Research and development costs are expensed as incurred.

2.23 Dividend distribution

Dividend distribution to the Target Company's shareholders is recognised as a liability in the Target Group's financial statements in the period in which the dividends are approved by the Target Company's shareholders.

3. FINANCIAL RISK MANAGEMENT

3.1 Financial risk factors

The Target Group's activities expose it to a variety of financial risks: foreign exchange risk, credit risk, liquidity risk and fair value interest rate risk. The Target Group's overall risk management programme focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the Target Group's financial performance.

(a) Foreign exchange risk

The Target Group has no significant concentrations of foreign exchange risk. Foreign exchange risks of the Target Group occur due to the fact that the Target Group has some business activities denominated in foreign currencies, primarily with respect to the United States dollar ("US dollar") and HK dollar. Foreign exchange risk arises from future commercial transactions and recognised assets and liabilities, including cash and cash equivalents and trade and other payable which are denominated in foreign currencies. In addition, the conversion of Renminbi into foreign currencies is subject to the rules and regulations of foreign exchange control promulgated by the PRC government.

The Target Group currently does not have a foreign currency hedge policy.

As less than 10% of the Target Group's transactions are denominated in foreign currencies, the directors of the Target Group are of the view that foreign exchange risk in relation to transactions denominated in foreign currencies is low. Therefore, no sensitivity analysis for these currencies is presented.

(b) Credit risk

The Target Group has no significant concentrations of credit risk. Credit risk arises from cash and cash equivalents and trade and other receivables. The carrying amounts of these balances represent the Target Group's maximum exposure to credit risk.

The Target Group has policies to ensure that the bank balances and short term deposits are placed with banks and financial institutions with good reputation and credit quality. During the Relevant Periods, the Target Group's bank balances and short term deposits were placed with the Bank of Beijing, Hua Xia Bank, Industrial Bank Co, Ltd., China Electronics Corporation Finance Co., Ltd. and New Times Securities Co., Ltd..

The counterparties of the trade and other receivables are mainly state-owned enterprises or related companies. As there was no recent history of defaults by them that have resulted into material bad debts expenses during the Relevant Period, the directors of the Target Group are of the view that credit quality of the trade and other receivables is high.

(c) Liquidity risk

Prudent liquidity risk management implies maintaining sufficient working capital, the availability of funding through an adequate amount of committed credit facilities and the ability to close out market positions. Due to the dynamic nature of the underlying business, the Target Group maintains flexibility in funding by keeping availability of committed credit lines.

The table below analyses the Target Group and the Target Company's financial liabilities that will be settled into relevant maturity groupings based on the remaining period at the balance sheet to the contractual maturity date. The amounts disclosed in the table are the contractual undiscounted cash flows. Balances due within 12 months equal their carrying balances, as the impact of discounting is not significant.

	Target Group			Target Company		
	As at 31 December			As at 31 December		
	2005	2006	2007	2005	2006	2007
Less than 1 year	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Short term bank loans	28,846	20,000	64,516	28,846	20,000	64,516
Interest payment on short term bank loans	956	946	3,402	956	946	3,402
Trade and other payables	112,501	328,501	193,014	112,231	326,605	182,289

(d) Fair value interest rate risk

The Target Group has no significant concentrations of fair value interest rate risk.

Other than deposits held in banks which were fixed rates, the Target Group does not have significant interest-bearing assets. The average rates of deposits held in banks as at 31 December 2005, 2006 and 2007 were approximately 1.69%, 1.52% and 1.07% per annum, respectively.

The Target Group is also exposed to fair value interest rate risk in relation to its fixed rate bank borrowings.

Since the financial assets and liabilities that are exposed to fair value interest rate risk are accounted for at amortised cost based on effective interest rate, its income statement and equity would not be affected by interest rate variability, therefore no sensitivity analysis has been presented.

3.2 Capital risk management

The Target Group's objectives when managing capital are to safeguard the Target Group's ability to continue as a going concern in order to provide returns for shareholders and benefits for other stakeholders and to maintain an optimal capital structure to reduce the cost of capital.

The Target Group reviews its capital structure regularly to ensure acceptable returns to its equity owner and accesses its future capital requirements, if necessary.

The Target Group monitors capital on the basis of the gearing ratio. This ratio is calculated as net debt divided by total capital. Net debt is calculated as total borrowings (including bank borrowings as shown in the consolidated balance sheets) less cash and cash equivalents. Total capital is calculated as equity, as shown in the consolidated balance sheet, plus net debt.

Total capital of the Target Group were HK\$93,207,000, HK\$134,618,000 and HK\$178,250,000 as at 31 December 2005, 2006 and 2007, respectively. The gearing ratio as at 31 December 2005 was 4%. As at 31 December 2006 and 2007, the cash and cash equivalents balances were greater than the balances of total borrowings. The directors are of the opinion that the Target Group does not have significant capital risk.

3.3 Fair value estimation

The Target Group's financial instruments mainly consist of cash and cash equivalents, trade and other receivables (excluding prepayment), available-for-sale financial assets, trade and other payables and short term bank loans.

The carrying amounts of financial instruments approximated their fair values at December 31, 2005, 2006 and 2007 because of the short-term maturities of these financial assets and financial liabilities.

4. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

(a) Estimated impairment of non-financial assets

At each balance sheet date, the Target Group considers both internal and external sources of information to assess whether there is any indication that assets are impaired. If any such indication exists, the recoverable amount of the asset is estimated and an impairment loss is recognised to reduce the carrying amount of the asset to its recoverable amount. Accordingly, there will be an impact to the future results if there is a significant change in the recoverable amounts of the assets.

(b) Income taxes

The Target Group is subject to income taxes in several jurisdictions. Significant judgement is required in determining the total provision for income taxes. There are many transactions and calculations for which the ultimate tax determination is uncertain during the ordinary course of business. The Target Group recognises liabilities for anticipated tax audit issues based on estimates of whether additional taxes will be due. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the income tax and deferred tax provisions in the period in which such determination is made.

(c) Revenue recognition

Goods shipped to certain customers are subject to quality inspection procedures. The customers have the right to return all the goods delivered during the inspection period. Since the quality inspection is performed by customers, the fulfilment of the quality standard is subject to various risks, including the quality checking method, tools and sampling risk. Management can not reasonably estimate the possibility of return, therefore, revenue is recognised when the products are formally accepted by the customer or the quality inspection period has elapsed.

5. PROPERTY, PLANT AND EQUIPMENT

Target Group

	Machinery <i>HK\$'000</i>	Motor vehicles <i>HK\$'000</i>	Furniture and fixtures <i>HK\$'000</i>	Total <i>HK\$'000</i>
At 1 January 2005				
Cost	9,077	857	–	9,934
Accumulated depreciation and impairment	(4,728)	(42)	–	(4,770)
Net book amount	4,349	815	–	5,164
Year ended 31 December 2005				
Opening net book amount	4,349	815	–	5,164
Exchange differences	83	19	–	102
Additions	1,763	406	–	2,169
Acquisition of a subsidiary	163	–	–	163
Depreciation charge	(2,274)	(129)	–	(2,403)
Closing net book amount	4,084	1,111	–	5,195
At 31 December 2005				
Cost	11,201	1,284	–	12,485
Accumulated depreciation and impairment	(7,117)	(173)	–	(7,290)
Net book amount	4,084	1,111	–	5,195
Year ended 31 December 2006				
Opening net book amount	4,084	1,111	–	5,195
Exchange differences	214	44	–	258
Additions	3,343	178	74	3,595
Acquisition of a subsidiary	138	–	–	138
Disposals	(121)	–	–	(121)
Depreciation charge	(1,667)	(195)	(4)	(1,866)
Closing net book amount	5,991	1,138	70	7,199
At 31 December 2006				
Cost	15,111	1,517	74	16,702
Accumulated depreciation and impairment	(9,120)	(379)	(4)	(9,503)
Net book amount	5,991	1,138	70	7,199
Year ended 31 December 2007				
Opening net book amount	5,991	1,138	70	7,199
Exchange differences	866	124	5	995
Additions	15,225	1,533	136	16,894
Disposals	–	(131)	–	(131)
Depreciation charge	(2,371)	(207)	(83)	(2,661)
Closing net book amount	19,711	2,457	128	22,296
At 31 December 2007				
Cost	25,402	3,021	215	28,638
Accumulated depreciation and impairment	(5,691)	(564)	(87)	(6,342)
Net book amount	19,711	2,457	128	22,296

Depreciation expense has been charged in selling and marketing costs and administrative expenses as follows:

	Year ended 31 December		
	2005 HK\$'000	2006 HK\$'000	2007 HK\$'000
Selling and marketing costs	112	47	213
Administrative expenses	2,291	1,819	2,448
	<u>2,403</u>	<u>1,866</u>	<u>2,661</u>
Target Company			
	Machinery HK\$'000	Motor vehicles HK\$'000	Total HK\$'000
At 1 January 2005			
Cost	9,077	857	9,934
Accumulated depreciation and impairment	<u>(4,728)</u>	<u>(42)</u>	<u>(4,770)</u>
Net book amount	<u>4,349</u>	<u>815</u>	<u>5,164</u>
Year ended 31 December 2005			
Opening net book amount	4,349	815	5,164
Exchange differences	81	18	99
Additions	1,346	298	1,644
Disposals	—	—	—
Depreciation charge	<u>(1,835)</u>	<u>(106)</u>	<u>(1,941)</u>
Closing net book amount	<u>3,941</u>	<u>1,025</u>	<u>4,966</u>
At 31 December 2005			
Cost	10,615	1,175	11,790
Accumulated depreciation and impairment	<u>(6,674)</u>	<u>(150)</u>	<u>(6,824)</u>
Net book amount	<u>3,941</u>	<u>1,025</u>	<u>4,966</u>
Year ended 31 December 2006			
Opening net book amount	3,941	1,025	4,966
Exchange differences	199	38	237
Additions	2,990	—	2,990
Disposals	(397)	—	(397)
Depreciation charge	<u>(1,223)</u>	<u>(119)</u>	<u>(1,342)</u>
Closing net book amount	<u>5,510</u>	<u>944</u>	<u>6,454</u>
At 31 December 2006			
Cost	13,711	1,222	14,933
Accumulated depreciation and impairment	<u>(8,201)</u>	<u>(278)</u>	<u>(8,479)</u>
Net book amount	<u>5,510</u>	<u>944</u>	<u>6,454</u>
Year ended 31 December 2007			
Opening net book amount	5,510	944	6,454
Exchange differences	832	111	943
Additions	15,225	1,533	16,758
Disposals	(5)	(126)	(131)
Depreciation charge	<u>(2,299)</u>	<u>(156)</u>	<u>(2,455)</u>
Closing net book amount	<u>19,263</u>	<u>2,306</u>	<u>21,569</u>
At 31 December 2007			
Cost	23,894	2,707	26,601
Accumulated depreciation and impairment	<u>(4,631)</u>	<u>(401)</u>	<u>(5,032)</u>
Net book amount	<u>19,263</u>	<u>2,306</u>	<u>21,569</u>

6. INTANGIBLE ASSETS

	Target Group			Target Company
	Goodwill <i>HK\$'000</i>	Computer software <i>HK\$'000</i>	Total <i>HK\$'000</i>	Computer software <i>HK\$'000</i>
At 1 January 2005				
Cost	–	9,401	9,401	9,401
Accumulated amortisation and impairment	–	(3,726)	(3,726)	(3,726)
Net book amount	–	5,675	5,675	5,675
Year ended 31 December 2005				
Opening net book amount	–	5,675	5,675	5,675
Additions	–	82	82	22
Acquisition of a subsidiary	–	6,293	6,293	–
Disposals	–	–	–	–
Amortisation charge	–	(3,810)	(3,810)	(2,120)
Exchange differences	–	137	137	93
Closing net book amount	–	8,377	8,377	3,670
At 31 December 2005				
Cost	–	16,024	16,024	9,610
Accumulated amortisation and impairment	–	(7,647)	(7,647)	(5,940)
Net book amount	–	8,377	8,377	3,670
Year ended 31 December 2006				
Opening net book amount	–	8,377	8,377	3,670
Additions	398	4,932	5,330	4,932
Disposals	–	–	–	–
Amortisation charge	–	(4,257)	(4,257)	(2,534)
Exchange differences	20	355	375	219
Closing net book amount	418	9,407	9,825	6,287
At 31 December 2006				
Cost	418	21,745	22,163	15,075
Accumulated amortisation and impairment	–	(12,338)	(12,338)	(8,788)
Net book amount	418	9,407	9,825	6,287
Year ended 31 December 2007				
Opening net book amount	418	9,407	9,825	6,287
Additions	3	709	712	709
Disposals	–	–	–	–
Amortisation charge	–	(5,780)	(5,780)	(4,848)
Exchange differences	32	544	576	496
Closing net book amount	453	4,880	5,333	2,644
At 31 December 2007				
Cost	453	18,594	19,047	11,422
Accumulated amortisation and impairment	–	(13,714)	(13,714)	(8,778)
Net book amount	453	4,880	5,333	2,644

The amortisation of computer software has been expensed in administrative expenses.

7. INVESTMENTS IN SUBSIDIARIES – TARGET COMPANY

	As at 31 December		
	2005	2006	2007
	HK\$'000	HK\$'000	HK\$'000
Investments – unlisted shares, at cost	5,827	13,775	9,487
Impairment provision	(1,019)	(1,060)	(1,140)
	<u>4,808</u>	<u>12,715</u>	<u>8,347</u>

(a) The following is a list of all subsidiaries as at 31 December 2005.

Name	Date of incorporation/establishment	Place of incorporation/establishment and kind of legal entity	Principal activities and place of operation	Particulars of issued share capital/registered and paid-in capital	Interest held
<i>Directly held:</i>					
CIDC (H.K.) Limited	31 July 1984	Hong Kong, limited liability company	Hong Kong, sale of digital video and related technology	Issued and fully paid share capital of HK\$1,000,000	100%
Beijing Huada Infosec Technology Co., Ltd.	23 May 2000	PRC, limited liability company	PRC, development and sale of digital system software and hardware	Registered and paid-in capital of RMB17,000,000	70%

(b) The following is a list of all subsidiaries as at 31 December 2006.

Name	Date of incorporation/establishment	Place of incorporation/establishment and kind of legal entity	Principal activities and place of operation	Particulars of issued share capital/registered and paid-in capital	Interest held
<i>Directly held:</i>					
CIDC (H.K.) Limited	31 July 1984	Hong Kong, limited liability company	Hong Kong, sale of digital video and related technology	Issued and fully paid share capital of HK\$1,000,000	100%
Beijing Huada Infosec Technology Co., Ltd.	23 May 2000	PRC, limited liability company	PRC, development and sale of digital system software and hardware	Registered and paid-in capital of RMB17,000,000	70%
Guangdong Huada Electronic Design Co., Ltd.	27 August 2003	PRC, limited liability company	PRC, design and sale of integrated circuit	Registered and paid-in capital of RMB8,000,000	99.38%

(c) The following is a list of all subsidiaries as at 31 December 2007.

Name	Date of incorporation/ establishment	Place of incorporation/ establishment and kind of legal entity	Principal activities and place of operation	Particulars of issued share capital/ registered and paid-in capital	Interest held
<i>Directly held:</i>					
CIDC (H.K.) Limited	31 July 1984	Hong Kong, limited liability company	Hong Kong, sale of digital video and related technology	Issued and fully paid share capital of HK\$1,000,000	100%
Beijing Huada Infosec Technology Co., Ltd.	23 May 2000	PRC, limited liability company	PRC, development and sale of digital system software and hardware	Registered and paid-in capital of RMB16,700,000	71.26%
Guangdong Huada Electronic Design Co., Ltd.	27 August 2003	PRC, limited liability company	PRC, design and sale of integrated circuit	Registered and paid-in capital of RMB3,000,000	100%

Pursuant to a shareholders' resolution on 25 December 2007, the Target Company decided to deregister CIDC (H.K.) Limited. As at 31 December 2007, the deregistration process has not been completed yet.

(d) Acquisition

Acquisition of Beijing Huada Infosec Technology Co., Ltd.:

During the year ended 31 December 2005, the Target Company acquired 70% of interests in Beijing Huada Infosec Technology Co., Ltd.. The carrying amounts of the assets and liabilities acquired approximated their fair value, details are as follows:

	Carrying amount HK\$'000
Cash and cash equivalents	1,215
Property, plant and equipment	163
Intangible assets	6,293
Trade and other payables	(788)
Net assets	6,883
Minority interests in equity (30%)	(2,065)
Net assets acquired	4,818
Purchase consideration settled in cash	4,818
Cash and cash equivalents in subsidiary acquired	(1,215)
Cash outflow on acquisition	3,603

Acquisition of Guangdong Huada Electronic Design Co., Ltd.:

During the year ended 31 December 2006, the Target Company acquired additional 61.88% interest in Guangdong Huada Electronic Design Co., Ltd.. After the acquisition, the Target Company held totalling 99.38% interest. The carrying amounts of the assets and liabilities acquired approximated their fair value, details are as follows:

	Carrying amount HK\$'000
Cash and cash equivalents	6,966
Property, plant and equipment	138
Inventories	371
Trade and other receivables	4,383
Trade and other payables	(5,116)
Net assets	6,742
Minority interests in equity (0.62%)	(42)
Goodwill	402
Net assets held	7,102
Equity interest held	(2,569)
Net assets acquired	4,533
Purchase consideration settled in cash	4,533
Cash and cash equivalents in subsidiary acquired	(6,966)
Cash inflow on acquisition	(2,433)

8. INVESTMENT IN AN ASSOCIATE

	Target Group			Target Company		
	As at 31 December			As at 31 December		
	2005	2006	2007	2005	2006	2007
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Unlisted shares, at cost	–	–	–	2,885	–	–
Share of net assets	2,504	–	–	–	–	–
	2,504	–	–	2,885	–	–

The Target Group's share of the results of its associate, which is unlisted, and its aggregated assets (including goodwill) and liabilities, are as follows:

Name	Particulars of registered capital	Place of establishment	Assets <i>HK\$'000</i>	Liabilities <i>HK\$'000</i>	Revenues <i>HK\$'000</i>	Loss <i>HK\$'000</i>	Interest held
2005							
Guangdong Huada Electronic Design Co., Ltd.	Registered capital of RMB8,000,000	PRC	12,176	5,500	8,237	(198)	37.50%

9. AVAILABLE-FOR-SALE FINANCIAL ASSETS

Available-for-sale financial assets are equity interest held by the Target Group in Beijing Huada Zhibao Electronic System Co., Ltd. and Beijing Huada Test Co., Ltd, with equity interest of 5% and 10%, respectively. These companies are unlisted.

10. INVENTORIES**Target Group**

	As at 31 December		
	2005	2006	2007
	HK\$'000	HK\$'000	HK\$'000
Finished goods	13,341	64,266	125,901
Goods in transit	1,211	136	146
Work in progress	13,472	116,590	32,012
	<u>28,024</u>	<u>180,992</u>	<u>158,059</u>

Target Company

	As at 31 December		
	2005	2006	2007
	HK\$'000	HK\$'000	HK\$'000
Finished goods	12,348	63,727	124,929
Goods in transit	1,211	136	146
Work in progress	13,472	116,590	32,012
	<u>27,031</u>	<u>180,453</u>	<u>157,087</u>

The cost of inventories included in cost of sales amounted to HK\$196,882,000, HK\$316,712,000 and HK\$382,729,000 for the years ended 31 December 2005, 2006 and 2007, respectively.

For the year ended 31 December 2005 and 2006, the Target Group did not provide any provision for net realisable value of inventory. Write down of inventories to net realisable value of HK\$2,269,000 was included in cost of sales for the year ended 31 December 2007.

11. TRADE AND OTHER RECEIVABLES

	Target Group			Target Company		
	As at 31 December			As at 31 December		
	2005	2006	2007	2005	2006	2007
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Trade receivables (<i>Note (a)</i>)	174,108	272,020	226,588	180,197	275,806	216,772
Less: provision for impairment	(2,196)	(2,895)	(1,710)	(5,881)	(6,593)	(1,237)
Trade receivables – net	171,912	269,125	224,878	174,316	269,213	215,535
Other receivables from related parties	96	–	–	96	–	–
Prepayments and deposits	2	427	330	–	–	199
Other receivables	1,152	708	2,359	2,142	2,218	4,041
	<u>173,162</u>	<u>270,260</u>	<u>227,567</u>	<u>176,554</u>	<u>271,431</u>	<u>219,775</u>

The directors of the Target Company are of the opinion that the carrying amounts of trade and other receivables (excluding prepayments) approximate their fair values. All trade and other receivables are due within 1 year and non interest-bearing.

Trade and other receivables from related parties of HK\$32,762,000, HK\$29,458,000 and HK\$37,346,000 were included in the above balances as at 31 December 2005, 2006 and 2007, respectively (Notes 28(a) and (b)).

The Target Group's trade and other receivables are all denominated in Renminbi.

- (a) The majority of the Target Group's sales are with credit term of 30 to 135 days, the remaining sales are due immediately after the delivery of goods. The ageing analysis of the Target Group and the Target Company's gross trade receivables was as follows:

Ageing	Target Group			Target Company		
	As at 31 December			As at 31 December		
	2005 HK\$'000	2006 HK\$'000	2007 HK\$'000	2005 HK\$'000	2006 HK\$'000	2007 HK\$'000
Current to 30 days	96,416	54,821	138,817	95,012	54,469	137,120
31 – 60 days	55,711	83,863	10,397	55,711	82,563	10,797
Over 60 days and within 1 year	18,743	129,791	74,375	18,743	127,277	67,508
Over 1 year	3,238	3,545	2,999	10,731	11,497	1,347
	<u>174,108</u>	<u>272,020</u>	<u>226,588</u>	<u>180,197</u>	<u>275,806</u>	<u>216,772</u>

- (b) The maximum exposure to credit risk at 31 December 2005, 2006 and 2007 is the fair value of the trade and other receivables (excluding prepayments) mentioned above. The Target Group does not hold any collateral as security.

