

ANNUAL REPORT

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VARITRONIX INTERNATIONAL LIMITED

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Board of Directors

Dr Chang Chu Cheng, *Chairman*

Dr Yan Sze Kwan

Chung Shun Ming

Kwok Siu Kwan

James Lee Goon Nam*

Professor Charles Kao Kuen**

Anthony Lui Chi Shing**

* *Non-Executive Directors*

** *Independent Non-Executive Directors*

Secretary

Peter Lo Chi Lik

Solicitors

Woo, Kwan, Lee & Lo

Auditors

KPMG

Bankers

HSBC Republic Bank (Suisse) SA

Citibank, N.A.

Standard Chartered Bank

Shanghai Commercial Bank Limited

Registered Office

Clarendon House

Church Street

Hamilton HM11

Bermuda

Head Office and Principal

Place of Business

22 Chun Cheong Street

Tseung Kwan O Industrial Estate

Tseung Kwan O

Hong Kong

Principal Registrar

Butterfield Corporate Services Limited

Rosebank Centre

14 Bermudiana Road

Hamilton

Bermuda

Hong Kong Branch Shares Registrar

Computershare Hong Kong Investor

Services Limited

19th Floor, Hopewell Centre

183 Queen's Road East

Hong Kong

ADR Depositary

The Bank of New York

American Depositary Receipts

101 Barclay Street, 22W

New York, NY 10286

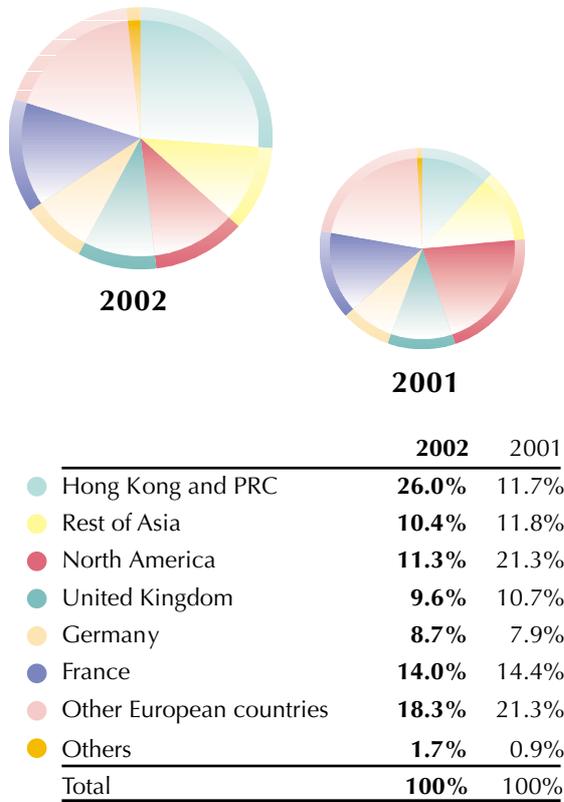
USA

Web Site

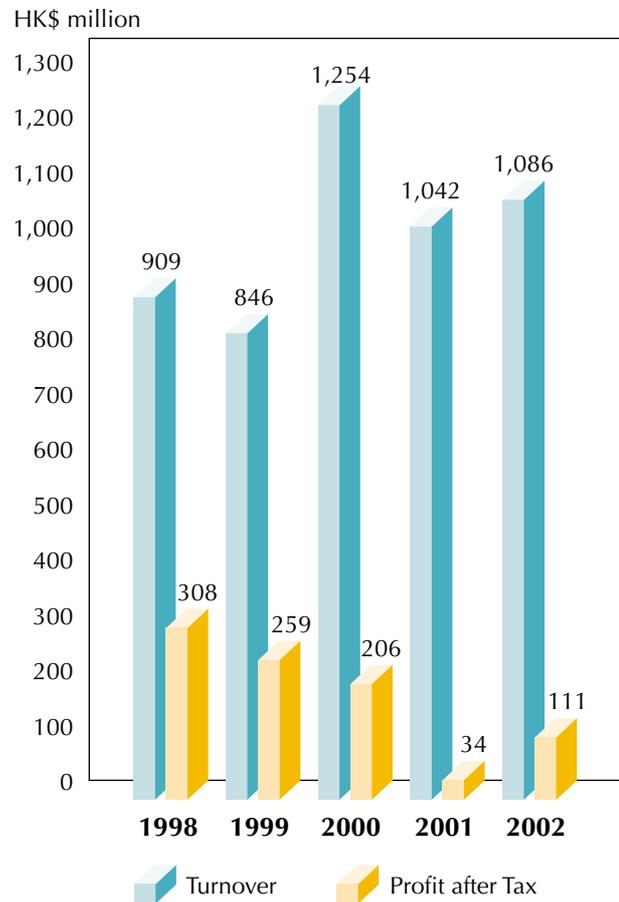
<http://www.varitronix.com>

FINANCIAL HIGHLIGHTS

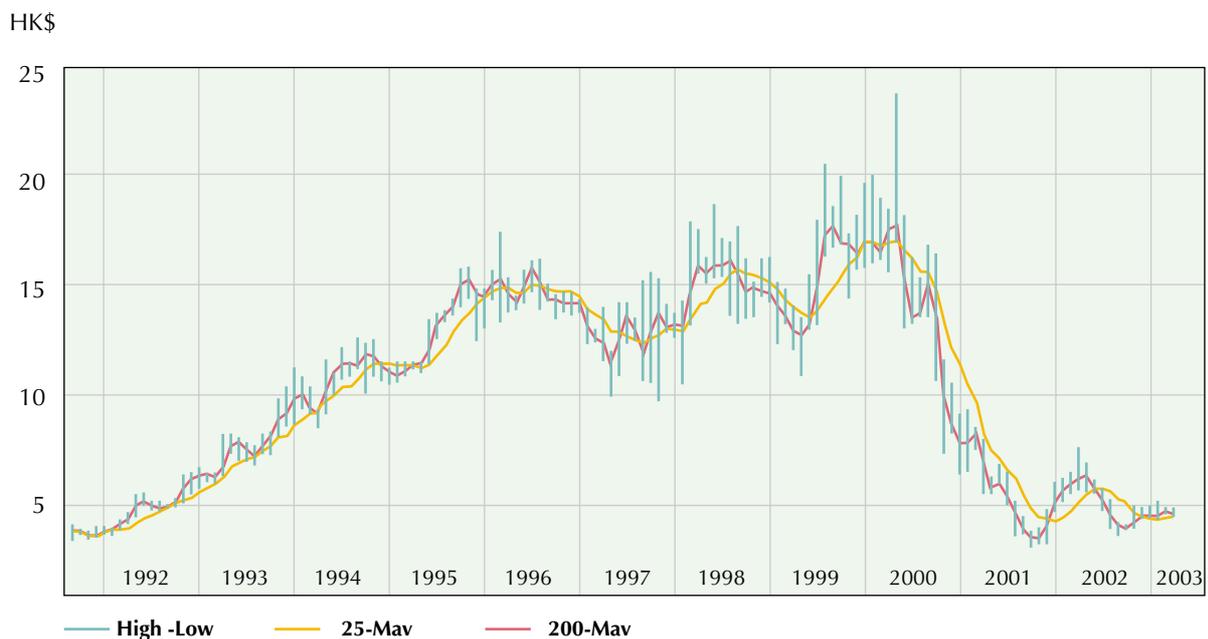
Geographic Destination for Products



Turnover/Profit After Tax



Share Price Movement (1 July 1991 - 31 March 2003)



BUSINESS REVIEW

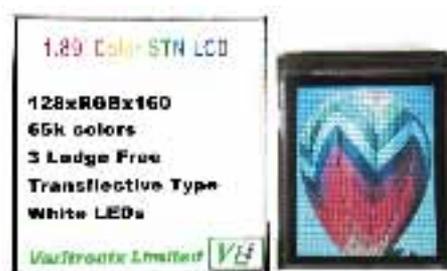
Review of operations

2002 was a steady year for Varitronix reflected by encouraging improvements in operating results and solid progress in technology development. Benefiting from significant sales growth in the PRC market, turnover was 4.2% higher than 2001 at HK\$1,086 million. The European market continued to be the Group's largest market, accounting for 50.6% of total turnover. Compared to 2001, turnover contribution from the North American market was lower at 11.3%. This can be partly explained by the growing number of customers who relocated their operations to the PRC, hence the share in the HK/China market increased from 11.7% to 26.0%. The significant rise in the PRC's contribution was also attributable to the valuable support from our joint venture partner Tsinghua University Enterprise Group, who helped to broaden our business connections and provided strategic guidance. In addition, it reflected the thriving conditions in the PRC domestic telecommunications sector.