Trade receivables of HK\$2,196,000, HK\$2,895,000 and HK\$1,710,000 of the Target Group were impaired and fully provided as at 31 December 2005, 2006 and 2007 respectively.

Trade receivables of HK\$5,881,000, HK\$6,593,000 and HK\$1,237,000 of the Target Company were impaired and fully provided as at 31 December 2005, 2006 and 2007 respectively.

Movement on the provision for impairment of the Target Group and Target Company's trade receivables are as follows:

	Target Group			Target Company		
	As at 31 December			As at 31 December		
	2005 HK\$'000	2006 HK\$'000	2007 HK\$'000	2005 HK\$'000	2006 HK\$'000	2007 HK\$'000
At 1 January	1,325	2,196	2,895	4,972	5,881	6,593
Provision for impairment	837	594	1,032	800	463	336
Written off	–	–	(2,468)	–	–	(6,200)
Exchange difference	34	105	251	109	249	508
At 31 December	<u>2,196</u>	<u>2,895</u>	<u>1,710</u>	<u>5,881</u>	<u>6,593</u>	<u>1,237</u>

The trade receivables past due but not impaired were HK\$16,467,000, HK\$24,012,000 and HK\$19,958,000 of the Target Group at 31 December 2005, 2006 and 2007 respectively.

The trade receivables past due but not impaired were HK\$14,891,000, HK\$20,506,000 and HK\$7,894,000 of the Target Company at 31 December 2005, 2006 and 2007 respectively.

Ageing

	Target Group			Target Company		
	As at 31 December			As at 31 December		
	2005 HK\$'000	2006 HK\$'000	2007 HK\$'000	2005 HK\$'000	2006 HK\$'000	2007 HK\$'000
31 – 60 days	3,750	4,076	1,934	3,731	3,810	259
Over 60 days and within 1 year	11,674	19,241	16,717	10,290	16,020	7,507
Over 1 year	1,043	695	1,307	870	676	128
	<u>16,467</u>	<u>24,012</u>	<u>19,958</u>	<u>14,891</u>	<u>20,506</u>	<u>7,894</u>

12. CASH AND CASH EQUIVALENTS

	Target Group			Target Company		
	As at 31 December			As at 31 December		
	2005 HK\$'000	2006 HK\$'000	2007 HK\$'000	2005 HK\$'000	2006 HK\$'000	2007 HK\$'000
Cash at bank and on hand						
China Electronics Corporation Finance Co., Ltd. (Note 28(a))	140	2,736	–	140	2,736	–
New Times Securities Co., Ltd.	–	–	36,766	–	–	36,766
Other banks and cash in hand	<u>23,376</u>	<u>85,216</u>	<u>121,112</u>	<u>19,322</u>	<u>73,938</u>	<u>116,009</u>
	<u>23,516</u>	<u>87,952</u>	<u>157,878</u>	<u>19,462</u>	<u>76,674</u>	<u>152,775</u>
Short-term deposits						
China Electronics Corporation Finance Co., Ltd. (Note 28(a))	–	–	30,268	–	–	30,268
Other banks and financial institutions	<u>1,250</u>	<u>–</u>	<u>756</u>	<u>–</u>	<u>–</u>	<u>756</u>
	<u>1,250</u>	<u>–</u>	<u>31,024</u>	<u>–</u>	<u>–</u>	<u>31,024</u>
	<u>24,766</u>	<u>87,952</u>	<u>188,902</u>	<u>19,462</u>	<u>76,674</u>	<u>183,799</u>
Currency	Target Group			Target Company		
	As at 31 December			As at 31 December		
	2005 '000	2006 '000	2007 '000	2005 '000	2006 '000	2007 '000
Renminbi	20,427	82,475	176,650	19,044	76,635	170,904
HK dollar	3,975	5,413	–	–	–	–
US dollar	148	5	2	148	5	2

China Electronics Corporation Finance Co., Ltd. is a non-bank financial institution approved by the People's Bank of China. The deposits yielded interest at prevailing saving deposit rates ranged from 0.72% to 2.25% during the Relevant Periods.

New Times Securities Co., Ltd. is a securities company approved by China Securities Regulatory Commission. The deposits yielded interest at prevailing saving deposit rates.

The annual interest rate of deposits with banks and financial institutions other than China Electronics Corporation Finance Co., Ltd. ranged from 0.72% to 1.71% during the Relevant Periods.

13. REGISTERED AND PAID-IN CAPITAL

	Registered and paid-in capital HK\$'000
At 1 January 2005	30,154
Capital injection from shareholders	2,488
At 31 December 2005, 2006 and 2007	32,642

Pursuant to a resolution of the shareholders' meeting held on 6 September 2005, the shareholders approved the capital injection from Beijing Shoufa Xinan Data System Technology Company Limited of RMB5,000,000. Out of the total amount, RMB2,594,600 was recorded as increase of registered and paid-in capital and the remaining balance of RMB2,405,400 was recorded in the capital reserve.

14. RESERVES

Target Group

	Capital reserve HK\$'000 (Note (a))	Statutory surplus reserves HK\$'000 (Note (b))	Currency translation reserve HK\$'000	Total HK\$'000
At 1 January 2005	441	1,538	17	1,996
Capital injection from shareholders	2,350	–	–	2,350
Appropriation from retained earnings	–	5,824	–	5,824
Currency translation differences	–	–	1,240	1,240
At 31 December 2005	2,791	7,362	1,257	11,410
At 1 January 2006	2,791	7,362	1,257	11,410
Appropriation from retained earnings	–	7,790	–	7,790
Currency translation differences	–	–	6,768	6,768
At 31 December 2006	2,791	15,152	8,025	25,968
At 1 January 2007	2,791	15,152	8,025	25,968
Appropriation from retained earnings	–	4,280	–	4,280
Currency translation differences	–	–	17,777	17,777
At 31 December 2007	2,791	19,432	25,802	48,025

Target Company

	Capital reserve HK\$'000 (Note (a))	Statutory surplus reserves HK\$'000 (Note (b))	Currency translation reserve HK\$'000	Total HK\$'000
At 1 January 2005	441	1,538	30	2,009
Capital injection from shareholders	2,294	–	–	2,294
Appropriation from retained earnings	–	5,824	–	5,824
Currency translation differences	–	–	1,206	1,206
At 31 December 2005	<u>2,735</u>	<u>7,362</u>	<u>1,236</u>	<u>11,333</u>
At 1 January 2006	2,735	7,362	1,236	11,333
Appropriation from retained earnings	–	7,790	–	7,790
Currency translation differences	–	–	6,769	6,769
At 31 December 2006	<u>2,735</u>	<u>15,152</u>	<u>8,005</u>	<u>25,892</u>
At 1 January 2007	2,735	15,152	8,005	25,892
Appropriation from retained earnings	–	4,280	–	4,280
Currency translation differences	–	–	17,999	17,999
At 31 December 2007	<u>2,735</u>	<u>19,432</u>	<u>26,004</u>	<u>48,171</u>

(a) Capital reserve

Capital reserve represents premium paid on capital contributed by shareholders.

(b) Statutory surplus reserves

The Target Company and its subsidiaries are required to appropriate at least 10% of its profit after tax as reported in their PRC statutory accounts to the statutory surplus reserve fund until the cumulative amounts reach 50% of the registered capital. The statutory reserve can only be used, upon approval obtained from the relevant authority, to offset accumulated losses or increase capital.

According to the relevant resolution of shareholders' meetings, the Target Company appropriated statutory surplus reserve from its profit after tax of approximately HK\$5,824,000, HK\$7,790,000 and HK\$4,280,000 during the year ended 31 December 2005, 2006 and 2007, respectively. As of 31 December 2007, the statutory surplus reserves balances of the Target Company has already reached 50% of the registered capital.

15. TRADE AND OTHER PAYABLES

	Target Group			Target Company		
	As at 31 December			As at 31 December		
	2005 HK\$'000	2006 HK\$'000	2007 HK\$'000	2005 HK\$'000	2006 HK\$'000	2007 HK\$'000
Notes payables	21,677	202,477	30,074	21,677	202,477	30,074
Trade payables	56,794	92,575	112,794	56,794	90,889	102,259
Advance from customers	1,257	1,823	2,069	1,257	3,169	2,069
Salary and welfare payable	11,988	15,860	34,769	11,136	14,686	33,764
Other taxes payable	7,715	832	17,113	7,699	925	17,252
Other levies payable	202	956	1,745	203	956	1,742
Other payables	22,894	17,748	16,173	22,624	17,610	15,982
Government grants	5,138	2,951	24,875	4,656	1,848	24,875
Accrued expenses	–	943	210	–	943	210
	<u>127,665</u>	<u>336,165</u>	<u>239,822</u>	<u>126,046</u>	<u>333,503</u>	<u>228,227</u>

Notes payable represents non interest bearing commercial paper issued to suppliers with maturity period within 6 months.

Trade and other payables to related parties amounted to HK\$67,256,000, HK\$84,283,000 and HK\$101,826,000 were included in the above balance as at 31 December 2005, 2006 and 2007, respectively (Note 28(a)).

Trade payables dominated in US dollar amounted to HK\$39,000, HK\$65,000 and nil were included in the above balance as at 31 December 2005, 2006 and 2007 respectively.

The carrying amount of notes payables and trade payables approximate their fair values.

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

	As at 31 December		
	2005 HK\$'000	2006 HK\$'000	2007 HK\$'000
Current to 30 days	22,067	43,597	16,266
31 – 60 days	30,284	30,109	21,073
Over 60 days	4,443	18,869	75,455
	<u>56,794</u>	<u>92,575</u>	<u>112,794</u>

16. SHORT TERM BANK LOANS

The bank loans as at 31 December 2005 were guaranteed by China Huada Integrated Circuit Design (Group) Co., Ltd. and repayable within one year. The bank loans as at 31 December 2006 and 2007 were dominated in Renminbi, unsecured and repayable within one year. The weighted average effective borrowing rate are 6.14%, 6.12% and 7.29% per annum as at 31 December in 2005, 2006 and 2007, respectively.

The carrying amounts of the short term bank loans approximate their fair value.

The Target Group has unutilised loan facilities of approximately HK\$9,615,000, HK\$20,000,000 as at 31 December 2005 and 2006 respectively. The Target Group has fully utilised the loan facilities as at 31 December 2007.

17. EXPENSES BY NATURE

Expenses included in cost of sales, selling and marketing costs and administrative expenses are analysed as follows:

	Year ended 31 December		
	2005	2006	2007
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Depreciation and amortisation expenses (Notes 5 and 6)	6,213	6,123	8,441
Employee benefit expenses (Note 18)	29,725	44,689	76,518
Changes in inventories	31,546	(152,968)	20,592
Purchase of finished goods	165,336	469,680	362,137
Royalty fee for intellectual patent	18,941	10,842	14,879
Write down of inventories	–	–	2,269
Impairment provision for receivables	837	594	1,032
Operating lease expenses on property	2,152	2,309	3,716
Research and development costs	10,694	14,143	26,374
Others	8,904	3,857	11,752
	<u>274,348</u>	<u>399,269</u>	<u>527,710</u>

18. EMPLOYEE BENEFIT EXPENSES

	Year ended 31 December		
	2005	2006	2007
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Basic salaries, allowances and benefits in kind	28,819	43,342	74,602
Contributions to retirement schemes	906	1,347	1,916
	<u>29,725</u>	<u>44,689</u>	<u>76,518</u>

19. OTHER GAINS – NET

	Year ended 31 December		
	2005	2006	2007
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Government grants	22,469	18,956	7,535
Other income	32	1,075	996
Other losses	(185)	(131)	(74)
	<u>22,316</u>	<u>19,900</u>	<u>8,457</u>

20. DIRECTORS', SUPERVISORS' AND SENIOR MANAGEMENT'S EMOLUMENTS

(a) Directors' and supervisors' emoluments

The remuneration of every Director and supervisor for the year ended 31 December 2005 is set out below:

Name of Director and supervisor	Fees <i>HK\$'000</i>	Salaries, allowance and benefits in kind <i>HK\$'000</i>	Total <i>HK\$'000</i>
Ms. Wang Qinsheng	—	457	457
Mr. Liu Weiping	—	821	821
Mr. Ji Xiaozhong*	—	—	—
Mr. Tao Quanyou*	—	—	—
Mr. Huang Guoyong	—	249	249
Mr. Liu Huamao	—	338	338
Mr. Fan Qingwu*	—	—	—
Mr. Zhuang Qinghai*	—	—	—
Mr. Hou Jinsong	—	325	325
	<u>—</u>	<u>325</u>	<u>325</u>
	<u>—</u>	<u>2,190</u>	<u>2,190</u>

The remuneration of every Director and supervisor for the year ended 31 December 2006 is set out below:

Name of Director and supervisor	Fees <i>HK\$'000</i>	Salaries, allowance and benefits in kind <i>HK\$'000</i>	Total <i>HK\$'000</i>
Mr. Lu Ming*	—	—	—
Mr. Liu Jinping*	—	—	—
Mr. Liu Weiping	—	1,660	1,660
Mr. Ji Xiaozhong*	—	—	—
Ms. Wang Qinsheng	—	78	78
Mr. Sun Xiaonian*	—	—	—
Mr. Cheng Shuguang*	—	—	—
Mr. Zhang Wenxiong*	—	—	—
Mr. Hou Jinsong	—	347	347
	<u>—</u>	<u>347</u>	<u>347</u>
	<u>—</u>	<u>2,085</u>	<u>2,085</u>

The remuneration of every Director and supervisor for the year ended 31 December 2007 is set out below:

Name of Director and supervisor	Fees HK\$'000	Salaries, allowance and benefits in kind HK\$'000	Total HK\$'000
Mr. Lu Ming*	–	–	–
Mr. Liu Jinping*	–	–	–
Mr. Liu Weiping	–	1,583	1,583
Mr. Ji Xiaozhong*	–	–	–
Ms. Wang Qinsheng	–	125	125
Mr. Sun Xiaonian*	–	–	–
Mr. Cheng Shuguang*	–	–	–
Mr. Zhang Wenxiong*	–	–	–
Mr. Hou Jinsong	–	361	361
	–	2,069	2,069

* These directors and supervisors are employees of certain subsidiaries of CEC Group and receive emoluments from these subsidiaries. No appropriation has been made as the directors and supervisors of the Target Company considered it is impracticable to apportion this amount between their services to the Target Group and certain subsidiaries of CEC Group.

During the Relevant Periods, no director or supervisor had waived or agreed to waive any emolument. No director or supervisor received any compensation for loss of office during the Relevant Periods.

(b) Five highest paid individuals

The five individuals whose emoluments were the highest in the Target Group for the year include one director whose emoluments are reflected in the analysis presented above. The emoluments payable to the remaining four individuals during the Relevant Periods are as follows:

	Year ended 31 December		
	2005 HK\$'000	2006 HK\$'000	2007 HK\$'000
Basic salaries, allowances and benefits in kind	1,595	4,945	4,048
Bonuses	14	358	1,199
	1,609	5,303	5,247

The emoluments fell within the following band:

	Number of individuals		
	2005	2006	2007
HK\$nil – HK\$1,000,000	4	–	1
HK\$1,000,001 – HK\$1,500,000	–	2	2
HK\$1,500,001 – HK\$2,000,000	–	2	1
	4	4	4

21. FINANCE COSTS – NET

	Year ended 31 December		
	2005	2006	2007
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Interest income on short-term deposits	(498)	(992)	(1,144)
Interest on bank loans	2,174	1,624	2,595
	<u> </u>	<u> </u>	<u> </u>
Net financial costs	1,676	632	1,451
	<u> </u>	<u> </u>	<u> </u>

22. TAXATION**(a) Income tax expense**

The amount of taxation charged to the consolidated income statement represents:

	Year ended 31 December		
	2005	2006	2007
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Current taxation – PRC enterprise income tax	3,017	8,847	11,996
Deferred taxation	(611)	(96)	(6,895)
Currency translation difference	(23)	(61)	(345)
	<u> </u>	<u> </u>	<u> </u>
	2,383	8,690	4,756
	<u> </u>	<u> </u>	<u> </u>

- (b) The Target Company was certified as a high/new technology enterprise established in Beijing New Technology Industry Development Zone in the PRC. Therefore, the applicable income tax rate is 15%. As approved by the tax authorities in 2003, the Target Company was exempted from income tax for the year ended 31 December 2003 and 2004, followed by a 50% deduction for the years ended 31 December 2005, 2006 and 2007.

CIDC (H.K.) Limited assessed its profit tax liability in Hong Kong using a tax rate of 17.5%. During the years ended 31 December 2005, 2006 and 2007, CIDC (H.K.) Limited did not have any assessable profits sourced from Hong Kong.

Beijing Huada Infosec Technology Co., Ltd. and Guangdong Huada Electronic Design Co., Ltd. were registered in the PRC and were subject to 33% statutory income tax rate in the years ended 31 December 2005, 2006 and 2007.

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

	Year ended 31 December		
	2005 HK\$'000	2006 HK\$'000	2007 HK\$'000
Profit before income tax	41,816	128,716	132,063
Calculated at a taxation rate of 33%	13,799	42,476	43,581
Effect of tax concession	(9,607)	(30,090)	(32,655)
Expenses not deductible for taxation purposes	235	562	1,110
Tax losses for which no deferred income tax asset was recognised	1,010	184	275
Research and development costs super deduction	(3,054)	(4,442)	(7,555)
Income tax expense	<u>2,383</u>	<u>8,690</u>	<u>4,756</u>

(d) **Deferred income tax**

The movement on the deferred tax assets during the years ended 31 December 2005, 2006 and 2007 are as follows:

	Impairment provision for receivables HK\$'000	Salary payable HK\$'000	Government grants HK\$'000	Impairment of inventories HK\$'000	Revenue recognition HK\$'000	Total HK\$'000
At 1 January 2005	91	445	298	–	–	834
Credited to the income statement	188	378	45	–	–	611
Currency translation difference	<u>4</u>	<u>12</u>	<u>7</u>	<u>–</u>	<u>–</u>	<u>23</u>
At 31 December 2005	<u>283</u>	<u>835</u>	<u>350</u>	<u>–</u>	<u>–</u>	<u>1,468</u>
At 1 January 2006	283	835	350	–	–	1,468
Credited/(Charged) to the income statement	88	226	(218)	–	–	96
Currency translation difference	<u>14</u>	<u>40</u>	<u>7</u>	<u>–</u>	<u>–</u>	<u>61</u>
At 31 December 2006	<u>385</u>	<u>1,101</u>	<u>139</u>	<u>–</u>	<u>–</u>	<u>1,625</u>
At 1 January 2007	385	1,101	139	–	–	1,625
(Charged)/credited to the income statement	(229)	7,030	5,880	567	(6,353)	6,895
Currency translation difference	<u>22</u>	<u>310</u>	<u>200</u>	<u>18</u>	<u>(205)</u>	<u>345</u>
At 31 December 2007	<u>178</u>	<u>8,441</u>	<u>6,219</u>	<u>585</u>	<u>(6,558)</u>	<u>8,865</u>

The amounts shown in the balance sheet include the following:

	As at 31 December		
	2005 <i>HK\$'000</i>	2006 <i>HK\$'000</i>	2007 <i>HK\$'000</i>
Deferred tax assets to be recovered after more than 12 months	–	–	–
Deferred tax assets to be recovered within 12 months	1,468	1,625	8,865

Deferred income tax assets are recognised for tax loss carrying-forwards to the extent that the realisation of the related tax benefit through the future taxable profits is probable. The Target Group did not recognise deferred income tax assets of HK\$1,010,000, HK\$1,194,000 and HK\$1,402,000 at 31 December 2005, 2006 and 2007 respectively, in respect of losses amounting HK\$3,061,000, HK\$3,619,000 and HK\$4,452,000, that can be carried forward against future taxable income. Losses amounting to HK\$3,061,000, HK\$558,000 and HK\$833,000 will expire in 2010, 2011 and 2012 respectively.

On 16 March 2007, the Corporate Income Tax Law of the PRC (the “new CIT Law”) was approved and became effective 1 January 2008. Accordingly, the Target Company’s applicable tax rate will be 25% from January 2008. In this regard, the new applicable tax rates are adopted in computing the deferred taxation as at 31 December 2007. The change of tax rates resulted a tax credit of approximately HK\$4,106,000 for the year ended 31 December 2007.

23. PROFIT ATTRIBUTABLE TO EQUITY HOLDERS OF THE TARGET COMPANY

The profit attributable to equity holders of the Target Company is dealt within the financial statements of the Target Company to the extent of HK\$44,070,000, HK\$121,590,000, HK\$129,323,000 for the years ended 31 December 2005, 2006 and 2007, respectively.

24. DIVIDENDS

Final dividend related to year 2005 of the Target Company totalling approximately HK\$13,435,000 (RMB13,838,000) was declared and paid in March 2006.

Final dividend related to year 2006 of the Target Company totalling approximately HK\$45,045,000 (RMB43,243,000) was declared and paid in March 2007.

At the shareholders’ meeting held on 19 March 2008, the shareholders of the Target Company approved the payment of a final dividend for the year ended 31 December 2007 of approximately HK\$74,397,000 (equivalent to RMB69,189,000). Furthermore, at the shareholders’ meeting held on 16 June 2008, the shareholders of the Target Company approved an additional payment of final dividend for the year ended 31 December 2007 of approximately HK\$74,397,000 (equivalent to RMB69,189,000). Totalling HK\$148,794,000 (equivalent to RMB138,378,000) final dividends for the year ended 31 December 2007 will be reflected as an appropriation of retained earnings during the year ended 31 December 2008.