Sales of our automotive products recorded impressive growth, a direct result of the QS9000 Quality System certification in 2001 and the cumulative efforts in deepening our understanding of customers' requirements. In view of stringent product requirements, the certification will continue to be a crucial asset in securing orders from our automotive customers. In addition, thanks to our highly flexible manufacturing facilities and technological capabilities, we were able to secure significant orders from telecommunication customers especially in the PRC

in the second half of the year. Annual sales in telecommunication products were however comparatively lower than last year. This can partly be explained by the fact that backlog orders from the telecommunication sector had carried forward to the first half of 2001. Notwithstanding this, sales in the telecommunications sector started to gradually improve in the second half of 2002 following a period of consolidation. Performance of our industrial products, which continued to be our most important product category, was steady in spite of the weak economic conditions prevailing in many parts of the world.

The Group's focused strategies in restoring performance have proven to be highly effective in further improving our first-half results. For the full year, the Group achieved profit attributable to shareholders of HK\$111 million, a rebound of 157.3% from the previous year. Amidst the highly competitive market environment, our business margins actually improved. Whilst careful production planning and stringent cost controls were important factors, continual improvements in operational management and process optimization have also contributed greatly. Together, these have helped to deliver a lower level of material content. Staff costs as well as other operating expenses were lower despite the higher level of sales achieved. Our profitability would have been higher if the charge against operating profit of HK\$10 million resulting from the winding up of an investment portfolio in the first-half was excluded. The overall results would have been even better if the Group could have achieved a turnaround at its Penang plant during the year.



Colour STN LCD

In addition to improving results, we have also moved forward in our technology roadmap. The Group's Bistable Cholesteric Display was awarded the 2002 Outstanding Innovation and Technology Silver Award by The Hong Kong Electronic Industries Association in recognition of its creative design, features and technology. Having successfully completed the prototypes of both monochrome and area color OLED displays, the Group pro-actively geared up its technical capacity in the second-half by entering various strategic partnerships. This included the alliance with DuPont Displays to assemble and distribute OLED display modules. In addition to this alliance, the Group had entered into a licensee agreement with Eastman Kodak Company permitting the Group to manufacture and sell passive matrix OLED modules based on Kodak's small molecule technology. The Group was the first Hong Kong company to be licensed by Kodak. The Group also collaborated with the UK based ZBD Displays Limited to develop the manufacturing process for zero-power displays. Prototype orders for our new color STN products were also secured during the year. These strategic moves are instrumental in planting the seeds for future sustainable growth and places the Group in the forefront in seizing emerging opportunities.



LCoS High Definition rear projection TV

The Group's balance sheet remained extremely healthy. Supported by robust cash flow from operations, net liquid funds were reported at a higher level of HK\$716 million at the end of the review period. This represents an increase of 16.2% over the level reported at the end of 2001 in spite of the fact that the majority of the payments for the construction, new equipment and facility costs of the new Heyuan plant had been settled during the year. To exercise prudent financial management, the Group was essentially in a debt free position. Inventory level was also lower than last year end.

PROSPECTS

The existing uncertainties besieging the global economy are expected to linger in 2003, creating overall cautious business sentiment. Amongst these concerns, the possible slowdown of the U.S economy will be a key influence. However, the PRC market is expected to sound a positive note, where the growth momentum of its telecommunications sector is anticipated to continue. We expect our sales in the PRC market to continue experiencing dynamic growth, reaching yet further highs in the year to come. As for the LCD industry, growing popularity of full color displays especially for handheld products will lend considerable support, helping the industry to develop steadily in the year ahead. Remaining at the forefront, we will not only deliver color solutions for color STN but also TFT solutions through alliance with TFT manufacturers, enabling us to stand out from our competitors.



Colour TFT Module

Faced with this market environment, defined corporate strategies combined with a high degree of production flexibility, are keys to maintaining competitiveness. As we approach our 25th year in business, our focus for 2003 will be to promote top line growth whilst continuing to raise efficiencies to enhance the bottom line. The rapidly expanding PRC economy will continue to create a background conducive to the Group's business. With the strong ability to deliver premier display products, our strength in capturing this market potential is further boosted by the technical support of the Tsinghua University Enterprise Group.

Whilst the Group's short term order growth appears promising, long term visibility remains low in view of the current world situation. However, ongoing efforts to review our technical capabilities have helped to expedite business expansion. The partnership with DuPont Display and licensee agreement from Eastman Kodak have placed the Group in the wings, poised to capture opportunities once the OLED market matures. To enrich our product variety, we are also actively developing full color OLED. Adhering to our commitment to research and development, we will continue to place strong emphasis on increasing the relevance of our production capabilities to match market requirements. In addition to the development of new products, the improvement of existing products, coupled with focused marketing strategies, will also be important elements.



Black-and-white bistable cholesteric display in electronic book application

Enhancing our operational leverage will also be a central task. Building construction at our new Heyuan plant has now drawn to a finish. Equipment installation is underway and is expected to be operational in the second half of the year. On the other hand, whilst resources are being allocated to revamp the Penang plant, the management remains conservative to its turnaround in the near term. However, we believe that our continuous commitment to reviewing and streamlining operations will ensure that our efficiencies and utilization rates will be further improved.

With clearly identified expansion plans and prudent production management, the Group is back on track to attaining better performance. Varitronix is committed to leveraging its renowned production excellence and innovation to deliver improved returns to shareholders in the years ahead.

On behalf of the directors, I would like to thank our staff for their dedication and efforts in the past year. I would also like to thank our customers, suppliers and shareholders for their continuous support. I look forward to working more closely with them to deliver even better results in the future.

Dr C.C. Chang

Chairman

Hong Kong, 3 April 2003

We Put Our Heart on **DISPLAY** 

MANAGEMENT DISCUSSION AND ANALYSIS

The Group's performance was discussed in detail in the Chairman's Statement. This part intends to offer further information not mentioned in the Chairman's Statement.

CASH FLOWS

During the year 2002, the net cash flows increased by HK\$97 million notwithstanding that HK\$99 million was paid for capital expenditures.

Cash generated from operations was HK\$210 million compared with HK\$278 million in 2001. The change was due to a slight increase in trade and other receivables. Additionally, there was exceptionally high cash generation in 2001 when the inventory and receivables were cut down from very high levels.

Compared to 2001, cash used in investing activities decreased slightly to HK\$63 million from HK\$67 million. The slight decrease in cash used in investing activities was due to proceeds received from liquidation of a non-trading mutual fund which also resulted in a loss of HK\$10.5 million. Capital expenditures were HK\$99 million, a similar level to 2001. These expenditures related to the construction of a new manufacturing facility in Heyuan, PRC and the necessary expansion of various other facilities.

Net cash used in financing activities decreased to HK\$27 million in 2002 from HK\$32 million in 2001, primarily due to the lower dividends paid in 2002 compared to 2001 though the repayment of bank loan increased by HK\$28 million.

FINANCIAL CONDITION, LIQUIDITY AND CAPITAL RESOURCES

Total assets as of 31 December 2002, increased HK\$116 million or 7.3% from 2001, largely due to increased liquid funds. The liquid funds comprising trading and non-trading securities, cash and cash equivalents amounted to HK\$777 million as at 31 December 2002.

For the year ended 31 December 2002, the Group's inventory turnover ratio was 5.3 times compared with 3.63 times for the twelve months ended 31 December 2001. The increase was primarily due to improved inventory management at the factories and in the distribution channels. Inventory turnover is defined as turnover divided by average inventory during the year.

Trade debtors and bills receivables were outstanding an average of 79.6 days for the year ended 31 December 2002, at similar level as 79.1 days for the same period in 2001. Working capital, defined as current assets less current liabilities, increased HK\$97.2 million from 31 December 2001 largely due to the increase in cash and cash equivalents.