25. CASH GENERATED FROM OPERATIONS

	2005 <i>HK\$'000</i>	2006 <i>HK\$'000</i>	2007 <i>HK\$'000</i>
Profit before income tax	41,816	128,716	132,063
Adjustment for:			
Depreciation	2,403	1,866	2,661
Amortisation of intangible assets	3,810	4,257	5,780
Loss on disposal of property, plant and equipment	–	121	50
Interest income	(498)	(992)	(1,144)
Interest expense	2,174	1,624	2,595
Dividend received	–	–	(376)
Changes in working capital			
Decrease/(increase) of Inventories	32,437	(147,051)	35,415
(Increase)/decrease of trade and other receivables	(80,349)	(83,120)	61,064
(Decrease)/increase of trade and other payables	(22,674)	192,649	(116,721)
Net cash (used in)/generated from operations	<u>(20,881)</u>	<u>98,070</u>	<u>121,387</u>

(a) Proceeds from disposal of property, plant and equipment include:

	2005 <i>HK\$'000</i>	2006 <i>HK\$'000</i>	2007 <i>HK\$'000</i>
Net book value (<i>Note 5</i>)	–	121	131
Loss on disposal of property, plant and equipment	<u>–</u>	<u>(121)</u>	<u>(50)</u>
Cash proceeds from disposal of property, plant and equipment	<u>–</u>	<u>–</u>	<u>81</u>

26. COMMITMENTS**(a) Capital lease commitments**

As at 31 December 2005, 2006 and 2007, the Target Group did not have any capital commitments.

(b) Operating lease commitments

As at 31 December 2005, 2006 and 2007, the Target Group had future aggregate minimum lease payments under non-cancellable operating leases for office premises as follows:

	Target Group			Target Company		
	As at 31 December			As at 31 December		
	2005 <i>HK\$'000</i>	2006 <i>HK\$'000</i>	2007 <i>HK\$'000</i>	2005 <i>HK\$'000</i>	2006 <i>HK\$'000</i>	2007 <i>HK\$'000</i>
Not later than one year	1,899	2,913	1,879	1,899	2,760	1,599
In the second to fifth years	<u>2,171</u>	<u>664</u>	<u>430</u>	<u>2,171</u>	<u>664</u>	<u>–</u>
	<u>4,070</u>	<u>3,577</u>	<u>2,309</u>	<u>4,070</u>	<u>3,424</u>	<u>1,599</u>

27. CONTINGENT LIABILITIES

The Target Group did not have any material outstanding contingent liabilities as at 31 December 2005, 2006 and 2007.

28. RELATED-PARTY TRANSACTIONS AND BALANCES

Parties are considered to be related if one company has the ability, directly or indirectly, to control the other company or exercise significant influence over the other party in making financial and operating decisions. Parties are also considered to be related if they are subject to common control or common significant influence.

(a) Transaction and balances with CEC and its subsidiaries*(1) Sales of integrated circuit products:*

	Year ended 31 December		
	2005 HK\$'000	2006 HK\$'000	2007 HK\$'000
Beijing Huada Zhibao Electronic System Co., Ltd.	27,880	30,706	26,338
Shanghai Hsic Application System Co., Ltd.	4,733	11,033	22,311
Beijing Hengtai Technologies Co., Ltd.	88	–	191

(2) Purchases of goods and services:

	Year ended 31 December		
	2005 HK\$'000	2006 HK\$'000	2007 HK\$'000
Shanghai Hua Hong NEC Electronics Co., Ltd.	155,379	393,258	262,623
China Electronics Smart Card Co., Ltd.	41,289	83,338	92,006
Beijing Huada Test Co., Ltd.	16,155	24,229	36,202

(3) Other transactions:

	Year ended 31 December		
	2005 HK\$'000	2006 HK\$'000	2007 HK\$'000
Receipt of interests:			
China Electronics Corporation Finance Co., Ltd.	127	50	181
China Huada Integrated Circuit Design (Group) Co., Ltd.	–	20	50
Payment of interests:			
China Electronics Corporation Finance Co., Ltd.	85	51	–
Rental expenses:			
Beijing Huada Zhibao Electronic System Co., Ltd.	1,644	1,631	2,099
Canteen services:			
Beijing Huada Zhibao Electronic System Co., Ltd.	470	446	624

(4) Year-end balance arising from sales, purchases and other transactions:

	As at 31 December		
	2005 HK\$'000	2006 HK\$'000	2007 HK\$'000
Trade receivables due from related parties:			
Beijing Huada Zhibao Electronic System Co., Ltd.	25,645	22,024	13,946
Shanghai Hsic Application System Co., Ltd.	4,402	7,434	23,400
	<u>30,047</u>	<u>29,458</u>	<u>37,346</u>
Trade payables due to related parties:			
Shanghai Hua Hong NEC Electronics Co., Ltd.	23,496	37,964	74,260
China Electronics Smart Card Co., Ltd.	15,837	32,323	16,384
Beijing Huada Test Co., Ltd	7,982	6,969	7,764
Beijing Huada Zhibao Electronic System Co., Ltd.	67	178	192
	<u>47,382</u>	<u>77,434</u>	<u>98,600</u>
Other payables due to related parties:			
China Huada Integrated Circuit Design (Group) Co., Ltd.	16,989	3,849	–
China Electronics Corporation	2,885	3,000	3,226
	<u>19,874</u>	<u>6,849</u>	<u>3,226</u>
Trade and other payables due to related parties in total:	<u>67,256</u>	<u>84,283</u>	<u>101,826</u>
Deposits:			
China Electronics Corporation Finance Co., Ltd.	140	2,736	30,268

(b) Transaction and balance with an associate – Guangdong Huada Electronic Design Co., Ltd.

(1) Sales of integrated circuit products:

	Year ended 31 December		
	2005 HK\$'000	2006 HK\$'000	2007 HK\$'000
Sales of products	<u>5,073</u>	<u>–</u>	<u>–</u>

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

	As at 31 December		
	2005 HK\$'000	2006 HK\$'000	2007 HK\$'000
Trade receivables	2,619	–	–
Other receivables	<u>96</u>	<u>–</u>	<u>–</u>
Trade and other receivables in total	<u>2,715</u>	<u>–</u>	<u>–</u>

(c) Additional information on other state-owned enterprises

The Target Company is controlled by CEC and SDIC and is ultimately controlled by Mainland China government, which also controls a significant portion of the productive assets and entities in the Mainland China. In accordance with Hong Kong Accounting Standard 24 “Related Party Disclosures” (“HKAS 24”), state-owned enterprises and their subsidiaries, other than CEC, are also defined as related parties of the Target Company and its subsidiaries (“Other State-owned Enterprises”).

(i) Summary of significant transactions with Other State-owned Enterprises

	Year ended 31 December		
	2005 HK\$'000	2006 HK\$'000	2007 HK\$'000
Sales of products and materials	225,824	421,684	497,520
Purchases of materials	66	20,874	8,831

(ii) Summary of balances with Other State-owned Enterprises

	As at 31 December		
	2005 HK\$'000	2006 HK\$'000	2007 HK\$'000
Trade receivables	130,754	210,998	129,336
Trade payables	194	3,725	3
Bank deposits in state-owned banks	–	2,844	3,570

Balances with Other State-owned Enterprises, except for bank deposits, were unsecured and interest-free.

The majority of the business activities of the Target Company and its subsidiaries are conducted with state-owned enterprises. For the purpose of the related party transactions disclosure in accordance with HKAS 24, the Target Company and its subsidiaries have established procedures to determine, to the extent possible, the identification of the ownership structure of its customers and suppliers as to whether they are state-owned enterprises. However, many state-owned enterprises have a multi-layered corporate structure and the ownership structures change over time as a result of transfers and privatization programs. Nevertheless, management believes that all material related party balances and transactions have been adequately disclosed.

29. EVENTS AFTER THE BALANCE SHEET DATE**(1) Sale of Beijing Huada Infosec Technology Co., Ltd.**

At the shareholders' meeting held on 20 January 2008, the shareholders of the Target Company approved to sell 71.26% of its share in Beijing Huada Infosec Technology Co., Ltd. in 2008.

As at 21 May 2008, the Target Company entered into a share transfer agreement with 北京訊安達科技有限公司 Beijing Xu An Da Technology Co., Ltd. to sell its interest in Beijing Huada Infosec Technology Co., Ltd. for cash consideration of RMB5,000,000. As at 17 June 2008, 100% of the cash consideration was received by the Target Company.

(2) Sale of Guangdong Huada Electronic Design Co., Ltd.

At the shareholders' meeting held on 19 March 2008, the shareholders of the Target Company approved to sell 80% of its interest in Guangdong Huada Electronic Design Co., Ltd. in 2008.

The shares will be traded through the equity exchange authorised by the government as required by regulations. As at the report day, the Target Company has not entered into any share transfer agreement.

III. SUBSEQUENT FINANCIAL STATEMENTS

No audited financial statements have been prepared for the Target Company and its subsidiaries in respect of any period subsequent to 31 December 2007. In addition, except for the dividends as disclosed in Note 24 of section II above, no other dividends or distribution has been declared, made or paid by the Target Company or its subsidiaries in respect of any period subsequent to 31 December 2007.

Yours faithfully,
PricewaterhouseCoopers
Certificated Public Accountants
Hong Kong

1. SUMMARY OF FINANCIAL INFORMATION

The following consolidated balance sheets and consolidated income statements are extracted from the audited consolidated financial statements of the Group for each of the years ended 31 December 2005, 2006 and 2007.

Consolidated Balance Sheets

As at 31 December 2005, 2006 and 2007

(All amounts in HK dollars thousands unless otherwise stated)

	As at 31 December		
	2005	2006	2007
ASSETS			
Non-current assets			
Property, plant and equipment	79,051	61,685	41,047
Intangible assets	14,113	16,251	16,144
Deferred income tax assets	4,514	8,916	46,691
	<u>97,678</u>	<u>86,852</u>	<u>103,882</u>
Current assets			
Inventories	447,034	335,802	444,189
Trade and other receivables	1,084,944	493,179	877,150
Cash and cash equivalents	306,381	419,809	391,741
	<u>1,838,359</u>	<u>1,248,790</u>	<u>1,713,080</u>
Total assets	<u><u>1,936,037</u></u>	<u><u>1,335,642</u></u>	<u><u>1,816,962</u></u>
EQUITY			
Capital and reserves attributable to the Company's equity holders			
Issued equity	370,074	370,074	370,074
Other reserves	35,062	55,137	71,807
Retained earnings			
– Proposed final dividend	21,671	17,337	–
– Unappropriated retained earnings	3,209	21,815	29,889
	<u>430,016</u>	<u>464,363</u>	<u>471,770</u>
Minority interests in equity	<u>138,379</u>	<u>138,775</u>	<u>129,066</u>
Total equity	<u><u>568,395</u></u>	<u><u>603,138</u></u>	<u><u>600,836</u></u>

	As at 31 December		
	2005	2006	2007
LIABILITIES			
Current liabilities			
Trade and other payables	1,129,194	717,826	741,030
Current income tax liabilities	5,573	2,044	3,725
Short term bank loans	230,769	–	394,111
Provision for warranty	2,106	12,634	77,260
Total liabilities	<u>1,367,642</u>	<u>732,504</u>	<u>1,216,126</u>
Total equity and liabilities	<u>1,936,037</u>	<u>1,335,642</u>	<u>1,816,962</u>
Net current assets	<u>470,717</u>	<u>516,286</u>	<u>496,954</u>
Total assets less current liabilities	<u>568,395</u>	<u>603,138</u>	<u>600,836</u>

Consolidated Income Statements*For the year ended 31 December 2005, 2006 and 2007**(All amounts in HK dollars thousands unless otherwise stated)*

	Year ended 31 December		
	2005	2006	2007
Revenue	4,768,526	3,549,329	3,167,708
Cost of sales	<u>(4,537,491)</u>	<u>(3,317,032)</u>	<u>(2,608,047)</u>
Gross profit	231,035	232,297	559,661
Other gains – net	13,822	5,130	9,699
Selling and marketing costs	(41,706)	(42,457)	(259,104)
Administrative expenses	<u>(106,401)</u>	<u>(125,118)</u>	<u>(331,740)</u>
Operating profit/(loss)	96,750	69,852	(21,484)
Finance income	4,697	8,109	11,442
Finance costs	<u>(11,501)</u>	<u>(6,444)</u>	<u>(9,075)</u>
Finance (costs)/income – net	<u>(6,804)</u>	<u>1,665</u>	<u>2,367</u>
Profit/(loss) before income tax	89,946	71,517	(19,117)
Income tax (expense)/credit	<u>(5,598)</u>	<u>(2,358)</u>	<u>31,640</u>
Profit for the year	<u>84,348</u>	<u>69,159</u>	<u>12,523</u>
Attributable to:			
Equity holders of the Company	49,899	43,276	8,074
Minority interests	<u>34,449</u>	<u>25,883</u>	<u>4,449</u>
	<u>84,348</u>	<u>69,159</u>	<u>12,523</u>
Earnings per share for profit attributable to the equity holders of the Company during the year (expressed in HK cents per share)			
– basic	<u>4.61</u>	<u>3.99</u>	<u>0.75</u>
– diluted	<u>4.61</u>	<u>3.99</u>	<u>0.74</u>
Dividends	<u>21,671</u>	<u>17,337</u>	<u>–</u>

2. AUDITED CONSOLIDATED FINANCIAL STATEMENTS

The following are the audited consolidated balance sheet of the Group and the balance sheet of the Company as at 31 December 2007, the audited consolidated income statement of the Group for the year ended 31 December 2007, the audited consolidated statement of changes in equity and the audited consolidated cash flow statement of the Group for the year ended 31 December 2007, together with the accompanying notes as extracted from the annual report of the Company for the year ended 31 December 2007:

Consolidated Balance Sheet

As at 31 December 2007

(All amounts in HK dollars thousands unless otherwise stated)

		As at 31 December	
	<i>Note</i>	2007	2006
ASSETS			
Non-current assets			
Property, plant and equipment	6	41,047	61,685
Intangible assets	7	16,144	16,251
Deferred income tax assets	22(e)	46,691	8,916
		<u>103,882</u>	<u>86,852</u>
Current assets			
Inventories	9	444,189	335,802
Trade and other receivables	10	877,150	493,179
Cash and cash equivalents	11	391,741	419,809
		<u>1,713,080</u>	<u>1,248,790</u>
Total assets		<u><u>1,816,962</u></u>	<u><u>1,335,642</u></u>
EQUITY			
Capital and reserves attributable to the Company's equity holders			
Issued equity	12	370,074	370,074
Other reserves	13	71,807	55,137
Retained earnings			
– Proposed final dividend	25	–	17,337
– Unappropriated retained earnings		29,889	21,815
		<u>471,770</u>	<u>464,363</u>
Minority interests in equity		<u>129,066</u>	<u>138,775</u>
Total equity		<u>600,836</u>	<u>603,138</u>

		As at 31 December	
	<i>Note</i>	2007	2006
LIABILITIES			
Current liabilities			
Trade and other payables	14	741,030	717,826
Current income tax liabilities		3,725	2,044
Short term bank loans	15	394,111	–
Provision for warranty	16	77,260	12,634
Total liabilities		1,216,126	732,504
Total equity and liabilities		1,816,962	1,335,642
Net current assets		496,954	516,286
Total assets less current liabilities		600,836	603,138

Balance Sheet*As at 31 December 2007**(All amounts in HK dollars thousands unless otherwise stated)*

		As at 31 December	
	<i>Note</i>	2007	2006
ASSETS			
Non-current assets			
Property, plant and equipment	6	758	900
Investments in subsidiaries	8	271,700	271,700
		<u>272,458</u>	<u>272,600</u>
Current assets			
Other receivables	10	918	469
Cash and cash equivalents	11	222,546	196,156
		<u>223,464</u>	<u>196,625</u>
Total assets		<u><u>495,922</u></u>	<u><u>469,225</u></u>
EQUITY			
Capital and reserves			
Share capital	12	335,891	335,891
Other reserves	13	73,635	71,898
Retained earnings			
– Proposed final dividend	25	–	17,337
– Unappropriated retained earnings		82,340	41,355
Total equity		<u>491,866</u>	<u>466,481</u>
Current liabilities			
Other payables	14	4,056	2,744
Total equity and liabilities		<u><u>495,922</u></u>	<u><u>469,225</u></u>
Net current assets		<u><u>219,408</u></u>	<u><u>193,881</u></u>
Total assets less current liabilities		<u><u>491,866</u></u>	<u><u>466,481</u></u>

Consolidated Income Statement*For the year ended 31 December 2007**(All amounts in HK dollars thousands unless otherwise stated)*

		Year ended 31 December	
	<i>Note</i>	2007	2006
Revenue	5	3,167,708	3,549,329
Cost of sales	18	<u>(2,608,047)</u>	<u>(3,317,032)</u>
Gross profit		559,661	232,297
Other gains – net	17	9,699	5,130
Selling and marketing costs	18	(259,104)	(42,457)
Administrative expenses	18	<u>(331,740)</u>	<u>(125,118)</u>
Operating (loss)/profit		(21,484)	69,852
Finance income		11,442	8,109
Finance costs		<u>(9,075)</u>	<u>(6,444)</u>
Finance income – net	21	<u>2,367</u>	<u>1,665</u>
(Loss)/profit before income tax		(19,117)	71,517
Income tax credit/(expense)	22	<u>31,640</u>	<u>(2,358)</u>
Profit for the year		<u><u>12,523</u></u>	<u><u>69,159</u></u>
Attributable to:			
Equity holders of the Company	23	8,074	43,276
Minority interests		<u>4,449</u>	<u>25,883</u>
		<u><u>12,523</u></u>	<u><u>69,159</u></u>
Earnings per share for profit attributable to the equity holders of the Company during the year (expressed in HK cents per share)			
– basic	24	<u><u>0.75</u></u>	<u><u>3.99</u></u>
– diluted	24	<u><u>0.74</u></u>	<u><u>3.99</u></u>
Dividends	25	<u><u>–</u></u>	<u><u>17,337</u></u>

Consolidated Statement of Changes in Equity*For the year ended 31 December 2007**(All amounts in HK dollars thousands unless otherwise stated)*

	<i>Note</i>	Attributable to equity holders of the Company				Minority interests	Total equity
		Issued equity	Other reserves	Retained earnings	Total		
		<i>(Note 12)</i>	<i>(Note 13)</i>				
Balance at 1 January 2006		370,074	35,062	24,880	430,016	138,379	568,395
Dividends related to 2005	25	–	–	(21,671)	(21,671)	(25,449)	(47,120)
Share option granted	13	–	3,654	–	3,654	–	3,654
Appropriation to other reserves		–	7,333	(7,333)	–	–	–
Currency translation differences		–	9,088	–	9,088	(38)	9,050
Profit for the year		–	–	43,276	43,276	25,883	69,159
Balance at 31 December 2006		<u>370,074</u>	<u>55,137</u>	<u>39,152</u>	<u>464,363</u>	<u>138,775</u>	<u>603,138</u>
Balance at 1 January 2007		370,074	55,137	39,152	464,363	138,775	603,138
Dividends related to 2006	25	–	–	(17,337)	(17,337)	(21,748)	(39,085)
Share option granted	13	–	1,737	–	1,737	–	1,737
Currency translation differences		–	14,933	–	14,933	7,590	22,523
Profit for the year		–	–	8,074	8,074	4,449	12,523
Balance at 31 December 2007		<u>370,074</u>	<u>71,807</u>	<u>29,889</u>	<u>471,770</u>	<u>129,066</u>	<u>600,836</u>

Consolidated Cash Flow Statement*For the year ended 31 December 2007**(All amounts in HK dollars thousands unless otherwise stated)*

		Year ended 31 December	
	<i>Note</i>	2007	2006
Cash flows from operating activities			
Cash (used in)/generated from operations	26	(362,808)	432,159
Interest paid		(8,257)	(6,444)
Income tax paid		<u>(4,454)</u>	<u>(10,289)</u>
Net cash (used in)/generated from operating activities		<u>(375,519)</u>	<u>415,426</u>
Cash flows from investing activities			
Interest received		11,216	8,109
Purchase of property, plant and equipment and intangible assets		(19,931)	(32,260)
Proceeds on disposal of property, plant and equipment	26(a)	<u>1,140</u>	<u>42</u>
Net cash used in investing activities		<u>(7,575)</u>	<u>(24,109)</u>
Cash flows from financing activities			
Dividends paid to Company's shareholders		(17,337)	(21,671)
Dividends paid to minority interests		(21,748)	(25,449)
Proceeds from bank loans		1,387,440	1,194,175
Repayment of bank loans borrowed		<u>(993,329)</u>	<u>(1,424,944)</u>
Net cash generated from/(used in) financing activities		<u>355,026</u>	<u>(277,889)</u>
Net (decrease)/increase in cash and cash equivalents		(28,068)	113,428
Cash and cash equivalents at beginning of the year		<u>419,809</u>	<u>306,381</u>
Cash and cash equivalents at end of the year		<u><u>391,741</u></u>	<u><u>419,809</u></u>

Notes to the Consolidated Financial Statements

For the year ended 31 December 2007

(All amounts in HK dollars thousands unless otherwise stated)

1. GENERAL INFORMATION

China Electronics Corporation Holdings Company Limited (the “Company”) was incorporated in the Cayman Islands and continued in Bermuda with limited liability. The Company has its shares listed on The Stock Exchange of Hong Kong Limited.

The principal activities of the Company and its subsidiaries (collectively the “Group”) comprise the manufacturing and sale of mobile handsets and other portable electronics products.

The address of the Company’s registered office is Clarendon House, 2 Church Street, Hamilton HM 11, Bermuda.

These consolidated financial statements are presented in thousands of units of Hong Kong dollar (HK\$’000), unless otherwise stated. These consolidated financial statements have been approved for issue by the Board of Directors on 25 April 2008.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies applied in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

2.1 Basis of preparation

The consolidated financial statements of the Group have been prepared in accordance with Hong Kong Financial Reporting Standards (“HKFRS”) issued by the Hong Kong Institute of Certified Public Accountants. The consolidated financial statements have been prepared under the historical cost convention.

The preparation of financial statements in conformity with HKFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group’s accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the financial statements, are disclosed in Note 4.

(a) Standards, amendment and interpretations effective in 2007

HKFRS 7, ‘Financial instruments: Disclosures’, and the complementary amendment to HKAS 1, ‘Presentation of financial statements – Capital disclosures’, introduces new disclosures relating to financial instruments and does not have any impact on the classification and valuation of the Group’s financial instruments, or the disclosures relating to taxation and trade and other payables.