The ratio of total debt to total capital (debt plus equity) was 6.2% at 31 December 2002 compared with 6.7% at 31 December 2001. Excluding the loss on liquidation of non-trading mutual fund during the year ended 31 December 2002, the return on assets was 8.7% compared with 6.7% for the year ended 31 December 2001, excluding the special write off of inventories.

EMPLOYEES AND REMUNERATION POLICIES

As at 31 December 2002, the Group employed approximately 4,150 persons around the world, of whom approximately 529 were in Hong Kong, 3,066 in PRC and 555 overseas. The Group remunerates its employees based on their performance, experience and prevailing industry practice. The Group operates an employee share option scheme and provides rent-free quarters to its employees in the PRC. For details of the Directors' emoluments, please refer to note 7 on the financial statements.

CONTINGENT LIABILITIES

Details of contingent liabilities are set out in note 28 on the financial statements.

FOREIGN CURRENCY EXPOSURE

The Group continues to conduct most of its business to US dollar or HK dollar. That, together with a policy of keeping the majority of our assets also in these currencies, ensures that our exposure to exchange rate fluctuations is minimal.

1. CUSTOMERS AND SUPPLIERS

The information in respect of the Group's turnover and purchases attributable to the major customers and suppliers during the financial year ended 31 December 2002 is as follows:

(a) Major customers

	Percentage of the Group's total turnover
The largest customer	7%
Five largest customers in aggregate	24%

(b) Major suppliers

	Percentage of the Group's total purchases
The largest supplier	8%
Five largest suppliers in aggregate	32%

At no time during the year have the Directors, their associates or any shareholder of the Company (which to the knowledge of the Directors owned more than 5% of the Company's share capital) any beneficial interests in these major customers and suppliers.

2. FINANCIAL REVIEW

The principal income of the Group for the year ended 31 December 2002 is derived mainly from sales of Liquid Crystal Displays and Liquid Crystal Display Modules. Turnover for the year was HK\$1,085,558,000 which is an increase of 4.2% over the previous year. The operating profit was HK\$140,838,000. The profit attributable to shareholders amounted to HK\$111,378,000, which represents an increase of 157.3% over the previous year.

There was a net cash inflow during 2002. Cash and deposits with banks and other financial institutions less bank overdrafts at 31 December 2002 totalled HK\$460,875,000.

3. DETAILS OF DIRECTORS

Dr Chang Chu Cheng, 59, is the Chairman of the Group. He gained his doctorate in Solid State Electronics from the University of Manchester Institute of Science & Technology in 1969 and lectured in Physics and Electronics at the Chinese University of Hong Kong prior to co-founding Varitronix in 1978 with other fellow directors. He presently serves as a Non-Executive Director of SAS Dragon Holdings Limited and Fujikon Industrial Holdings Limited which are both listed on The Hong Kong Stock Exchange Limited. He is also currently a member of TDC Electronics/Electrical Appliances Industry Advisory Committee, an Honorary Advisor of Hong Kong Critical Components Manufacturers Association and an honorary Chairman of Hong Kong Photographic and Optics Manufacturers Association.

3. **DETAILS OF DIRECTORS** *(continued)*

Dr Yan Sze Kwan, 59, is a Director of the Company with responsibility for overlooking operations and plant expansion. He has a Ph.D. in Physics from Massachusetts Institute of Technology and a postdoctoral from Wesleyan University, USA. From 1978 to 1987 he lectured firstly at Baptist College and subsequently at Hong Kong Polytechnic. Dr. Yan has been a Director since 1978 and subsequently became an Operations Manager of Varitronix in 1987.

Chung Shun Ming, 56, is a Director of the Company and Varitronix Limited, the main production arm of the Group, responsible for production planning and marketing. He holds a B.Sc. in Electrical Engineering from the University of California, Berkeley. From 1970 to 1978 he worked for Tai Wo Electronics Co. before joining Varitronix in 1978.

Kwok Siu Kwan, 51, is a Director of the Company responsible for technical development. He graduated from Hong Kong University and subsequently gained an M.Phil in Electronics at the Chinese University of Hong Kong and worked for Microelectronics Ltd. and Ampex Ferrotec Ltd. before joining Varitronix in 1979.