HK(IFRIC) – Int 8, ‘Scope of HKFRS 2’, requires consideration of transactions involving the issuance of equity instruments, where the identifiable consideration received is less than the fair value of the equity instruments issued in order to establish whether or not they fall within the scope of HKFRS 2. This standard does not have any impact on the Group’s financial statements.

HK(IFRIC) – Int 10, ‘Interim financial reporting and impairment’, prohibits the impairment losses recognised in an interim period on goodwill and investments in equity instruments and in financial assets carried at cost to be reversed at a subsequent balance sheet date. This standard does not have any impact on the Group’s financial statements.

HK(IFRIC) – Int 7, ‘Applying the restatement approach under HKAS 29, Financial reporting in hyperinflationary economies’ and HK(IFRIC) – Int 9, ‘Re-assessment of embedded derivatives’. These standards are not relevant to the Group’s operations.

(b) Standards, amendments and interpretations to existing standards that are not yet effective

The following standards, amendments and interpretations to existing standards have been published and are mandatory for the Group's accounting periods beginning on or after 1 March 2007 or later periods, and the Group has not early adopted them:

HKAS 1 (Revised), 'Presentation of Financial Statements' (effective from 1 January 2009). The revised standard requires presentational changes and further disclosures in the financial statements but does not change the recognition and measurement of specific transactions. The directors of the Group are assessing the impact and believe that the impact on the Group's consolidated financial statements is not significant.

HKAS 23 (Amendment), 'Borrowing costs' (effective from 1 January 2009). The amendment requires an entity to capitalise borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset (one that takes a substantial period of time to get ready for use or sale) as part of the cost of that asset. The option of immediately expensing those borrowing costs will be removed. The Group will apply HKAS 23 (Amended) from 1 January 2009 but is not expected to have material impact on the Group's consolidated financial statements.

HKFRS 8, 'Operating segments' (effective from 1 January 2009). HKFRS 8 replaces HKAS 14 and aligns segment reporting with the requirements of the US standard SFAS 131, 'Disclosures about segments of an enterprise and related information'. The new standard requires a 'management approach', under which segment information is presented on the same basis as that used for internal reporting purposes. The Group will apply HKFRS 8 from 1 January 2009. The expected impact is still being assessed in detail by management, but it appears likely that the number of reportable segments, as well as the manner in which the segments are reported, will change in a manner that is consistent with the internal reporting provided to the chief operating decision-maker.

HK(IFRIC) – Int 11, 'HKFRS 2 – Group and treasury share transactions', (effective from 1 March 2007). HK(IFRIC) – Int 11 provides guidance on whether share-based transactions involving treasury shares or involving Group entities (for example, options over a parent's shares) should be accounted for as equity-settled or cash-settled share-based payment transactions in the stand-alone accounts of the parent and group companies. This interpretation does not have an impact on the Group's consolidated financial statements.

HK(IFRIC) – Int 14, 'HKAS 19 – The limit on a defined benefit asset, minimum funding requirements and their interaction' (effective from 1 January 2008). HK(IFRIC) – Int 14 provides guidance on assessing the limit in HKAS 19 on the amount of the surplus that can be recognised as an asset. It also explains how the pension asset or liability may be affected by a statutory or contractual minimum funding requirement. The Group will apply HK(IFRIC) – Int 14 from 1 January 2008, but it is not expected to have any impact on the Group's financial statements.

HK(IFRIC) – Int 12, 'Service concession arrangements' (effective from 1 January 2008). HK(IFRIC) – Int 12 applies to contractual arrangements whereby a private sector operator participates in the development, financing, operation and maintenance of infrastructure for public sector services. HK(IFRIC) – Int 12 is not relevant to the Group's operations because none of the Group's companies provide for public sector services.

HK(IFRIC) – Int 13, 'Customer loyalty programmes' (effective from 1 July 2008). HK(IFRIC) – Int 13 clarifies that where goods or services are sold together with a customer loyalty incentive (for example, loyalty points or free products), the arrangement is a multiple-element arrangement and the consideration receivable from the customer is allocated between the components of the arrangement using fair values. HK(IFRIC) – Int 13 is not relevant to the Group's operations because none of the Group's companies operate any loyalty programmes.

HKAS 27 (Revised) 'Consolidated and Separate Financial Statements' (effective from annual period beginning on or after 1 July 2009). The amendment requires non-controlling interests (i.e. minority interests) to be presented in the consolidated statement of financial position within equity, separately from the equity of the owners of the parent. Total comprehensive income must be attributed to the owners of the parent and to the non-controlling interests even if this results in the non-controlling interests having a deficit balance. Changes in a parent's ownership interest in a subsidiary that do not result in the loss of control are accounted for within equity. When control of a subsidiary is lost, the assets and liabilities and related equity components of the former subsidiary are derecognised. Any gain or loss is recognised in profit or loss. Any investment retained in the former subsidiary is measured at its fair value at the date when control is lost. The Group will apply HKAS 27 (Revised) from 1 January 2010.

HKFRS 3 (Revised) ‘Business Combination’ (effective for business combinations with acquisition date on or after the beginning of the first annual reporting period beginning on or after 1 July 2009). The amendment may bring more transactions into acquisition accounting as combinations by contract alone and combinations of mutual entities are brought into the scope of the standard and the definition of a business has been amended slightly. It now states that the elements are ‘capable of being conducted’ rather than ‘are conducted and managed’. It requires considerations (including contingent consideration), each identifiable asset and liability to be measured at its acquisition-date fair value, except leases and insurance contracts, reacquired right, indemnification assets as well as some assets and liabilities required to be measured in accordance with other HKFRSs. They are income taxes, employee benefits, share-based payment and non current assets held for sale and discontinued operations. Any non-controlling interest in an acquiree is measured either at fair value or at the non-controlling interest’s proportionate share of the acquiree’s net identifiable assets. The Group will apply HKFRS 3 (Revised) from 1 January 2010.

HKFRS 2 Amendment ‘Share-based Payment Vesting Conditions and Cancellations’ (effective from 1 January 2009). The amendment clarifies the definition of ‘vesting conditions’ and specifies the accounting treatment of “cancellations” by the counterparty to a share-based payment arrangement. Vesting conditions are service conditions (which require a counterparty to complete a specified period of service) and performance conditions (which require a specified period of service and specified performance targets to be met) only. All ‘non-vesting conditions’ and vesting conditions that are market conditions shall be taken into account when estimating the fair value of the equity instruments granted. All cancellations are accounted for as an acceleration of vesting and the amount that would otherwise have been recognised over the remainder of the vesting period is recognised immediately. The Group will apply HKFRS 2 Amendment from 1 January 2009, but it is not expected to have any impact on the Group’s financial statements.

2.2 Consolidation

The consolidated financial statements include the financial statements of the Company and all its subsidiaries made up to 31 December.

(a) Subsidiaries

Subsidiaries are all entities (including special purpose entities) over which the Group has the power to govern the financial and operating policies generally accompanying a shareholding of more than one half of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group controls another entity.

Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are de-consolidated from the date that control ceases.

The purchase method of accounting is used to account for the acquisition of subsidiaries by the Group. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any minority interest. The excess of the cost of acquisition over the fair value of the Group’s share of the identifiable net assets acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognised directly in the income statement.

Inter-company transactions, balances and unrealised gains on transactions between group companies are eliminated. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group.

In the Company’s balance sheet the investments in subsidiaries are stated at cost less provision for impairment losses (Note 2.7). The results of subsidiaries are accounted for by the Company on the basis of dividend received and receivable.

(b) Transactions with minority interests

The Group applies a policy of treating transactions with minority interests as transactions with parties external to the Group. Disposals to minority interests result in gains and losses for the Group that are recorded in the consolidated income statement. Purchases from minority interests result in goodwill, being the difference between any consideration paid and the relevant share acquired of the carrying value of net assets of the subsidiary.

2.3 Segment reporting

A business segment is a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different from those of other business segments. A geographical segment is engaged in providing products or services within a particular economic environment that are subject to risks and returns that are different from those of segments operating in other economic environments.

2.4 Foreign currency translation

(a) *Functional and presentation currency*

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates (the "functional currency"). The consolidated financial statements are presented in Hong Kong dollars, which is different from the Group's functional currency of Renminbi. The Directors consider that presentation of consolidated financial statements in Hong Kong dollars will facilitate analysis of financial information of the Group.

(b) *Transactions and balances*

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement.

(c) *Group companies*

The results and financial position of all the group entities (none of which has the currency of a hyperinflationary economy) that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

- assets and liabilities for each balance sheet presented are translated at the closing rate at the date of that balance sheet;
- income and expenses for each income statement are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the dates of the transactions); and
- all resulting exchange differences are recognised as a separate component of equity.

On consolidation, exchange differences arising from the translation of the net investment in foreign entities, and of borrowings are taken to shareholders' equity. When a foreign operation is partially disposed of or sold, such exchange differences that were recorded in equity are recognised in the income statement as part of the gain or loss on sale.

2.5 Property, plant and equipment

Property, plant and equipment are stated at historical cost less depreciation and impairment losses. Historical cost includes expenditure that is directly attributable to the acquisition of the items. Cost may also include transfers from equity of any gains/losses on qualifying cash flow hedges of foreign currency purchases of property, plant and equipment.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. All other repairs and maintenance are expensed in the income statement during the financial period in which they are incurred.

Depreciation of property, plant and equipment is calculated using the straight-line method to allocate cost to their residual values over their estimated useful lives, as follows:

– Leasehold improvements	5 years (or over the lease term, whichever is shorter)
– Plant and machinery	3-4 years
– Motor vehicles	5 years
– Furniture and fixtures	3-5 years

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount (Note 2.7).

Gains and losses on disposals are determined by comparing the proceeds with the carrying amount and are recognised in the income statement.

2.6 Intangible assets

(a) Goodwill

Goodwill represents the excess of the cost of an acquisition over the fair value of the Group's share of the net identifiable assets of the acquired subsidiary at the date of acquisition. Goodwill on acquisitions of subsidiaries is included in intangible assets. Goodwill is tested annually for impairment and carried at cost less accumulated impairment losses. Impairment losses on goodwill are not reversed. Gains and losses on the disposal of an entity include the carrying amount of goodwill relating to the entity sold.

Goodwill is allocated to cash-generating units for the purpose of impairment testing. The allocation is made to those cash-generating units or groups of cash-generating units that are expected to benefit from the business combination in which the goodwill arose.

If the fair value of the Group's share of the net identifiable assets of the acquired subsidiary at the date of acquisition exceeds the cost of acquisition, the excess should be recognised immediately in the income statement.

(b) Computer software

Acquired computer software licences are capitalised on the basis of the costs incurred to acquire and bring to use the specific software. These costs are amortised over their estimated useful lives (three to five years).

Costs associated with developing or maintaining computer software programmes are recognised as an expense as incurred. Costs that are directly associated with the development of identifiable and unique software products controlled by the Group, and that will probably generate economic benefits exceeding costs beyond one year, are recognised as intangible assets. Direct costs include the employee costs incurred as a result of developing software and an appropriate portion of relevant overheads.

Computer software development costs recognised as assets are amortised over their estimated useful lives.

(c) 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.

2.7 Impairment of investments in subsidiaries and non-financial assets

Assets that have an indefinite useful life or have not yet available for use are not subject to amortisation and are tested annually for impairment. Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). Non-financial assets other than goodwill that suffered an impairment are reviewed for possible reversal of the impairment at each reporting date.

2.8 Financial assets

The Group classifies its financial assets in the following categories: financial assets at fair value through profit or loss, loans and receivables, held-to-maturity investments, and available-for-sale financial assets. The classification depends on the purpose for which the financial assets were acquired. Management determines the classification of its financial assets at initial recognition.

(a) *Financial assets at fair value through profit or loss*

Financial assets at fair value through profit or loss are financial assets held for trading. A financial asset is classified in this category if acquired principally for the purpose of selling in the short term. Derivatives are also categorised as held for trading unless they are designated as hedges. Assets in this category are classified as current assets.

(b) *Loans and receivables*

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are included in current assets, except for maturities greater than 12 months after the balance sheet date. These are classified as non-current assets. Loans and receivables are classified as trade and other receivables in the balance sheet (Note 2.10).

(c) *Held-to-maturity investments*

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Group's management has the positive intention and ability to hold to maturity. During the year, the Group did not hold any investments in this category.

(d) *Available-for-sale financial assets*

Available-for-sale financial assets are non-derivatives that are either designated in this category or not classified in any of the other categories. They are included in non-current assets unless management intends to dispose of the investment within 12 months of the balance sheet date. During the year, the Group did not hold any investments in this category.

Regular purchases and sales of financial assets are recognised on trade-date – the date on which the Group commits to purchase or sell the asset. Investments are initially recognised at fair value plus transaction costs for all financial assets not carried at fair value through profit or loss. Financial assets carried at fair value through profit or loss are initially recognised at fair value, and transaction costs are expensed in the income statement. Financial assets are derecognised when the rights to receive cash flows from the investments have expired or have been transferred and the Group has transferred substantially all risks and rewards of ownership. Available-for-sale financial assets and financial assets at fair value through profit or loss are subsequently carried at fair value. Loans and receivables and held-to-maturity investments are carried at amortised cost using the effective interest method.

Gains or losses arising from changes in the fair value of the 'financial assets at fair value through profit or loss' category are included in the income statement in the period in which they arise.

The Group assesses at each balance sheet date whether there is objective evidence that a financial asset or a group of financial assets is impaired. Impairment testing of loan and receivable is set out in Note 2.10.

2.9 Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is determined using the first-in, first-out method. The cost of finished goods and work in progress comprises design costs, raw materials, direct labour, other direct costs and related production overheads (based on normal operating capacity). It excludes borrowing costs. Net realisable value is the estimated selling price in the ordinary course of business, less applicable variable selling expenses.

2.10 Trade and other receivables

Trade and other receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less provision for impairment. A provision for impairment of trade and other receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of receivables. Significant financial difficulties of the debtor, probability that the debtor will enter bankruptcy or financial reorganisation, and default or delinquency in payments are considered indicators that the trade receivable is impaired. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account, and the amount of the loss is recognised in the income statement within administrative expenses. When the receivable is uncollectible, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited against administrative expenses in the income statement.

2.11 Cash and cash equivalents

Cash and cash equivalents include cash in hand, deposits held at call with banks, other short-term highly liquid investments with original maturities of three months or less, and bank overdrafts.

2.12 Share capital

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction, net of tax, from the proceeds.

2.13 Trade payables

Trade payables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method.

2.14 Borrowings

Borrowings are recognised initially at fair value, net of transaction costs incurred. Borrowings are subsequently stated at amortised cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognised in the income statement over the period of the borrowings using the effective interest method.

Borrowings are classified as current liabilities unless the Group has an unconditional right to defer settlement of the liability for at least 12 months after the balance sheet date.

2.15 Deferred income tax

Deferred income tax 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 consolidated financial statements. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

Deferred income 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.

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

2.16 Provision

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 the amount has been reliably estimated. Provisions are not recognised for future operating losses.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognised even if the likelihood of an outflow with respect to any one item included in the same class of obligations may be small.

Provisions are measured at the present value of expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to passage of time is recognised as interest expense.

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

2.17 Employee benefits*(a) 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 Group’s subsidiaries operating in the People’s Republic of China (the “PRC”) have 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 income statement as and when incurred.

(b) 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.

(c) 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.

(d) Share-based compensation

The Group operates an equity-settled, share-based compensation plan. The fair value of the employee services received in exchange for the grant of the options is recognised as an expense. The total amount to be expensed over the vesting period is determined by reference to the fair value of the options granted, excluding the impact of any non-market vesting conditions. Non-market vesting conditions are included in assumptions about the number of options that are expected to vest. At each balance sheet date, the entity revises its estimates of the number of options that are expected to vest. It recognises the impact of the revision of original estimates, if any, in the income statement, and a corresponding adjustment to equity.

The proceeds received net of any directly attributable transaction costs are credited to share capital (nominal value) and share premium when the options are exercised.

2.18 Contingent liabilities

A contingent liability is a possible obligation that arises from past events and whose existence 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.

2.19 Revenue recognition

Revenue comprises the fair value of the consideration received or receivable for the sale of goods, net of value-added tax, returns, rebates and discounts. Revenue is recognised when the goods are delivered to customers, the customers has accepted the goods and collectibility of the related receivables is reasonably assured.

Interest income is recognised on a time-proportion basis using the effective interest method. When a receivable is impaired, the Group reduces the carrying amount to its recoverable amount, being the estimated future cash flow discounted at original effective interest rate of the instrument, and continues unwinding the discount as interest income.

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

2.20 Operating leases (as the lessee for operating leases)

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are charged to the income statement on a straight-line basis over the period of the lease.

2.21 Dividend distribution

Dividend distribution to the Company's shareholders is recognised as a liability in the Group's financial statements in the period in which the dividends are approved by the Company's shareholders.

3. FINANCIAL RISK MANAGEMENT

3.1 Financial risk factors

The Group's activities expose it to a variety of financial risks: foreign exchange risk, credit risk, liquidity risk and cash flow and fair value interest rate risk. The Group's overall risk management programme focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the Group's financial performance.

(a) Foreign exchange risk

The foreign exchange risks of the Group occur due to the fact that the Group has business activities denominated in foreign currencies, primarily with respect to the United States dollar ("US dollar"), Hong Kong dollar, Euro and Japanese Yen. Foreign exchange risk arises from future commercial transactions and recognised assets and liabilities. Nevertheless, the conversion of Renminbi into foreign currencies is subject to the rules and regulations of foreign exchange control promulgated by the PRC government.

The Group currently does not have a foreign currency hedge policy.

At 31 December 2007, if RMB had strengthened/weakened by 5% against US dollar with all other variables held constant, post-tax profit for the years would have been HK\$3,678,000 higher/lower (2006: HK\$10,483,000 lower/higher), mainly as a result of foreign exchange gains or losses on translation of US dollar denominated trade receivables, cash and cash equivalents and financial liabilities.

At 31 December 2007, if RMB had strengthened/weakened by 5% against HK dollar with all other variables held constant, post-tax profit for the years would have been HK\$5,086,000 higher/lower (2006: HK\$4,319,000 higher/lower), mainly as a result of foreign exchange gains or losses on translation of HK dollar denominated trade receivables, cash and cash equivalents and financial liabilities.

At 31 December 2007, if RMB had strengthened/weakened by 5% against Euro with all other variables held constant, post-tax profit for the year would have been HK\$24,064,000 lower/higher (2006: HK\$306,000 higher/lower), mainly as a result of foreign exchange gains or losses on translation of Euro denominated trade receivables, cash and cash equivalents and financial liabilities.

As less than 10% of the Group's foreign currency transactions are denominated in Japanese Yen and other foreign currencies, the directors of the Group are of the view that foreign exchange risk in relation to transactions denominated in Japanese Yen and other foreign currencies is low. Therefore, no sensitivity analysis for these currencies is presented.

(b) Credit risk

The Group has no significant concentrations of credit risk. Credit risk arises from cash and cash equivalents, and trade and other receivables.

As at 31 December 2007, all the Group's bank deposits are placed in high quality financial institutions without significant exposure to credit risk.

For trade and other receivables, the credit quality of the counterparties is assessed by taking into account their financial position, credit history and other factors. Individual credit limits are set based on the assessment of the credit quality. Given the constant repayment history, the directors are of the opinion that the risk of default by these counterparties is not significant.

The Group's credit sales are only made to customers with an appropriate credit history and at credit period of 30 to 60 days.

(c) Liquidity risk

Prudent liquidity risk management implies maintaining sufficient working capital, the availability of funding through an adequate amount of committed credit facilities and the ability to close out market positions. Due to the dynamic nature of the underlying businesses, the Group maintains flexibility in funding by keeping availability of committed credit lines.

The table below analyses the Group's financial liabilities that will be settled on a net basis into relevant maturity groupings based on the remaining period at the balance sheet to the contractual maturity date. The amounts disclosed in the table are the contractual undiscounted cash flows. Balances due within 12 months equal their carrying balances, as the impact of discounting is not significant.

Less than 1 year	2007	2006
Short term bank loans	394,111	–
Interest payment on short term bank loans	7,935	–
Trade and other payables	741,030	717,826
Provision for warranty	77,260	12,634
Current income tax liabilities	3,725	2,044

(d) Cash flow and fair value interest rate risk

Other than deposits held in banks, the Group does not have significant interest-bearing assets. The average rate of deposits held in banks as at 31 December 2007 was approximately 2.46% per annum (2006: 1.68%). Any change in the interest rate from time to time is not considered to have significant impact to the Group.

The Group's interest rate risk which affects its income and operating cash flows mainly arises from bank borrowings. The bank borrowings were at fixed rates and expose the Group to fair value interest rate risk. As all the Group's bank borrowings were short term loans and any change in the interest rate from time to time is not considered to have significant impact to the Group.

3.2 Capital risk management

The Group's objectives when managing capital are to safeguard the Group's ability to continue as a going concern in order to provide returns for shareholders and benefits for other stakeholders and to maintain an optimal capital structure to reduce the cost of capital.

In order to maintain or adjust the capital structure, the Group may adjust the amount of dividends paid to shareholders, issue new shares or sell assets to reduce debt.

The Group monitors capital on the basis of the gearing ratio. This ratio is calculated as net debt divided by total capital. Net debt is calculated as total borrowings (including bank borrowings, finance lease liabilities and the borrowing component of convertible notes as shown in the consolidated balance sheets) less cash and cash equivalents. Total capital is calculated as equity, as shown in the consolidated balance sheets, plus net debt.

The Company's strategy is to maintain an operation with minimal capital risk. The gearing ratio as at 31 December 2007 was 0.4%. The Group did not have any borrowing at 31 December 2006 and all its capital was sourced from equity. The directors are of the opinion that the Group does not have significant capital risk.

3.3 Fair value estimation

The carrying value less impairment provision of trade receivables and payables are a reasonable approximation of their fair values. The fair values of financial liabilities for disclosure purposes is estimated by discounting the future contractual cash flows at the current market interest rate that is available to the Group for similar financial instruments.

4. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

(a) Estimated impairment of non-financial assets

The Group tests annually whether non-financial assets, mainly including property, plant and equipment and intangible assets has suffered any impairment in accordance with the accounting policy stated in Note 2.7. The recoverable amounts of cash-generating units have been determined based on value-in-use calculations. These calculations require the use of estimates.

(b) Income taxes

The Group is subject to income taxes in numerous jurisdictions. Significant judgement is required in determining the worldwide provision for income taxes. There are many transactions and calculations for which the ultimate tax determination is uncertain during the ordinary course of business. The Group recognises liabilities for anticipated tax audit issues based on estimates of whether additional taxes will be due. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the income tax and deferred tax provisions in the period in which such determination is made.

(c) Share option

The Group operates a share option scheme. The fair value of the options granted during the year (Note 13 (c)) is determined by using valuation techniques. The Group uses its judgements to select the valuation method and make assumptions for the significant inputs into the valuation model. At each balance sheet date, the Group Reviews its estimates of the number of options that are expected to become exercisable. It recognises the impact of the revision of original estimates, if any, in the income statement, and a corresponding adjustment to equity over the remaining vesting period.

(d) Provision for warranty

The Group generally offers warranties for its certain products and undertakes to repair and replace items that fail to operate satisfactorily. Management estimates the related provision for future warranty claims based on historical warranty claim information, as well as recent trends that might suggest that past cost information may differ from future claims.

Factors that could impact the estimated claim information include the success of the Group's productivity and quality initiatives, as well as parts and labour costs. The estimates and judgments used are however not expected to have a significant risk of causing a material adjustment to the carrying amounts of the provision for warranty within the next financial year.

Should the estimated annual warranty expenses rate differ by 10% from management's estimates, the Group would have charged additional warranty expenses amount to approximate HK\$11,749,000 for the year ended 2007 (2006: HK\$2,109,000).

5. SEGMENT INFORMATION

Primary reporting format – business segments

The Group is principally engaged in manufacturing and sale of mobile handsets and other portable electronics products.

	<i>“Philips”</i> mobile handsets <i>(note a)</i>		Own branded and other mobile handsets		Multi-media players		Total	
	2007	2006	2007	2006	2007	2006	2007	2006
Turnover	<u>1,944,582</u>	<u>2,586,710</u>	<u>535,309</u>	<u>654,053</u>	<u>687,817</u>	<u>308,566</u>	<u>3,167,708</u>	<u>3,549,329</u>
Segment results	<u>168,719</u>	<u>132,765</u>	<u>36,400</u>	<u>82,320</u>	<u>28,717</u>	<u>17,212</u>	233,836	232,297
Other gains, net							9,699	5,130
Unallocated costs							<u>(265,019)</u>	<u>(167,575)</u>
Operating (loss)/profit							(21,484)	69,852
Finance income – net							<u>2,367</u>	<u>1,665</u>
(Loss)/profit before income tax							(19,117)	71,517
Income tax credit/(expenses)							<u>31,640</u>	<u>(2,358)</u>
Profit for the year							<u>12,523</u>	<u>69,159</u>
Segment assets	698,636	358,700	56,748	118,693	139,481	38,040	894,865	515,433
Unallocated assets							<u>922,097</u>	<u>820,209</u>
Total assets							<u>1,816,962</u>	<u>1,335,642</u>
Segment liabilities	227,045	371,762	8,243	170,488	3,378	48,983	238,666	591,233
Unallocated liabilities							<u>977,460</u>	<u>141,271</u>
Total liabilities							<u>1,216,126</u>	<u>732,504</u>
Capital expenditures							19,931	32,260
Depreciation/amortisation charge							44,240	49,646
Impairment charge/(reversal)							<u>28,174</u>	<u>(4,952)</u>

- (a) “*Philips*” mobile handsets were OEM products which all sold to Philips Group (See definition in Note 29 (a)) in 2006. During the year, the Group assumed the business of “*Philips*” mobile products and sold such products directly to distributors.

Unallocated costs consist primarily of selling and marketing costs and administrative expenses, which contribute to all business segments.

Segment assets consist primarily of inventories and trade receivables. Unallocated assets comprise property, plant and equipment, intangible assets, deferred taxation, other receivables and cash and cash equivalents.

Segment liabilities comprise trading liabilities. Unallocated liabilities comprise items such as taxation, borrowings, provisions and other payables.

Secondary reporting format – geographical segments

The Group’s three business segments operate in five main geographical areas – Mainland China, Europe, Hong Kong, Asia (excluding Mainland China and Hong Kong) and North America. The segment sales based on the geographical location of its customers are presented below:

	2007	2006
Sales		
Mainland China	1,243,354	1,676,916
Europe (<i>Note b</i>)	630,047	6,540
Asia excluding Mainland China and Hong Kong (<i>Note b</i>)	228,762	1,030,871
Hong Kong (<i>Note b</i>)	1,041,209	835,002
North America	24,336	–
	<u>3,167,708</u>	<u>3,549,329</u>

- (b) In 2006, most of “*Philips*” branded mobile products for the Europe market was arranged through the Philips Group companies located in Asia. In 2007, sales to Europe market was mostly made to distributors located in Europe directly.

No segment assets and liabilities are presented as over 90% of the Group’s assets are located in Mainland China.

6. PROPERTY, PLANT AND EQUIPMENT

Group

	Leasehold improvements	Plant and machinery	Motor vehicles	Furniture and fixtures	Total
At 1 January 2006					
Cost	37,834	286,627	3,265	29,068	356,794
Accumulated depreciation and impairment	(25,851)	(229,047)	(2,055)	(20,790)	(277,743)
Net book amount	11,983	57,580	1,210	8,278	79,051
Year ended 31 December 2006					
Opening net book amount	11,983	57,580	1,210	8,278	79,051
Exchange differences	342	1,259	17	154	1,772
Additions	2,853	19,024	1,375	2,982	26,234
Disposals	–	(12)	–	(36)	(48)
Depreciation charge	(4,323)	(34,792)	(592)	(5,617)	(45,324)
Closing net book amount	10,855	43,059	2,010	5,761	61,685
At 31 December 2006					
Cost	24,795	307,331	4,743	32,596	369,465
Accumulated depreciation and impairment	(13,940)	(264,272)	(2,733)	(26,835)	(307,780)
Net book amount	10,855	43,059	2,010	5,761	61,685
Year ended 31 December 2007					
Opening net book amount	10,855	43,059	2,010	5,761	61,685
Exchange differences	665	2,295	78	283	3,321
Additions	1,096	8,462	446	5,565	15,569
Disposals	–	(20)	–	(783)	(803)
Depreciation charge	(4,619)	(29,334)	(715)	(4,057)	(38,725)
Closing net book amount	7,997	24,462	1,819	6,769	41,047
At 31 December 2007					
Cost	27,197	336,411	5,458	38,487	407,553
Accumulated depreciation and impairment	(19,200)	(311,949)	(3,639)	(31,718)	(366,506)
Net book amount	7,997	24,462	1,819	6,769	41,047

Depreciation expense of HK\$29,577,000 (2006: HK\$35,415,000) has been expensed in cost of sales, HK\$237,000 (2006: HK\$200,000) in selling and marketing costs and HK\$8,911,000 (2006: HK\$9,709,000) in administrative expenses.

Lease rental expense amounting to HK\$25,791,000 (2006: HK\$14,860,000) relating to the lease of property and machinery are included in the income statement.

Company

	Motor vehicles	Furniture and fixtures	Total
At 1 January 2006			
Cost	684	124	808
Accumulated depreciation	<u>(182)</u>	<u>(21)</u>	<u>(203)</u>
Net book amount	<u>502</u>	<u>103</u>	<u>605</u>
Year ended 31 December 2006			
Opening net book amount	502	103	605
Additions	488	57	545
Disposal	–	(10)	(10)
Depreciation charge	<u>(211)</u>	<u>(29)</u>	<u>(240)</u>
Closing net book amount	<u>779</u>	<u>121</u>	<u>900</u>
At 31 December 2006			
Cost	1,172	166	1,338
Accumulated depreciation	<u>(393)</u>	<u>(45)</u>	<u>(438)</u>
Net book amount	<u>779</u>	<u>121</u>	<u>900</u>
Year ended 31 December 2007			
Opening net book amount	779	121	900
Additions	134	24	158
Disposal	–	(17)	(17)
Depreciation charge	<u>(254)</u>	<u>(29)</u>	<u>(283)</u>
Closing net book amount	<u>659</u>	<u>99</u>	<u>758</u>
At 31 December 2007			
Cost	1,307	164	1,471
Accumulated depreciation	<u>(648)</u>	<u>(65)</u>	<u>(713)</u>
Net book amount	<u>659</u>	<u>99</u>	<u>758</u>

7. INTANGIBLE ASSETS – GROUP

	Computer software
At 1 January 2006	
Cost	23,918
Accumulated amortisation and impairment	(9,805)
Net book amount	14,113
Year ended 31 December 2006	
Opening net book amount	14,113
Exchange differences	434
Additions	6,026
Amortisation charge	(4,322)
Closing net book amount	16,251
At 31 December 2006	
Cost	30,900
Accumulated amortisation and impairment	(14,649)
Net book amount	16,251
Year ended 31 December 2007	
Opening net book amount	16,251
Exchange differences	1,046
Additions	4,362
Amortisation charge	(5,515)
Closing net book amount	16,144
At 31 December 2007	
Cost	37,588
Accumulated amortisation and impairment	(21,444)
Net book amount	16,144

Amortisation of HK\$1,778,000 (2006: HK\$634,000) has been expensed in cost of sales, HK\$42,000 (2006: HK\$32,000) in selling and marketing costs and HK\$3,695,000 (2006: HK\$3,649,000) in administrative expenses.

8. INVESTMENTS IN SUBSIDIARIES – COMPANY

	2007	2006
Investments – unlisted shares, at cost (<i>Note (a)</i>)	260,000	260,000
Amounts due from subsidiaries (<i>Note (b)</i>)	11,700	11,700
	<u>271,700</u>	<u>271,700</u>

(a) The following is a list of the principal subsidiaries as at 31 December 2007.

Name	Place of incorporation and kind of legal entity	Principal activities and place of operation	Particulars of issued share capital	Interest held
<i>Indirectly held:</i>				
Shenzhen Sang Fei Consumer Communications Co., Ltd. (“Sang Fei”)	PRC, a Sino- foreign equity joint venture company	PRC, manufacture and sale of mobile handsets and other portable electronics products	Registered capital of US\$33,000,000	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%

(b) The balance is unsecured, interest free and has no fixed repayment term. It is classified as investment in subsidiaries.

9. INVENTORIES – GROUP

	2007	2006
Raw materials	257,504	230,856
Work in progress	46,950	54,850
Finished goods	139,735	50,096
	<u>444,189</u>	<u>335,802</u>

The cost of inventories recognised as expense and included in cost of sales amounted to HK\$2,400,076,000 (2006: HK\$3,127,030,000).

Written down of inventories to net realisable value of HK\$27,908,000 (2006: reversal of written down with amount of HK\$4,952,000) has been included in cost of sales during the year.

10. TRADE AND OTHER RECEIVABLES

	Group		Company	
	2007	2006	2007	2006
Trade receivables (<i>Note (a)</i>)	755,474	415,932	–	–
Less: provision for impairment	(266)	–	–	–
Trade receivables – net	755,208	415,932	–	–
Notes receivables	15,081	799	–	–
Other receivables from related parties	7,091	24,026	–	–
Prepayments and deposits	64,526	21,011	428	219
Value-added tax refundable	14,129	25,739	–	–
Other receivables	21,115	5,672	490	250
	<u>877,150</u>	<u>493,179</u>	<u>918</u>	<u>469</u>

The Directors are of the opinion that the carrying amounts of trade and other receivables approximate their fair values. All trade and other receivables are due within 1 year and non interest-bearing.

- (a) The majority of the Group's sales are on letter of credit or documents against payment. The remaining amounts are with credit term of 30 to 60 days. At 31 December 2007, the ageing analysis of the Group's gross trade receivables was as follows:

Ageing	2007	2006
Current to 30 days	734,238	410,109
31 – 60 days	12,151	2,561
Over 60 days and within 1 year	8,324	1,725
Over 1 year	761	1,537
	<u>755,474</u>	<u>415,932</u>

Including in the balance were trade and other receivables from related parties of HK\$61,305,000 (2006: HK\$382,828,000) (Note 29(c)).

- (b) The maximum exposure to credit risk at 31 December 2007 and 2006 is the fair value of the trade receivables mentioned above. The Group does not hold any collateral as security.

Movement on the provision for impairment at the Group's trade receivables are as follows:

	2007	2006
At 1 January	–	–
Provision for impairment	266	–
At 31 December	<u>266</u>	<u>–</u>

At 31 December 2007, trade receivables of HK\$31,063,000 (2006: HK\$7,888,000) were past due but not impaired. These related to a number of customers which had no history of default, the ageing analysis of these trade receivable is as follows:

Ageing	2007	2006
Current to 30 days	10,093	2,065
31 – 60 days	12,151	2,561
Over 60 days and within 1 year	8,324	1,725
Over 1 year	495	1,537
	<u>31,063</u>	<u>7,888</u>

As at 31 December 2007, trade receivables of HK\$266,000 were impaired and fully provided for (2006: nil).

The carrying amounts of the Group's trade and other receivables are denominated in the following currencies:

Currency	2007	2006
Renminbi	170,672	156,454
HK dollar	918	469
US dollar	165,208	336,256
Euro	540,225	–
Other currencies	127	–
	<u>877,150</u>	<u>493,179</u>

11. CASH AND CASH EQUIVALENTS

	Group		Company	
	2007	2006	2007	2006
Cash at bank and in hand				
China Electronics Corporation				
Finance Co., Ltd. (<i>Note 29(c)</i>)	–	51,595	–	–
Other banks and financial				
institutions	163,841	170,131	6,105	9,151
	<u>163,841</u>	<u>221,726</u>	<u>6,105</u>	<u>9,151</u>
Short-term bank deposits	227,900	198,083	216,441	187,005
	<u>391,741</u>	<u>419,809</u>	<u>222,546</u>	<u>196,156</u>

China Electronics Corporation Finance Co., Ltd. is a non-bank financial institution approved by the People's Bank of China. The deposits yield interest at prevailing saving deposit rates.

The effective interest rate on short-term bank deposits was 1.68% per annum (2006: 2.46%). The maturity days of these deposits ranged from 2 to 18 days (2006: 5 to 29 days).

12. ISSUED EQUITY/SHARE CAPITAL

(a) Issued equity – Group

	Number of shares	Issued equity
As 1 January and 31 December 2006	<u>1,083,560,000</u>	<u>370,074</u>
As 1 January and 31 December 2007	<u>1,083,560,000</u>	<u>370,074</u>

(i) The number of share reflect the company's ordinary

(ii) On 10 December 2003, China Electronics Corporation ("CEC"), the Company, the Company's then holding company, Winsan International Holdings Limited entered into a sale and purchase agreement. Pursuant to the agreement, the Company acquired CEC's 65% equity interest in Sang Fei (the "Acquisition") and the consideration was satisfied by the issuance of the Company's 6,500,000,000 shares to CEC. The Acquisition was completed on 24 September 2004 and has been accounted for as a reverse acquisition. For accounting purpose, Sang Fei is regarded as the acquirer while the Company and its then subsidiaries are deemed to have been acquired by Sang Fei. Accordingly, the amount recognised as issued equity of the Group, 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 Company and its then subsidiaries.

(b) Share capital – Company

	Number of shares – ordinary share of HK\$0.01 each				
	Authorised	Issued and fully paid	Share capital	Share premium	Total
At 1 January and 31 December 2006	<u>30,000,000,000</u>	<u>1,083,560,000</u>	<u>10,836</u>	<u>325,055</u>	<u>335,891</u>
At 1 January and 31 December 2007	<u>30,000,000,000</u>	<u>1,083,560,000</u>	<u>10,836</u>	<u>325,055</u>	<u>335,891</u>

13. OTHER RESERVES

Group

	Capital reserve (Note (a))	Surplus reserves (Note (b))	Share option (Note (c))	Translation reserve	Total
At 1 January 2006	(1,806)	25,992	6,572	4,304	35,062
Share option granted	–	–	3,654	–	3,654
Appropriation from retained earnings	–	7,333	–	–	7,333
Currency translation differences	–	–	–	9,088	9,088
At 31 December 2006	<u>(1,806)</u>	<u>33,325</u>	<u>10,226</u>	<u>13,392</u>	<u>55,137</u>
At 1 January 2007	(1,806)	33,325	10,226	13,392	55,137
Share option granted	–	–	1,737	–	1,737
Currency translation differences	–	–	–	14,933	14,933
At 31 December 2007	<u>(1,806)</u>	<u>33,325</u>	<u>11,963</u>	<u>28,325</u>	<u>71,807</u>

(a) Capital reserve

Capital reserve represents the exchange differences arising from paid-in capital paid by foreign currencies in the principal subsidiary, Sang Fei.

(b) Surplus reserves

In accordance with the “Laws of the People’s Republic of China 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.

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.

(c) Share option

On 25 October 2005, 28,450,000 options were granted to certain directors, employees and other participants at an exercise price of HK\$1.488 under the Share Option Scheme. 40% of the options granted are exercisable from 1 November 2005 to 31 October 2008, another 30% are exercisable from 1 November 2006 to 31 October 2009 and the remaining 30% are exercisable from 1 November 2007 to 31 October 2010. The options have an option term of 3 years commencing from the exercisable date. No option was exercised during the year.

Movements in the number of share options outstanding are as follows:

	2007	2006
At 1 January	21,150,000	28,450,000
Lapsed	<u>(200,000)</u>	<u>(7,300,000)</u>
At 31 December	<u>20,950,000</u>	<u>21,150,000</u>

All share options outstanding as at 31 December 2007 were exercisable (2006: 14,805,000).

Share options outstanding at 31 December 2007 and 2006 have the following expiry date:

	2007	2006
Expiry date – 31 October		
2008	8,380,000	8,460,000
2009	6,285,000	6,345,000
2010	<u>6,285,000</u>	<u>6,345,000</u>
	<u>20,950,000</u>	<u>21,150,000</u>

Expense arising from the Share Option Scheme recognised in administrative expenses during the year amounted to HK\$1,737,000 (2006: HK\$3,654,000).

Company

	Contributed surplus	Share option	Total
At 1 January 2006	61,672	6,572	68,244
Share option granted	–	3,654	3,654
	<u> </u>	<u> </u>	<u> </u>
At 31 December 2006	<u>61,672</u>	<u>10,226</u>	<u>71,898</u>
	<u> </u>	<u> </u>	<u> </u>
At 1 January 2007	61,672	10,226	71,898
Share option granted	–	1,737	1,737
	<u> </u>	<u> </u>	<u> </u>
At 31 December 2007	<u>61,672</u>	<u>11,963</u>	<u>73,635</u>
	<u> </u>	<u> </u>	<u> </u>

14. TRADE AND OTHER PAYABLES

	Group		Company	
	2007	2006	2007	2006
Trade payables	381,597	511,472	–	–
Other payables from related parties				
<i>(Note 29(c))</i>	1,332	17,072	–	–
Accrued expenses	192,149	47,205	4,040	2,744
Advance from customers	65,197	52,870	–	–
Other payables	100,755	89,207	16	–
	<u>741,030</u>	<u>717,826</u>	<u>4,056</u>	<u>2,744</u>
	<u> </u>	<u> </u>	<u> </u>	<u> </u>

At 31 December 2007, the ageing analysis of the Group's trade payables was as follows:

	2007	2006
Current to 30 days	367,655	487,812
31 – 60 days	474	14
Over 60 days	<u>13,468</u>	<u>23,646</u>
	<u>381,597</u>	<u>511,472</u>
	<u> </u>	<u> </u>

Included in the balance of trade and other payables to related parties amounted to HK\$17,834,000 (2006: HK\$48,159,000) (Note 29(c)).

The Directors are of the opinion that the carrying amount of trade and other payables approximate their fair values.

15. SHORT TERM BANK LOANS – GROUP

The bank loans as at 31 December 2007 were unsecured, repayable within one year and bear interest at the average borrowing rate of 6.19% per annum.

The Group's bank loans as at 31 December 2007 exposed to interest rate changes and the contractual repricing dates within 6 months.

The carrying amounts of the short term bank loans approximate their fair value, which are denominated in the following currencies:

	2007	2006
Renminbi	354,839	–
US dollar	39,272	–
	<u>394,111</u>	<u>–</u>

The Group has undrawn borrowing facilities of approximately HK\$466,104,000 as at 31 December 2007 (2006: HK\$1,000,000,000). The facilities are at floating rate and expiring within one year which are subject to review at various dates during 2008.

16. PROVISION FOR WARRANTY – GROUP

The Group provides free repair and replacement services ranging from 12 to 15 months after sales. The cost of the warranty obligation under which the Group agrees to remedy defects in its products is accrued at the time the related sales are recognised. As at 31 December 2007, the Group had provided for expected warranty claims on own mobile products and certain ODM products based on past experience of the level of repairs and returns.

	2007	2006
At 1 January	12,634	2,106
Charged for the year (a)	64,437	21,089
Provision related to OEM products (b)	53,055	–
Less: utilised during the year	<u>(52,866)</u>	<u>(10,561)</u>
At 31 December	<u>77,260</u>	<u>12,634</u>

(a) Provision for warranty of HK\$64,437,000 (2006: HK\$21,089,000) has been charged to selling and marketing costs;

(b) Provision for warranty of HK\$53,055,000 was related to OEM products which were sold to Philips Group before 1 April 2007 (see Note 5(a)). In this respect, Philips Group reimbursed nearly the same amount to the Group.

17. OTHER GAINS – NET

	2007	2006
Sales of samples and materials	1,633	5,355
Written off of payables (Note a)	7,504	–
Others	<u>562</u>	<u>(225)</u>
	<u>9,699</u>	<u>5,130</u>

(a) These represented long-aged trade payables which the Directors are of the opinion that the obligation for future settlement is remote and therefore write off them in current year.

18. EXPENSES BY NATURE

Expenses included in cost of sales, selling and marketing costs and administrative expenses are analysed as follows:

	2007	2006
Depreciation and amortisation expenses (<i>Notes 6 and 7</i>)	44,240	49,646
Employee benefit expenses (<i>Note 19</i>)	173,221	149,056
Changes in inventories of finished goods and work in progress	(91,023)	61,363
Raw materials and consumables used	2,491,099	3,065,667
Impairment provision for receivables	266	–
Written down/(reversal) of inventories to net realisable value (<i>Note 9</i>)	27,908	(4,952)
Provision for warranty (<i>Note 16</i>)	64,437	21,089
Operating lease expenses on property and machinery	25,791	14,860
Research and development costs	49,071	34,667
Auditors' remuneration	1,890	1,247
	<u>173,221</u>	<u>149,056</u>

19. EMPLOYEE BENEFIT EXPENSE

	2007	2006
Basic salaries, allowances and benefits in kind	156,359	137,000
Contributions to retirement schemes (<i>Note (a) and (b)</i>)	15,125	8,402
Share-based compensation (<i>Note 13(c)</i>)	1,737	3,654
	<u>173,221</u>	<u>149,056</u>

- (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 expensed as incurred.
- (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% (2006: 8%) of the basis salaries of employees in the PRC.

20. DIRECTORS' AND SENIOR MANAGEMENT'S EMOLUMENTS**(a) Directors' emoluments**

The remuneration of every director for the year ended 31 December 2007 is set out below:

Name of Director	Fees	Salaries, allowance and benefits in kind	Employer's contribution to pension scheme	Share- based payment	Total
Mr. Chen Zhaoxiong*	—	—	—	—	—
Mr. Tong Baoan	500	—	—	333	833
Mr. Fan Qingwu	—	400	49	315	764
Mr. Hua Longxing	—	526	—	315	841
Mr. Chan Kay Cheung	180	—	—	—	180
Mr. Wong Po Yan	180	—	—	—	180
Mr. Yin Yongli	180	—	—	—	180
	<u>1,040</u>	<u>926</u>	<u>49</u>	<u>963</u>	<u>2,978</u>

During the year, no director has waived emolument or has agreed to waived the directors' emoluments (2006: nil).

* Resigned on 14 January 2008

The remuneration of every director for the year ended 31 December 2006 is set out below:

Name of Director	Fees	Salaries, allowance and benefits in kind	Employer's contribution to pension scheme	Share- based payment	Total
Mr. Chen Zhaoxiong	—	—	—	—	—
Mr. Yang Xiaotang	167	—	8	—	175
Mr. Tong Baoan	500	—	19	960	1,479
Mr. Fan Qingwu	—	400	20	909	1,329
Mr. Hua Longxing	—	404	—	909	1,313
Mr. Chan Kay Cheung	180	—	—	—	180
Mr. Wong Po Yan	180	—	—	—	180
Mr. Yin Yongli	180	—	—	—	180
	<u>1,207</u>	<u>804</u>	<u>47</u>	<u>2,778</u>	<u>4,836</u>

(b) Five highest paid individuals

The emoluments payable to the five individuals (2006: three individuals, and two directors whose emoluments are reflected in the analysis presented above) whose emoluments were the highest in the Group during the year are as follows:

	2007	2006
Basic salaries, allowances and benefits in kind	12,434	4,064
Bonuses	2,192	1,194
Contributions to retirement schemes	460	179
Share-based compensation (<i>Note 13(c)</i>)	109	315
	<u>15,195</u>	<u>5,752</u>

(c) The emoluments fell within the following band:

	Number of individuals	
	2007	2006
HK\$1,000,001 – HK\$1,500,000	1	1
HK\$1,500,001 – HK\$2,000,000	–	–
HK\$2,000,001 – HK\$2,500,000	2	2
HK\$2,500,001 – HK\$3,000,000	–	–
HK\$3,000,001 – HK\$3,500,000	–	–
HK\$3,500,001 – HK\$4,000,000	1	–
HK\$4,000,001 – HK\$4,500,000	–	–
HK\$4,500,001 – HK\$5,000,000	–	–
HK\$5,000,001 – HK\$5,500,000	1	–
	<u>5</u>	<u>3</u>

21. FINANCE INCOME – NET

	2007	2006
Interest income on short-term deposits	11,442	8,109
Interest on bank loans	<u>(9,075)</u>	<u>(6,444)</u>
Net finance income	<u>2,367</u>	<u>1,665</u>

22. TAXATION

(a) Income tax (credit)/expense

The amount of taxation (credited)/charged to the consolidated income statement represents:

	2007	2006
Current taxation – PRC enterprise income tax	6,135	6,760
Deferred taxation	(37,775)	(4,402)
	<u>(31,640)</u>	<u>2,358</u>

(b) No provision for Hong Kong profits tax has been made as the Group has no assessable profit for the year (2006: nil).

(c) The principal subsidiary, Sang Fei, is a foreign investment production enterprise established in Shenzhen Special Economic Zone in the PRC, the prevailing PRC enterprise income tax rate is 15%. As approved by the tax authorities in 1998, Sang Fei is entitled to exemption from income tax 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. Accordingly, the tax holiday ended at 31 December 2004.

Sang Fei was certified as a high-tech enterprise from 2002 and as approved by the tax authorities in 2004, Sang Fei is entitled to 50% tax reduction from enterprise income tax for further three years starting from 2005. Consequently, enterprise income tax has been provided at the rate of 7.5% (2006: 7.5%) for the year. Such tax reduction ended at 31 December 2007.

(d) 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:

	2007	2006
(Loss)/profit before income tax	<u>(19,117)</u>	<u>71,517</u>
Calculated at a taxation rate of 15% (2006: 15%)	(2,868)	10,728
Effect of tax concession	(406)	(9,804)
Expenses not deductible for taxation purposes	136	313
Tax losses for which no deferred income tax asset was recognised	266	1,121
Effect on change of tax rate (<i>Note (e)</i>)	<u>(28,768)</u>	<u>–</u>
Income tax (credit)/expense	<u>(31,640)</u>	<u>2,358</u>

(e) Deferred taxation

The movement on the deferred tax assets during the year is as follows:

	Impairment of inventories	Accelerated depreciation of property, plant and equipment	Provision for warranty and other accruals	Others	Total
At 1 January 2006	2,939	540	158	877	4,514
(Charged)/credited to the income statement	<u>(405)</u>	<u>4,177</u>	<u>790</u>	<u>(160)</u>	<u>4,402</u>
At 31 December 2006	<u>2,534</u>	<u>4,717</u>	<u>948</u>	<u>717</u>	<u>8,916</u>
At 1 January 2007	2,534	4,717	948	717	8,916
Credited/(charged) to the income statement	<u>9,028</u>	<u>8,314</u>	<u>21,150</u>	<u>(717)</u>	<u>37,775</u>
At 31 December 2007	<u>11,562</u>	<u>13,031</u>	<u>22,098</u>	<u>–</u>	<u>46,691</u>

The amounts shown in the balance sheet include the following:

	2007	2006
Deferred tax assets to be recovered after more than 12 months	10,879	7,251
Deferred tax assets to be recovered within 12 months	<u>35,812</u>	<u>1,665</u>
	<u>46,691</u>	<u>8,916</u>

Deferred income tax assets are recognised for tax loss carrying-forwards to the extent that the realisation of the related tax benefit through the future taxable profits is probable. The Group did not recognise deferred income tax assets of HK\$4,250,000 (2006: HK\$3,984,000) in respect of losses amounted to HK\$23,210,000 (2006: HK\$22,184,000) that can be carried forward against future taxable income.

On 16 March 2007, the Corporate Income Tax Law of the PRC (the “new CIT Law”) was approved and became effective 1 January 2008. In accordance with the new CIT law, Sang Fei’s applicable tax rate will be changed to 25% with a transitional period of 5 years from 2008 in which the tax rate will be changed to 18%, 20%, 22%, 24% and 25% for the five years from 2008 to 2012 respectively. In this regard, the new applicable tax rates are adopted in computing the deferred taxation as at 31 December 2007 (31 December 2006: 7.5%). The change of tax rates resulted a tax credit of HK\$28,768,000 in 2007.

23. PROFIT ATTRIBUTABLE TO EQUITY HOLDERS OF THE COMPANY

The profit attributable to equity holders of the Company is dealt with the financial statements of the Company to the extent of the HK\$40,985,000 (2006: HK\$58,692,000).

24. EARNINGS PER SHARE**(a) Basic earnings per share**

The calculation of the basic earnings per share is based on the Group's profit attributable to equity holders of the Company for the year ended 31 December 2007 of HK\$8,074,000 (2006: HK\$43,276,000) and the 1,083,560,000 (2006: 1,083,560,000) ordinary shares in issue during the year.

(b) Diluted earnings per share

Diluted earnings per share for the year ended 31 December 2007 is calculated by adjusting the number of 1,083,560,000 ordinary shares by adding 6,405,096 to assume conversion of all dilutive potential ordinary shares granted under the Share Option Scheme of the Company. A calculation is done to determine the number of shares that could have been acquired at fair value (determine as the average market price during the year) based on the monetary value of subscription rights attached to outstanding share options as following:

Profit attributable to equity holders of the Company (<i>HK\$</i>)	8,074,000
Weighted average number of shares outstanding	1,083,560,000
Weighted average number of shares under Share Option Scheme	15,712,500
Weighted average number of shares that would have been issued at average market price	(9,307,404)
Weighted average number of ordinary shares in issue on fully diluted basis	1,089,965,096
Diluted earnings per share (<i>HK\$</i>)	0.0074

For the year ended 31 December 2006, potential diluted ordinary shares were not included in the calculation of diluted earnings per share because they were anti-dilutive.

25. DIVIDENDS

2006 final dividend of HK\$0.016 (2005 final: HK\$0.02) per ordinary share totalling HK\$17,337,000 (2005 final: HK\$21,671,000) was declared in March 2007 and paid in June 2007.

The Board does not recommend the payment of a dividend for the year ended 31 December 2007 (2006: HK\$0.016 per share).

26. CASH GENERATED FROM OPERATIONS

	2007	2006
(Loss)/profit before income tax	(19,117)	71,517
Adjustment for:		
Depreciation of owned property, plant and equipment	38,725	45,324
Amortisation of intangible assets	5,515	4,322
(Gain)/loss on disposal of property, plant and equipment	(337)	6
Interest income	(11,442)	(8,109)
Interest expense	9,075	6,444
Share-based compensation	1,737	3,654
Effect of foreign exchange translation	18,156	6,844
	<u> </u>	<u> </u>
Changes in working capital		
Inventories	(108,387)	111,232
Trade and other receivables	(383,745)	591,765
Trade and other payables	22,386	(411,368)
Provision for warranty	64,626	10,528
	<u> </u>	<u> </u>
Net cash (used in)/generated from operations	<u>(362,808)</u>	<u>432,159</u>

(a) Proceeds from disposal of property, plant and equipment include:

	2007	2006
Net book value (<i>Note 6</i>)	803	48
Gain/(loss) on disposal of property, plant and equipment	337	(6)
	<u> </u>	<u> </u>
Cash proceeds from disposal of property, plant and equipment	<u>1,140</u>	<u>42</u>

27. COMMITMENTS**(a) Capital commitments – Group**

At 31 December 2007, the Group's capital commitment which were contracted but not provided for were as follows:

	2007	2006
Purchase of property, plant and equipment and computer software	2,502	1,259
	<u> </u>	<u> </u>

(b) Operating lease commitments

As at 31 December 2007, the Group had future aggregate minimum lease payments under non-cancellable operating leases for factories and office premises as follows:

	Group		Company	
	2007	2006	2007	2006
Not later than one year	30,612	26,218	343	651
In the second to fifth years	21,901	19,774	344	–
	<u> </u>	<u> </u>	<u> </u>	<u> </u>
	52,513	45,992	687	651
	<u> </u>	<u> </u>	<u> </u>	<u> </u>

28. CONTINGENT LIABILITY

The Group did not have any material contingent liabilities outstanding as at 31 December 2007 (2006: nil).

29. RELATED-PARTY TRANSACTIONS AND BALANCES

Parties are considered to be related if one company has the ability, directly or indirectly, to control the other company or exercise significant influence over the other party in making financial and operating decisions. Parties are also considered to be related if they are subject to common control or common significant influence.

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

- China Electronics Corporation, 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.

In March 2007, KPE disposed of its equity interests, through its subsidiary in Sang Fei to Shenzhen SED Electronics Group Co., Ltd., a subsidiary of China Electronics Corporation and ceased its significant influence on Sang Fei. From then onward, KPE and the companies under its common control are not the Group’s related parties. Consequently, the Group’s transactions with them since 1 April 2007 and the balances with them as at 31 December 2007 are not disclosed as related party transactions and balances.

(a) Sales of products, samples and materials:

		2007	2006
Sales of products:			
Philips (China) Investment Co., Ltd	#	207,345	1,561,368
Philips Electronics Singapore Pte. Ltd.	#	171,609	1,014,335
Philips Electronics Hong Kong Ltd.	#	67,253	273,944
Shenzhen SED Coalition Electronics Co., Ltd.	*	330,310	2,448
Philips Consumer Electronics B.V.	#	156	949
Philips France S.A.S.	#	–	2,175
Philips Electronics Trading Services (Shanghai) Co., Ltd.	#	–	1,241
Shenzhen SED Electronics Sales Corporation	*	8,136	–
Shenzhen SED Electronics Group Company Ltd	*	51	–
Shanghai SED ARC Co., Ltd.	*	8	–
China Electronic Appliance Corporation	*	78,033	–
		<u>207</u>	<u>2006</u>

		2007	2006
Sales of samples and materials:			
Philips Consumer Electronics B.V.	#	336	4,353
Philips (China) Investment Co., Ltd.	#	311	34,494
Philips Electronics Singapore Pte Ltd.	#	660	950
Philips Electronics Hong Kong Ltd.	#	81	682
Shenzhen SED Coalition Electronics Co., Ltd.	*	40	860
Shenzhen Sang Da Baili Electronics Co., Ltd.	*	1,822	407
Shenzhen SED International Electronic Device Co., Ltd.	*	–	713
Shenzhen SED Electronics Sales Corporation	*	64	–
Philips Group, others	#	–	24
		<u>2007</u>	<u>2006</u>

Sales of maintenance services:

Philips (China) Investment Co., Ltd	#	3,158	25,338
		<u>2007</u>	<u>2006</u>

Members of KPE and its subsidiaries (the “Philips Group”) and members of CEC and its group companies (the “CEC Group”) are the major customers of the Group.

(b) Other transactions

		2007	2006
Receipt of interests:			
China Electronics Corporation Finance Co., Ltd.	*	—	214
		<u> </u>	<u> </u>
Purchase of goods:	(i)		
Philips Electronics Hong Kong Ltd.	#	288	214,168
Philips (China) Investment Co., Ltd.	#	559	1,085
Philips France S.A.S.	#	—	2,531
Philips Electronics Trading Services (Shanghai) Co., Ltd.	#	—	946
Philips Electronics Beijing Co., Ltd.	#	—	646
Shenzhen SED Electronics Sales Corporation	*	867	—
Shenzhen Sang Da Baili Electronics Co., Ltd.	*	75,726	20,895
SED (Hong Kong) Company Limited	*	44,178	—
CEC Group, others	*	—	638
Philips Group, others	#	—	42
		<u> </u>	<u> </u>
Processing services:	(ii)		
Shenzhen Sang Da Baili Electronics Co., Ltd.	*	6,532	6,645
Shenzhen SED Industry Co., Ltd.	*	4,379	4,898
		<u> </u>	<u> </u>
Fitment and decoration services:	(iii)		
Shenzhen SED Fitment & Decoration Co., Ltd.	*	221	1,820
		<u> </u>	<u> </u>
Canteen services:	(iv)		
Shenzhen Sang Da Baili Electronics Co., Ltd.	*	11,899	10,918
		<u> </u>	<u> </u>
Repair and maintenance services:	(v)		
Shenzhen SED Coalition Electronics Co., Ltd.	*	26	—
Shanghai SED ARC Co., Ltd.	*	1,321	2,144
Shenzhen SED ARC Co., Ltd.	*	11,088	628
		<u> </u>	<u> </u>
Rental:	(vi)		
Shenzhen SED Industry Co., Ltd.	*	8,018	7,473
China Great Wall Computer Shenzhen Co., Ltd.	*	1,762	493
Great Wall Technology Company Limited	*	1,250	655
		<u> </u>	<u> </u>
Licence fee:	(vii)		
Shenzhen SED Electronics Group Co., Ltd	*	14,063	—
		<u> </u>	<u> </u>
Comprehensive services:	(viii)		
P-Marshall Hong Kong Limited	*	26,910	—
P-Marshall Singapore Pte. Limited	*	13,149	—
		<u> </u>	<u> </u>

- (i) Members of the Philips Group are the suppliers of raw materials. Purchases of raw materials from the Philips Group 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 goods from the CEC Group were carried out in the ordinary course of business and on commercial terms and conditions.

- (ii) The Group secured dedicated processing services of surface mount assembly production lines from members of the CEC Group. The processing services were carried out on commercial terms and conditions.
- (iii) 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 carried out in the ordinary course of business and were on commercial terms and conditions.
- (iv) Shenzhen Sang Da Baili Electronics Co., Ltd. provides canteen services to the production staff of the Group. The fee of the canteen services were calculated by reference to actual consumption and an agreed fixed premium and were carried out on commercial terms and conditions.
- (v) The Group engaged Shenzhen SED ARC Co., Ltd. and Shanghai SED ARC Co., Ltd. for after sales product repair services in respect of its own-branded products. The repair and maintenance services were carried out on commercial terms and conditions.
- (vi) 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.
- (vii) Members of the CEC Group licence the "Xenium" trademark to the Group for use. The licensing were based on the licence agreement and were carried out on normal commercial terms and conditions with reference to market rates.
- (viii) The Group engaged members of the CEC Group to provide various business support services in relation to sales of products. The business support services were based on the comprehensive services agreements and were carried out on normal commercial terms and conditions with reference to market rates.

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

		2007	2006
Trade receivables due from related parties:			
Philips Electronics Singapore Pte. Ltd.	#, (i)	–	223,114
Philips (China) Investment Co., Ltd.	#, (i)	–	93,525
Philips Electronics Hong Kong Ltd.	#, (i)	–	35,407
Philips Electronics Trading Services (Shanghai) Co., Ltd.	#, (i)	–	551
Shenzhen SED Coalition Electronics Co., Ltd.	*	5,503	–
Shenzhen SED Electronics Sales Corporation	*	737	–
Shenzhen Sang Da Baili Electronics Co., Ltd.	*	695	–
China Electronic Appliance Corporation	*	24,483	–
		<u>31,418</u>	<u>352,597</u>

		2007	2006
Other receivables due from related parties:			
Philips Electronics Hong Kong Ltd.	#, (i)	–	11,621
Philips (China) Investment Co., Ltd.	#, (i)	–	10,035
Philips Consumer Electronics B.V	#, (i)	–	1,867
Philips France S.A.S.	#, (i)	–	164
Philips Electronics Singapore Pte. Ltd.	#, (i)	–	139
Shenzhen SED Coalition Electronics Co., Ltd.	*	23	–
Shenzhen SED Electronics Sales Corporation	*	16	–
Shenzhen SED International			
Electronic Device Co., Ltd.	*	141	101
Shenzhen SED Electronics Group Company Ltd.	*	6,667	–
Shenzhen Sang Da Baili Electronics Co., Ltd.	*	244	99
		<u>7,091</u>	<u>24,026</u>
Prepayments:			
Shenzhen Sang Da Baili Electronics Co., Ltd.	*	15,411	6,205
SED (Hong Kong) Company Limited	*	7,385	–
		<u>22,796</u>	<u>6,205</u>
Trade and other receivables due from related parties in total (<i>Note 10</i>)			
		<u>61,305</u>	<u>382,828</u>
Trade payables due to related parties:			
Philips Electronics Hong Kong Ltd.	#, (i)	–	16,263
Philips (China) Investment Co., Ltd.	#, (i)	–	6,223
Philips France S.A.S.	#, (i)	–	4,248
Philips Electronics Singapore Pte. Ltd.	#, (i)	–	287
Philips Electronics (Beijing) Co., Ltd.	#, (i)	–	180
Philips Electronics Trading			
Services (Shanghai) Co., Ltd.	#, (i)	–	22
Shenzhen SED Electronics Sales Corporation	*	150	–
SED (Hong Kong) Company Limited	*	2,283	–
Shenzhen Sang Da Baili Electronics Co., Ltd.	*	11	1,823
Langfang CEC Dacheng Electronic Co., Ltd.	*	–	14
		<u>2,444</u>	<u>29,060</u>

		2007	2006
Other payables due to related parties:			
Philips France S.A.S.	#, (i)	–	6,244
Philips Electronics Hong Kong Ltd.	#, (i)	–	6,197
Philips Electronics Singapore Pte. Ltd.	#, (i)	–	2,408
Philips (China) Investment Co., Ltd.	#, (i)	–	399
Philips Electronics Trading Services (Shanghai) Co., Ltd.	#, (i)	–	285
Shenzhen Sang Da Baili Electronics Co., Ltd.	*	461	998
Shenzhen SED ARC Co., Ltd.	*	864	448
Shanghai SED ARC Co., Ltd.	*	7	–
Shenzhen SED Fitment and Decoration Co., Ltd.	*	–	93
		<u>1,332</u>	<u>17,072</u>
Advance from customers:			
China Electronic Appliance Corporation	*	10,753	–
Shenzhen SED Electronics Group Company Ltd.	*	261	–
Shenzhen SED Electronics Sales Corporation	*	2,158	–
Shanghai SED ARC Co., Ltd.	*	102	–
Shenzhen SED Coalition Electronics Co., Ltd.	*	784	2,027
		<u>14,058</u>	<u>2,027</u>
Trade and other payables due to related parties in total (<i>Note 14</i>)		<u>17,834</u>	<u>48,159</u>
Deposits:			
China Electronics Corporation Finance Co., Ltd.	*	–	51,595

- (i) As detailed above, KPE and the companies under its common control are not the Group's related parties since 1 April 2007. Consequently, the balances with them as at 31 December 2007 are not disclosed as related party balances.

(d) Additional information on other state-owned enterprises

The Company is controlled by CEC, and is ultimately controlled by Mainland China government, which also controls a significant portion of the productive assets and entities in the Mainland China. In accordance with Hong Kong Accounting Standard 24 “Related Party Disclosures” (“HKAS 24”), state-owned enterprises and their subsidiaries, other than CEC Group, are also defined as related parties of the Company (“Other State-owned Enterprises”).

(i) Summary of significant transactions with Other State-owned Enterprises

	2007	2006
Sales of products and materials	<u>428,418</u>	<u>85</u>
Purchase of materials	<u>24,431</u>	<u>–</u>
Interest income from state-owned banks	<u>9,955</u>	<u>6,982</u>
Interest expenses to state-owned banks	<u>9,075</u>	<u>6,444</u>

(ii) Summary of balances with Other State-owned Enterprises

	2007	2006
Trade receivables	<u>13,383</u>	<u>394</u>
Trade payables	<u>170</u>	<u>–</u>
Bank deposits in state-owned banks	<u>311,477</u>	<u>341,292</u>
Bank borrowings from state-owned banks	<u>394,111</u>	<u>–</u>

Balances with Other State-owned Enterprises, except for bank deposits and bank borrowings, were unsecured and interest-free.

FINANCIAL SUMMARY

Hua Da Electronics is a leading company in the design of integrated circuits established under the laws of the PRC. It is principally engaged in the design and sale of integrated circuits and the research and development of electronic design automation tools. The technologies and products of Hua Da Electronics have been widely applied in the areas of telecommunications, social security, electronic payments and consumer electronics.

The audited consolidated financial statements of Hua Da Group prepared in accordance with Hong Kong Financial Reporting Standards for the three years ended 31 December 2005, 2006 and 2007 are set out in Appendix I to this circular. Set out below are certain key financial information of Hua Da Group, as extracted from the audited consolidated financial statements of Hua Da Group:

	Year ended 31 December		
	2005	2006	2007
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Revenue	295,524	508,717	652,767
Profit before income tax	41,816	128,716	132,063
Net profit attributable to equity holders			
of Hua Da Electronics	40,352	120,202	127,443
Net assets	89,127	202,570	302,636

As shown from the above table, Hua Da Group has experienced high growth rate in both turnover and profit during the three years ended 31 December 2007. The main driver for the growth in turnover and profit is the healthy growth and expansion of Hua Da Electronics' operations, which is attributable to the strong demand in the smart cards market, in particular, the rapid growth in products such as national identification cards, telecommunications smart cards and social security cards, and effective cost reduction.

As at 31 December 2007, the total assets of Hua Da Group was approximately HK\$615,322,000, representing an approximately 148.8% increase as compared to Hua Da Group's total assets as at 31 December 2005. The increase in net assets value during the three years ended 31 December 2007 almost doubled that of the growth of total assets during the same period, which shows that Hua Da Group has better asset management and utilisation during the three years ended 31 December 2007.

CAPITAL RESOURCES AND LIQUIDITY

Hua Da Group finances its operations primarily by internal resources and short term bank borrowings. As at 31 December 2007, Hua Da Group has cash and cash equivalent amounted to approximately HK\$188,902,000, which were denominated in RMB, Hong Kong dollars and United States dollars. Hua Da Group's source of funds is mainly derived from its operating activities and increasing cash flow was generated by Hua Da Group as a result of its healthy growth and expansion of its operations.

The consolidated total liabilities of Hua Da Group as at 31 December 2007 was approximately HK\$312,686,000, all of which were accounted for as current liabilities. As at 31 December 2007, Hua Da Group had unsecured short-term bank loans of approximately HK\$64,516,000, which was denominated in RMB. The weighted average effective borrowing rate was 7.29% per annum as at 31 December 2007. Hua Da Group has fully utilised its banking facilities as at 31 December 2007. As at 31 December 2007, Hua Da Group neither pledged any assets or bank deposits nor granted any guarantee to secure banking facilities.

Hua Da Group's gearing ratio is calculated as net debt divided by total capital, whereby net debt is calculated as total borrowings less cash and cash equivalents and total capital is calculated as total equity plus net debt. As at 31 December 2007, the cash and cash equivalents balances were greater than the balances of total borrowings, thereby attributing to a negative gearing ratio. The directors of Hua Da Electronics are of the view that Hua Da Group does not have significant capital risk. Hua Da Electronics' strategy is to maintain a low gearing ratio.

Hua Da Group's business activities are primarily denominated in RMB. The directors of Hua Da Electronics are of the view that Hua Da Group has no significant concentrations of foreign exchange risk, hence it is not necessary to arrange for hedging of Hua Da Group's foreign currency investments, nor to implement a foreign currency hedge policy.

CAPITAL COMMITMENT AND CONTINGENT LIABILITIES

As at 31 December 2007, Hua Da Group did not have any capital commitments. In addition, Hua Da Group did not have any material contingent liabilities outstanding as at 31 December 2007.

EMPLOYEE AND REMUNERATION POLICIES

As at 31 December 2007, Hua Da Group had approximately 290 employees, the majority of whom were based in the PRC. Employee benefit expenses during the year ended 31 December 2007 were HK\$76,518,000, which includes basic salaries, allowances, benefits in kind and contribution to staff retirement schemes managed by local government authorities in the PRC.

Hua Da Group undertakes a review of salaries and the extent of salary increment annually, with close reference to Hua Da Group's results, the relevant labour market and economic situation. Hua Da Group also provides bonuses based upon staff performance and profits of Hua Da Group. This acts as an incentive for motivating employees to provide greater contribution to Hua Da Group.

SEGMENTAL INFORMATION

Hua Da Group operates and manages its business as a single segment. Hua Da Group also operates within one geographical segment because its revenues are generated in the PRC and its assets are located in the PRC. Accordingly, no segmental data has been prepared and presented by Hua Da Group.

EXCLUDED ASSETS

During the year ended 31 December 2005, Hua Da Electronics acquired 70% equity interests in Beijing Hua Da Xinan, a limited liability company established under the laws of the PRC and principally engaged in the development and sale of digital system software and hardware. Hua Da Electronics' equity interest in Beijing Hua Da Xinan was subsequently increased to 71.26%. On 21 May 2008, Hua Da Electronics entered into a share transaction agreement with Beijing Xu An Da Technology Co., Ltd. in relation to the disposal of 71.26% of equity interest in Beijing Hua Da Xinan for a consideration of RMB5,000,000.

In 2006, Hua Da Electronics acquired an additional 61.88% interest in Guangdong Hua Da, a limited liability company established under the laws of the PRC and principally engaged in the design and sale of integrated circuits. After such acquisition, Hua Da Electronics held a total of 99.38% equity interest in Guangdong Hua Da. Further in 2007, Hua Da Electronics acquired the remaining 0.62% equity interest in Guangdong Hua Da, whereby Guangdong Hua Da became a wholly-owned subsidiary of Hua Da Electronics as at the end of 2007. At the shareholders' meeting held on 19 March 2008, the shareholders of Hua Da Electronics approved the disposal of 80% of its equity interest in Guangdong Hua Da. As at the Latest Practicable Date, Hua Da Electronics has not entered into any share transfer agreement regarding such disposal.

In addition, pursuant to a shareholders' resolution dated 25 December 2007, Hua Da Electronics decided to deregister its wholly-owned subsidiary, CIDC, a limited liability company incorporated in Hong Kong and principally engaged in the sale of digital video and related technology. As at 31 December 2007, the deregistration process has not yet been completed.

The directors of Hua Da Electronics believe that by disposing the Excluded Assets Hua Da Electronics will be able to focus on the development of its core businesses in the future.

Hua Da Electronics will explore business opportunities to further develop its integrated circuit business. As at the Latest Practicable Date, no material investment nor capital assets acquisition opportunities have been identified yet. Should any such opportunities arise during the year, Hua Da Electronics will finance such investments or acquisitions by its capital, internal resources and/or bank borrowings.

FUTURE PROSPECTS

Hua Da Electronics has a strong presence in the integrated circuits industry. Integrated circuits have been widely applied in a wide range of areas including communications, home and personal entertainment, social and public business. The principal products of Hua Da Group includes chipset and module for smart cards, wireless local area network (WLAN) chips, and electronic design automation (EDA) tools.

Hua Da Electronics' overall business strategy is to focus on and continue to expand its core business in relation to the production of smart cards, WLAN chips and EDA tools, and to stand as a leading supplier in the domestic market of such products. It is expected that the overall market demand of smart cards will experience stable growth due to the increasing application and utilisation of smart cards within the telecommunications, transportation, financial industries and social security, as well as for personal identification purposes. Hua Da Electronics will continue to invest in the development and production of smart cards, thereby further strengthening its position as a leading smart card producer in the PRC. In addition, the WLAN market has experienced substantial growth since 2004. It is expected that the WLAN market will continue to grow rapidly as a result of the broadening of the scope and capacity of the WLAN industry, with approximately a third of WLAN related products being produced in the PRC. Hua Da Electronics had established a team dedicated for the research and development, as well as design of new WLAN products, in particular, WLAN products for handheld and portable customer electronic products such as personal digital assistants and portable electronic gaming devices. The directors of Hua Da Electronics believe this will facilitate Hua Da Group in seizing the growing opportunities within the sector. Furthermore, Hua Da Electronics intends to extend its sales and marketing efforts to existing major domestic and international customers of EDA related products by customising EDA solutions and tools to such customers, and thereby strengthening customer loyalty and increasing revenue and profits generated from these products.

A. UNAUDITED PRO FORMA CONSOLIDATED STATEMENT OF ASSETS AND LIABILITIES OF THE ENLARGED GROUP

The following is an illustrative and unaudited pro forma consolidated statement of assets and liabilities of the Enlarged Group, which has been prepared to illustrate the effect of the Acquisition.

The unaudited pro forma consolidated statement of assets and liabilities of the Enlarged Group is prepared on the basis of the notes set out below for the purpose of illustrating the effect of the Acquisition as if it has taken place on 31 December 2007.

This unaudited pro forma consolidated statement of assets and liabilities of the Enlarged Group has been prepared on the basis of the notes set out below and in a manner consistent with the accounting policies adopted by the Group. It has been prepared for illustrative purpose only and because of its hypothetical nature, it may not give a true picture of the financial position of the Enlarged Group that had the Acquisition been completed as at 31 December 2007 or at any future date.

	<u>Pro forma adjustments</u>		
	The	Target	Other pro
	Group	Group	form
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>adjustments</i>
	<i>(Audited)</i>	<i>(Audited)</i>	<i>HK\$'000</i>
	<i>(Note 1)</i>	<i>(Note 2)</i>	<i>(Note 4)</i>
			Pro forma
			Enlarged
			Group
			<i>HK\$'000</i>
ASSETS			
Non-current assets			
Property, plant and equipment	41,047	22,296	63,343
Intangible assets	16,144	5,333	21,477
Deferred income tax assets	46,691	8,865	55,556
Available for sale financial assets	—	4,300	4,300
	<u>103,882</u>	<u>40,794</u>	<u>144,676</u>
Current assets			
Inventories	444,189	158,059	602,248
Trade and other receivables	877,150	227,567	1,104,717
Cash and cash equivalents	391,741	188,902	(5,983) 574,660
	<u>1,713,080</u>	<u>574,528</u>	<u>2,281,625</u>
Total assets	<u>1,816,962</u>	<u>615,322</u>	<u>2,426,301</u>

	<u>Pro forma adjustments</u>		
	The	Target	Other pro
	Group	Group	form
	adjustments	Group	form
	Group	Group	Group
	Enlarged	Enlarged	Enlarged
	Group	Group	Group
	HK\$'000	HK\$'000	HK\$'000
	(Audited)	(Audited)	(Note 4)
	(Note 1)	(Note 2)	(Note 4)
LIABILITIES			
Current liabilities			
Trade and other payables	741,030	239,822	980,852
Current income tax liabilities	3,725	8,348	12,073
Short term bank loans	394,111	64,516	458,627
Provision for warranty	77,260	–	77,260
Total liabilities	1,216,126	312,686	1,528,812
Net assets	600,836	302,636	897,489

Notes to the unaudited pro forma consolidated statement of assets and liabilities of the Enlarged Group

1. The figures are extracted from the audited consolidated balance sheet of the Group as included in the annual report for the year ended 31 December 2007.
2. The figures are extracted from the audited consolidated balance sheet of the Target Group as set out in appendix I of this Circular.
3. Pursuant to the China Hua Da Agreement, the Beijing Shoufa Xinan Agreement and the Other Vendors Agreement, the Company has conditionally agreed to purchase the entire equity interest in Hua Da Electronics by allotting and issuing an aggregate of 608,000,000 Consideration Shares.

Hua Da Electronics is controlled by China Hua Da which is jointly owned and controlled by CEC and State Development & Investment Corp. ("SDIC"). Both CEC and SDIC are state-owned enterprises and controlled by State-owned Assets Supervision and Administration Commission. Accordingly the Company treats the Acquisition as a transaction under common control and has applied the principles of merger accounting, as prescribed in Hong Kong Accounting Guideline 5 "Merger Accounting for Common Control Combinations" issued by the Hong Kong Institute of Certified Public Accountants, in accounting for the Acquisition for the purpose of the unaudited pro forma consolidated statement of assets and liabilities of the Enlarged Group.

For the purpose of this unaudited pro forma consolidated statement of assets and liabilities, the Group treats the acquisitions of 7.5% and 27.75% equity interests in Hua Da Electronics from Beijing Shoufa Xinan and Other Vendors (the minority shareholders of Hua Da Electronics) respectively as transactions with equity owners of the Group. The difference between any consideration paid and the relevant shares acquired of the carrying value of net assets of the Target Group is recorded in equity.

4. The adjustment relates to the transaction costs, such as professional fees and printing cost, of approximately HK\$5,983,000 incurred for the Acquisition.
5. Since the carrying value of the Target Group at the date of completion of the Acquisition may be substantially different from the values used in the preparation of this unaudited pro forma consolidated statement of assets and liabilities of the Enlarged Group, the final amounts of assets and liabilities to be recognised in connection with the Acquisition will be different from the amounts stated herein.
6. No adjustments have been made to reflect any trading results or other transactions of the Group and the Target Group entered into subsequent to 31 December 2007.

B. REPORT ON THE UNAUDITED PRO FORMA CONSOLIDATED STATEMENT OF ASSETS AND LIABILITIES OF THE ENLARGED GROUP

The following is the text of a report received from PricewaterhouseCoopers, Certified Public Accountants, Hong Kong, for the purpose of incorporation in this circular.



羅兵咸永道會計師事務所

PricewaterhouseCoopers
22/F, Prince's Building
Central, Hong Kong

ACCOUNTANT'S REPORT ON UNAUDITED PRO FORMA FINANCIAL INFORMATION TO THE DIRECTORS OF CHINA ELECTRONICS CORPORATION HOLDINGS COMPANY LIMITED

We report on the unaudited pro forma financial information set out on pages 144 to 145 under the heading of “Unaudited Pro Forma Consolidated Statement of Assets and Liabilities of the Enlarged Group” (the “Unaudited Pro Forma Financial Information”) in Appendix IV of the circular dated 30 June 2008 (the “Circular”) of China Electronics Corporation Holdings Company Limited (the “Company”), in connection with the proposed acquisition of CEC Huada Electronic Design Co., Ltd. (the “Transaction”) by the Company. The Unaudited Pro Forma Financial Information has been prepared by the directors of the Company, for illustrative purposes only, to provide information about how the Transaction might have affected the relevant financial information of the Company and its subsidiaries (hereinafter collectively referred to as the “Group”). The basis of preparation of the Unaudited Pro Forma Financial Information is set out on pages 144 to 145 of the Circular.

Respective Responsibilities of Directors of the Company and the Reporting Accountant

It is the responsibility solely of the directors of the Company to prepare the Unaudited Pro Forma Financial Information in accordance with rule 4.29 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the “Listing Rules”) and Accounting Guideline 7 “Preparation of Pro Forma Financial Information for Inclusion in Investment Circulars” issued by the Hong Kong Institute of Certified Public Accountants (the “HKICPA”).

It is our responsibility to form an opinion, as required by rule 4.29(7) of the Listing Rules, on the Unaudited Pro Forma Financial Information and to report our opinion to you. We do not accept any responsibility for any reports previously given by us on any financial information used in the compilation of the Unaudited Pro Forma Financial Information beyond that owed to those to whom those reports were addressed by us at the dates of their issue.

Basis of Opinion

We conducted our engagement in accordance with Hong Kong Standard on Investment Circular Reporting Engagements 300 “Accountants’ Reports on Pro Forma Financial Information in Investment Circulars” issued by the HKICPA. Our work, which involved no independent examination of any of the underlying financial information, consisted primarily of comparing the unadjusted audited consolidated statement of assets and liabilities of the Group as at 31 December 2007 with the audited consolidated financial statements of the Group for the year ended 31 December 2007, considering the evidence supporting the adjustments and discussing the Unaudited Pro Forma Financial Information with the directors of the Company.

We planned and performed our work so as to obtain the information and explanations we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the Unaudited Pro Forma Financial Information has been properly compiled by the directors of the Company on the basis stated, that such basis is consistent with the accounting policies of the Group and that the adjustments are appropriate for the purposes of the Unaudited Pro Forma Financial Information as disclosed pursuant to rule 4.29(1) of the Listing Rules.

The Unaudited Pro Forma Financial Information is for illustrative purposes only, based on the judgements and assumptions of the directors of the Company, and, because of its hypothetical nature, does not provide any assurance or indication that any event will take place in the future and may not be indicative of the financial position of the Group as at 31 December 2007 or any future date.

Opinion

In our opinion:

- (a) the Unaudited Pro Forma Financial Information has been properly compiled by the directors of the Company on the basis stated;
- (b) such basis is consistent with the accounting policies of the Group; and
- (c) the adjustments are appropriate for the purposes of the Unaudited Pro Forma Financial Information as disclosed pursuant to rule 4.29(1) of the Listing Rules.

PricewaterhouseCoopers

Certified Public Accountants

Hong Kong, 30 June 2008

C. WORKING CAPITAL

Taking into consideration the financial resources available to the Enlarged Group, including the internally generated funds of the Enlarged Group, the banking facilities and other financial resources available to the Enlarged Group, and in the absence of unforeseen circumstances, the Directors are of the opinion that the Enlarged Group will, following completion of the Acquisition, have sufficient working capital for its present requirements, that is for at least the next 12 months from the date of this circular.

D. INDEBTEDNESS**Borrowings**

As at the close of business on 30 April 2008, being the latest practicable date for the purpose of this indebtedness statement, the Enlarged Group had outstanding unsecured short-term borrowings of approximately HK\$699.1 million.

Disclaimer

Save as aforesaid and apart from intra-group liabilities and normal trade payables, the Enlarged Group did not have, at the close of business on 30 April 2008, any mortgages, charges, debentures, debt securities issued and outstanding, and authorised or otherwise created but unissued, outstanding borrowings or indebtedness in the nature of borrowing including term loans, bank overdrafts, liabilities under acceptances, acceptance credits, hire purchase and finance lease commitments or other similar indebtedness, or any guarantees or other material contingent liabilities.

E. BANKING FACILITIES AND CAPITAL COMMITMENT

As at 30 April 2008, the Enlarged Group had undrawn borrowing facilities of approximately HK\$576.7 million.

As at 30 April 2008, the Enlarged Group has capital commitment in relation to the purchase of property, plant and equipment and computer software which were contracted but not provided for were approximately HK\$2.2 million.

1. RESPONSIBILITY STATEMENT

This circular includes particulars given in compliance with the Listing Rules for the purpose of giving information with regard to the Company. The Directors collectively and individually accept full responsibility for the accuracy of the information contained in this circular and confirm, having made all reasonable enquiries, that to the best of their knowledge and belief there are no other facts the omission of which would make any statement herein misleading.

2. SHARE CAPITAL

The authorised and issued share capital of the Company as at the Latest Practicable Date and upon completion of the Acquisition were and will be as follows:

HK\$

Authorised

<u>30,000,000,000</u>	Shares as at the Latest Practicable Date	<u>300,000,000</u>
-----------------------	--	--------------------

Issued and to be issued, fully paid or credited as fully paid

1,083,560,000	Shares in issue as at the Latest Practicable Date	10,835,600
608,000,000	Consideration Shares to be allotted and issued upon completion of the Acquisition	6,080,000
<u>1,691,560,000</u>	Shares	<u>16,915,600</u>

The Consideration Shares, when allotted and issued, will rank pari passu in all respects among themselves and with the Shares in issue on the date of allotment and issue of the Consideration Shares, including but not limited to the right to receive all dividends, distributions or entitlements declared, paid or made in respect of the Shares, the record date for which shall fall on or after the date of allotment and issue of the Consideration Shares.

3. DISCLOSURE OF INTERESTS

As at Latest Practicable Date, the following Directors and chief executive of the Company had, or were deemed to have, interests or short positions in the shares, underlying shares or debentures of the Company or any of its associated corporations (within the meaning of Part XV of the SFO) which were required to be notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests and short positions which they were deemed or taken to have under such provisions of the SFO), or which were required, pursuant to section 352 of the SFO, to be entered in the register referred to therein, or which were required, pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers contained in the Listing Rules, to be notified to the Company and the Stock Exchange.

Name of Directors	Number and description of equity derivatives	No. of underlying Shares involved in the Options	Approximate % of the issued capital of the Company
Tong Baoan	3,800,000 Options ^(Note)	3,800,000 ^(L)	0.35%
Fan Qingwu	3,600,000 Options ^(Note)	3,600,000 ^(L)	0.33%
Hua Longxing	3,600,000 Options ^(Note)	3,600,000 ^(L)	0.33%
Total		<u>11,000,000</u>	<u>1.01%</u>

^L long position

Note:

The Options were all granted on 25 October 2005 under the share option scheme approved and adopted by the Shareholders on 20 June 2002. The Options represent personal interest held by the Directors as beneficial owners. Grantees of such Options are entitled to exercise the Options at a price of HK\$1.488 per Share in the following periods:

- (i) in respect of 40% of the Options granted, from 1 November 2005 to 31 October 2008;
- (ii) in respect of a further 30% of the Options granted, from 1 November 2006 to 31 October 2009; and
- (iii) in respect of the remaining 30% of the Options granted, from 1 November 2007 to 31 October 2010.

Save as disclosed above, as at the Latest Practicable Date, none of the Directors nor the chief executive of the Company had or was deemed to have any interests or short positions in the shares, underlying shares or debentures of the Company or any of its associated corporations (within the meaning of Part XV of the SFO) which were required to be notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests and short positions which they were deemed or taken to have under such provisions of the SFO), or which were required, pursuant to section 352 of the SFO, to be entered in the register referred to therein, or which were required, pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers contained in the Listing Rules, to be notified to the Company and the Stock Exchange.

Mr. Xiong Qunli, the Chairman of the Company and a non-executive Director, is the chairman of CEC. Mr. Tong Baoan, the Vice Chairman of the Company and a non-executive Director, is a director of China Electronics Corporation (BVI) Holdings Company Limited (“CEC (BVI)”). Mr. Fan Qingwu, the Managing Director and an executive Director, is also a director of CEC (BVI). Details of the shareholding of CEC and CEC (BVI) in the Company are set out in the paragraph headed “Substantial Shareholders” in this Appendix. Save as disclosed herein, none of the Directors is a director or employee of a company which has, or is deemed to have, an interest or a short position in the Shares or underlying Shares which would fall to be disclosed to the Company under the provisions of Divisions 2 and 3 of Part XV of the SFO.

None of the Directors was materially interested in any contract or arrangement subsisting as at the Latest Practicable Date which is significant in relation to the business of the Enlarged Group taken as a whole.

Since 31 December 2007, being the date to which the latest published audited consolidated financial statements of the Group were made up, up to the Latest Practicable Date, none of the Directors nor any expert named in the paragraph headed “Qualifications of Experts” in this Appendix had any direct or indirect interest in any assets which had been acquired or disposed of by or leased to any member of the Enlarged Group, or were proposed to be acquired or disposed of by or leased to any member of the Enlarged Group.

4. SUBSTANTIAL SHAREHOLDERS

So far as is known to the Directors and the chief executive of the Company, as at the Latest Practicable Date, the following persons had, or were deemed to have, interests or short positions in the Shares or the underlying Shares which would fall to be disclosed to the Company and the Stock Exchange under the provisions of Divisions 2 and 3 of Part XV of the SFO:

Name of Shareholder	Number or attributable number of Shares held	Approximate percentage or attributable percentage of total issued share capital of the Company
CEC (BVI)	812,500,000 ^(L)	74.98%
China Hua Da	393,680,000 ^(L)	36.33%
CEC ^(Notes 1 and 2)	1,206,180,000 ^(L)	111.32%
SDIC High-Tech Investment Co., Ltd. ^(Note 2)	393,680,000 ^(L)	36.33%
The State Development and Investment Corporation ^(Note 2)	393,680,000 ^(L)	36.33%
Devon Fortune Limited (“Devon Fortune”)	71,129,358 ^(L)	6.56%
Chan Chak Shing (“Mr. Chan”)	75,254,358 ^{(L)(Note 3)}	6.95%
Wang Qinsheng	55,733,840 ^{(L)(Note 4)}	5.14%

^L long position

Notes:

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

- (2) On 20 June 2008, the Company entered into the China Hua Da Agreement with China Hua Da in relation to the acquisition of 64.75% equity interest in Hua Da Electronics for a consideration of HK\$984.20 million which shall be satisfied by the Company allotting and issuing 393,680,000 Consideration Shares at an issue price of HK\$2.50 per Consideration Share.

The equity interest of China Hua Da is contributed as to 50% by CEC and as to 50% by SDIC High-Tech Investment Co., Ltd. SDIC High-Tech Investment Co., Ltd. is a wholly-owned subsidiary of The State Development and Investment Corporation, which is a state-owned investment holding company established under the laws of the PRC. By virtue of the SFO, CEC, SDIC High-Tech Investment Co., Ltd. and The State Development and Investment Corporation are deemed to be interested in the 393,680,000 Shares (to be allotted and issued upon completion of the China Hua Da Acquisition) which China Hua Da is interested in.

- (3) These 75,254,358 Shares represent the aggregate of: (i) the family interest of Mr. Chan of 4,125,000 Shares and (ii) the corporate interest of 71,129,358 Shares held by Devon Fortune. As Mr. Chan holds 100% interest in Devon Fortune, Mr. Chan is deemed to be interested in the shares held by Devon Fortune.
- (4) On 20 June 2008, the Company entered into the Other Vendors Agreement with, among others, Ms. Wang Qinsheng, pursuant to which the Company agreed to purchase from Ms. Wang Qinsheng a 9.1668% equity interest in Hua Da Electronics for a consideration of HK\$139,334,600 which shall be satisfied by the Company allotting and issuing 55,733,840 Consideration Shares at an issue price of HK\$2.50 per Consideration Share.

So far as is known to the Directors and the chief executive of the Company, as at the Latest Practicable Date, the following corporations were, directly or indirectly, interested in 10% or more of the nominal value of any class of share capital carrying rights to vote in all circumstances at general meetings of any member of the Group:

Name of subsidiary	Name of shareholder	Interest held (%)
Sang Fei	Shenzhen SED Electronics Group Co., Ltd. ^(Note 1)	25
Sang Fei	Shenzhen SED Industry Co., Ltd. ^(Note 2)	10

Notes:

- (1) Shenzhen SED Electronics Group Co., Ltd. is a company established in the PRC and is a non wholly-owned subsidiary of CEC.
- (2) Shenzhen SED Industry Co., Ltd. is a company established in the PRC with its A shares listed on the Shenzhen Stock Exchange. Shenzhen SED Industry Co., Ltd. is indirectly owned as to approximately 42.23% by CEC as at the Latest Practicable Date.

Save as disclosed above, there is no person known to the Directors or the chief executive of the Company who, as at the Latest Practicable Date, had, or was deemed to have, an interest or short position in the Shares or the underlying Shares, which would fall to be disclosed to the Company and the Stock Exchange under the provisions of Divisions 2 and 3 of Part XV of the SFO, or who was, directly or indirectly, interested in 10% or more of the nominal value of any class of share capital carrying rights to vote in all circumstances at general meetings of any member of the Group, or any option in respect of such capital.

5. LITIGATION

As at the Latest Practicable Date, no member of the Enlarged Group was engaged in any litigation, arbitration or claim of material importance and no litigation, arbitration or claim of material importance is known to the Directors to be pending or threatened against any member of the Enlarged Group.

6. DIRECTORS' SERVICE CONTRACTS

As at the Latest Practicable Date, none of the Directors had entered into, or proposed to enter into, any service contract with the Company or any member of the Enlarged Group (excluding contracts expiring or determinable by the employer within one year without payment of compensations (other than statutory compensation)).

7. COMPETING INTEREST

Mr. Xiong Qunli, the Chairman of the Company and a non-executive Director, is the chairman of CEC.

Currently, CEC is engaging in, or having subsidiaries or associates which are engaging in, mobile handset related businesses which compete or are likely to compete, either directly or indirectly, with the business of the Group.

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

Apart from the above, none of the Directors nor his associates is or was interested in any business, apart from the Company's business, that competes or competed or is or was likely to compete, either directly or indirectly, with the Company's business.

8. MATERIAL CONTRACTS

The following contracts (not being contracts entered into in the ordinary course of business) have been entered into by members of the Enlarged Group within the two years immediately preceding the date of this circular, and are or may be material:

- (i) the China Hua Da Agreement;
- (ii) the Beijing Shoufa Xinan Agreement;
- (iii) the Other Vendors Agreement;

- (iv) the Hua Da Business Services Agreement;
- (v) the Hua Da Deposit Services Agreement;
- (vi) the Hua Da Tenancy Agreement;
- (vii) a share transaction agreement dated 20 November 2006 entered into between Guangzhou Technology Risk Investment Company Ltd. (廣州科技風險投資有限公司) as transferor and Hua Da Electronics as transferee in relation to the acquisition by Hua Da Electronics of 24.38% equity interests in Guangdong Hua Da for a consideration of RMB1,855,563.23;
- (viii) a share transfer agreement dated 21 November 2006 entered into between Mr. Dong Haoran as transferor and Hua Da Electronics as transferee in relation to the acquisition by Hua Da Electronics of 12.50% equity interest in Guangdong Hua Da for a consideration of RMB1 million;
- (ix) a share transfer agreement dated 21 November 2006 entered into between Mr. Yang Lin as transferor and Hua Da Electronics as transferee in relation to the acquisition by Hua Da Electronics of 0.62% equity interest in Guangdong Hua Da for a consideration of RMB50,000; and
- (x) a share transaction agreement dated 21 May 2008 entered into between Hua Da Electronics as transferor and Beijing Xu An Da Technology Co., Ltd. (北京訊安達科技有限公司) as transferee in relation to the disposal by Hua Da Electronics of 71.26% equity interests in Beijing Hua Da Xinan for a consideration of RMB5,000,000.

9. MATERIAL ADVERSE CHANGE

As at the Latest Practicable Date, the Directors were not aware of any material adverse change in the financial or trading position of the Group since 31 December 2007, being the date to which the latest published audited consolidated financial statements of the Group were made up.

10. QUALIFICATIONS OF EXPERTS

The following are the qualifications of the professional advisers who have given opinions or advice contained in this circular:

Names	Qualifications
Altus	a licensed corporation for types 4, 6 and 9 regulated activities under the SFO
PricewaterhouseCoopers	certified public accountants

11. CONSENTS

Altus and PricewaterhouseCoopers have given and have not withdrawn their respective written consent to the issue of this circular with the inclusion of their reports and letters, as the case may be, and references to their names in the form and context in which they respectively appear.

None of Altus nor PricewaterhouseCoopers is beneficially interested in the share capital of any member of the Group and none of them has any right (whether legally enforceable or not) to subscribe for or to nominate persons to subscribe for securities in any member of the Group.

12. PROCEDURES FOR DEMANDING A POLL AT THE SGM

In accordance with the Listing Rules, any vote taken at the SGM to approve the China Hua Da Acquisition, the Beijing Shoufa Xinan Acquisition, the Other Vendors Acquisition and the Non-exempt Continuing Connected Transactions must be taken by poll. According to bye-law 66 of the bye-laws of the Company, a resolution put to the vote of a meeting shall be decided on a show of hands unless (before or on the declaration of the result of the show of hands or on the withdrawal of any other demand for a poll) a poll is demanded:

- (a) by the chairman of such meeting; or
- (b) by at least three Shareholders present in person (or, in the case of a Shareholder being a corporation, by its duly authorised representative) or by proxy for the time being entitled to vote at the meeting; or
- (c) any Shareholder or Shareholders present in person (or, in the case of a Shareholder being a corporation, by its duly authorised representative) or by proxy and representing not less than one-tenth of the total voting rights of all Shareholders having the right to vote at the meeting; or
- (d) any Shareholder or Shareholders present in person (or, in the case of a Shareholder being a corporation, by its duly authorised representative) or by proxy and holding shares in the Company conferring a right to vote at the meeting being shares on which an aggregate sum has been paid up equal to not less than one-tenth of the total sum paid up on all the shares conferring that right.

A poll shall be taken in such manner (including the use of ballot or voting papers or tickets) and either forthwith or at such time (being not later than thirty (30) days after the date of the demand) and place as the chairman of the SGM directs. On a poll, votes may be given either personally or by proxy and every Shareholder present in person or by proxy (or, in the case of a Shareholder being a corporation, by its duly authorised representative) shall have one vote for every fully paid Share of which he is the holder. The result of such poll shall be deemed to be the resolution of the meeting at which the poll was demanded.

13. MISCELLANEOUS

- (a) The qualified accountant of the Company appointed pursuant to Rule 3.24 of the Listing Rules and the company secretary of the Company is Mr. Yam Pui Hung, Robert. 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.
- (b) The registered office of the Company is at Clarendon House, 2 Church Street, Hamilton HM 11, Bermuda. The principal place of business of the Company in Hong Kong is at Room 3503, 35th Floor, China Resources Building, 26 Harbour Road, Wanchai, Hong Kong.
- (c) Tricor Abacus Limited, the Company's branch share registrar in Hong Kong, is at 26th Floor, Tesbury Centre, 28 Queen's Road East, Hong Kong.
- (d) The English text of this circular and form of proxy shall prevail over the Chinese text.

14. DOCUMENTS AVAILABLE FOR INSPECTION

Copies of the following documents will be available for inspection at Linklaters, 10th Floor, Alexandra House, Chater Road, Hong Kong during normal business hours on any business day from the date of this circular up to and including 21 July 2008 and at the SGM:

- (a) the China Hua Da Agreement;
- (b) the Beijing Shoufa Xinan Agreement;
- (c) the Other Vendors Agreement;
- (d) the Business Services Agreement;
- (e) the Deposit Services Agreement;
- (f) the Sang Da Tenancy Agreement;
- (g) the Great Wall Tenancy Agreement;
- (h) the memorandum and articles of association of the Company;
- (i) the letter of recommendation from the Independent Board Committee to the Independent Shareholders, the text of which is set out on pages 34 to 35 of this circular;
- (j) the letter of advice from Altus to the Independent Board Committee and the Independent Shareholders, the text of which is set out on pages 36 to 53 of this circular;

- (k) the consent letters from Altus and PricewaterhouseCoopers referred to in the paragraph headed “Consents” in this Appendix;
- (l) the accountant’s report of Target Group from PricewaterhouseCoopers, the text of which is set out in Appendix I to this circular;
- (m) the report from PricewaterhouseCoopers on the unaudited pro forma financial information of the Enlarged Group, the text of which is set out in Appendix IV to this circular;
- (n) the audited consolidated financial statements of the Group for each of the years ended 31 December 2005, 2006 and 2007; and
- (o) the material contracts referred to in the paragraph headed “Material Contracts” in this Appendix.



CHINA ELECTRONICS CORPORATION HOLDINGS COMPANY LIMITED

中國電子集團控股有限公司*

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

(Stock Code: 00085)

NOTICE OF SPECIAL GENERAL MEETING

NOTICE IS HEREBY GIVEN that a special general meeting of the shareholders of China Electronics Corporation Holdings Company Limited (the “**Company**”) will be held at Plaza I-III, Lower Lobby, Novotel Century Hong Kong, 238 Jaffe Road, Wanchai, Hong Kong on Monday, 21 July 2008 at 3:00 p.m. for the purpose of considering and, if thought fit, passing, with or without modifications, the following resolutions as ordinary resolutions:

ORDINARY RESOLUTIONS

1. **“THAT** the conditional equity transfer agreement dated 20 June 2008 and entered into between the Company as purchaser and 中國華大集成電路設計集團有限公司 (China Huada Integrated Circuit Design (Group) Co., Ltd.) (“**China Hua Da**”) as vendor (the “**China Hua Da Agreement**”, a copy of which has been initialled by the chairman of this meeting and for the purpose of identification marked “**A**”), pursuant to which the Company has agreed to purchase, and China Hua Da has agreed to sell, a 64.75% equity interest of 北京中電華大電子設計有限責任公司 (CEC Huada Electronic Design Co., Ltd.) (“**Hua Da Electronics**”) at a consideration of HK\$984.20 million, which consideration shall be satisfied by the allotment and issue of 393,680,000 new shares (the “**China Hua Da Consideration Shares**” and each a “**China Hua Da Consideration Share**”) of HK\$0.01 each in the share capital of the Company, credited as fully paid, at an issue price of HK\$2.50 per China Hua Da Consideration Share to China Hua Da and that such China Hua Da Consideration Shares shall, when allotted and issued, rank pari passu in all respects with all other shares of the Company in issue as at the date of such allotment and issue, be and is hereby generally and unconditionally approved and any one director of the Company be and is hereby authorised to do all such further acts and things and execute all such further documents and take all such steps which he considers necessary, desirable or expedient to implement and/or give effect to the terms of the China Hua Da Agreement and the transactions contemplated thereunder.”

* For identification purpose only

2. “**THAT** the conditional equity transfer agreement dated 20 June 2008 and entered into between the Company as purchaser and 北京首發信安數據系統科技有限公司 (Beijing Shoufa Xinan Data System Technology Company Limited) (“**Beijing Shoufa Xinan**”) as vendor (the “**Beijing Shoufa Xinan Agreement**”, a copy of which has been initialled by the chairman of this meeting and for the purpose of identification marked “**B**”), pursuant to which the Company has agreed to purchase, and Beijing Shoufa Xinan has agreed to sell, a 7.50% equity interest of Hua Da Electronics at a consideration of HK\$114 million, which consideration shall be satisfied by the allotment and issue of 45,600,000 new shares (the “**Beijing Shoufa Xinan Consideration Shares**” and each a “**Beijing Shoufa Xinan Consideration Share**”) of HK\$0.01 each in the share capital of the Company, credited as fully paid, at an issue price of HK\$2.50 per Beijing Shoufa Xinan Consideration Share to Beijing Shoufa Xinan and that such Beijing Shoufa Xinan Consideration Shares shall, when allotted and issued, rank pari passu in all respects with all other shares of the Company in issue as at the date of such allotment and issue, be and is hereby generally and unconditionally approved and any one director of the Company be and is hereby authorised to do all such further acts and things and execute all such further documents and take all such steps which he considers necessary, desirable or expedient to implement and/or give effect to the terms of the Beijing Shoufa Xinan Agreement and the transactions contemplated thereunder.”
3. “**THAT** the conditional equity transfer agreement dated 20 June 2008 and entered into between the Company as purchaser and Wang Qinsheng, Liu Weiping, Dong Haoran, Huang Guoyong, Sun Xiaonian, Cheng Jinge, Xiao Gang and Jiang Shiping (collectively the “**Other Vendors**”) as vendors (the “**Other Vendors Agreement**”, a copy of which has been initialled by the chairman of this meeting and for the purpose of identification marked “**C**”), pursuant to which the Company has agreed to purchase, and the Other Vendors has agreed to sell, an aggregate of 27.75% equity interest of Hua Da Electronics at an aggregate consideration of HK\$421.80 million, which consideration shall be satisfied by the allotment and issue of an aggregate of 168,720,000 new shares (the “**Other Vendors Consideration Shares**” and each a “**Other Vendors Consideration Share**”) of HK\$0.01 each in the share capital of the Company, credited as fully paid, at an issue price of HK\$2.50 per Other Vendors Consideration Share to the Other Vendors in accordance with the terms of the Other Vendors Agreement and that such Other Vendors Consideration Shares shall, when allotted and issued, rank pari passu in all respects with all other shares of the Company in issue as at the date of such allotment and issue, be and is hereby generally and unconditionally approved and any one director of the Company be and is hereby authorised to do all such further acts and things and execute all such further documents and take all such steps which he considers necessary, desirable or expedient to implement and/or give effect to the terms of the Other Vendors Agreement and the transactions contemplated thereunder.”

NOTICE OF THE SGM

4. “**THAT** the continuing connected transactions contemplated under the business services agreement dated 20 June 2008 and entered into between Hua Da Electronics and 中國電子信息產業集團公司 (China Electronics Corporation), a copy of which has been initialled by the chairman of this meeting and for the purpose of identification marked “**D**”, and the proposed annual caps be and are hereby generally and unconditionally approved and any one director of the Company be and is hereby authorised to do all such further acts and things and execute all such further documents and take all such steps which he considers necessary, desirable or expedient to implement and/or give effect to the terms of the continuing connected transactions contemplated thereunder.”

By Order of the Board
China Electronics Corporation Holdings Company Limited
Yam Pui Hung, Robert
Company Secretary

Hong Kong, 30 June 2008

Registered office:

Clarendon House
2 Church Street
Hamilton HM 11
Bermuda

Principal place of business in Hong Kong:

Room 3503, 35th Floor
China Resources Building
26 Harbour Road
Wanchai
Hong Kong

Notes:

1. Any shareholder of the Company entitled to attend and vote at the meeting convened by the above notice is entitled to appoint another person as his proxy to attend and vote instead of him. A shareholder who is the holder of two or more shares may appoint more than one proxy to represent him and vote on his behalf at the meeting. A proxy need not be a shareholder of the Company but must be present in person at the meeting to represent the shareholder. If more than one proxy is so appointed, the appointment shall specify the number and class of shares in respect of which each such proxy is so appointed.
2. A form of proxy for use at the meeting is enclosed. In order to be valid, the form of proxy must be duly completed and signed in accordance with the instructions printed thereon and returned together with the power of attorney or other authority, if any, under which it is signed, or a certified copy of such power or authority, to the Company's branch share registrar in Hong Kong, Tricor Abacus Limited at 26th Floor, Tesbury Centre, 28 Queen's Road East, Wanchai, Hong Kong not less than 48 hours before the time appointed for holding the meeting or any adjournment thereof. Completion and return of a form of proxy will not preclude a shareholder from attending in person and voting at the meeting or any adjournment thereof, should he so wish.
3. In the case of joint holders of any shares, any one of such holders may vote at the meeting, either personally or by proxy, in respect of such shares as if he were solely entitled thereto, but if more than one of such joint holders are present at the meeting personally or by proxy, that one of the said persons so present whose name stands first in the register of members of the Company in respect of such shares shall alone be entitled to vote in respect thereof.
4. In accordance with the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited, voting on the above ordinary resolutions will be taken by poll.