James Lee Goon Nam, 62, was an Executive Director of the Company and had primary responsibility for project development. He holds an M.Sc.Eng. from the University of New South Wales and from 1966 to 1974 was with AWA Limited in Australia. He subsequently lectured in Electronics at the Chinese University of Hong Kong before joining Varitronix full time in 1986 but has been a Director of Varitronix since its establishment and a non-executive director since beginning of 2001.

Professor Charles Kao Kuen, 69, has been an independent Non-Executive Director of the Company since 1991. He is a member of the Audit Committee of the Company. He was the former Vice-Chancellor of the Chinese University of Hong Kong (October 87 – July 96). He gained a Ph.D. from the University of London and is a world renowned expert in telecommunications and fibre optics. Since his retirement from the University in 1996, he has become a consultant. He is the Chairman and CEO of his consulting company, ITX Services Limited.

Anthony Lui Chi Shing, 57, has been an independent Non-Executive Director of the Company since 1991. He is the Chairman of the Audit Committee of the Company. He is a Fellow of the Institute of Chartered Accountants in England and Wales, an Associate Member of the Chartered Institute of Taxation and an Associate Member of the Hong Kong Society of Accountants. He has been practising as an accountant in Hong Kong for 24 years and is the sole proprietor of the firm Milne Ross (Certified Public Accountants).

4. SENIOR MANAGEMENT'S PROFILES

The management executives of the Company during the financial year were as follows:

Hong Kong and China

Craig Masterton	Deputy Operations Officer
Patrick Pun	Financial Controller
Dr Y.K. Fung	Project Manager
K.P. Ho	Technical Manager/LCM R&D
Amy Hsu	Human Resources Manager

Malaysia

Dr Tom S.K. Seah	Chief Executive Officer, Varitronix (Malaysia) Sdn. Bhd.
Peter T.H. Chang	General Manager, Varitronix (Malaysia) Sdn. Bhd.

The details of the management executives are as follows:

Craig Masterton, 55, is the Deputy Operations Officer of the Company. His primary responsibility for Manufacturing, Quality, Production and Material Control, Design Development, Process Engineering, and Purchasing. He has a M.Sc in Organizational Effectiveness from the University of New Haven and continued postgraduate studies in Organizational Effectiveness at Yale University. He has over 30 years of experience in various industries and was a consultant to companies in the international business environment for nine of those years.

Patrick Pun, 42, is the Financial Controller responsible for overall finance matters of the Group. Mr. Pun is a Chartered Management Accountant in U.K. and a Fellow of the Hong Kong Society of Accountants. Mr. Pun has over 15 years working experience with several multinational companies before joining the Group in 1997. Presently he is the Chairman of Industry and Technology Committee of the Hong Kong General Chamber of Commerce, a member of the Hong Kong Productivity Council and a member of Committee on Technologist Training of the Vocational Training Council.

Dr Y.K. Fung, 48, is a Project Manager of Varitronix Limited. After graduating from Ottawa University with a B.A.Sc. in Electrical Engineering in 1981, he worked for many years in the LCD industry both in this region and in the U.S.. Before joining the Group in 1995, he was with Kent States University from 1989 to 1994 working for his master and doctorate degrees in Physics.

K.P. Ho, 56, graduated from Hong Kong Polytechnic in 1973 with a Higher Certificate in Electrical Engineering and joined the Group in 1982. He is responsible for research and development of LCM products.

Amy Hsu, 48, is a Human Resources Manager of Varitronix Limited. She has over 20 years of extensive experience in all aspects of human resources management from diversified fields and with several multi-national companies working in HK, PRC, Canada & Taiwan before joining the Group in 2000. She graduated from Kingston University in UK and has been certified as HR Professional of Ontario (CHRP), MIPM in UK, and also members of various distinguished professional bodies such as Business British Graduate Society (UK), HK Society of Training & Development and Institute of Human Resources Management in HK.

4. SENIOR MANAGEMENT'S PROFILES *(continued)*

Dr Tom S.K. Seah, 53, is the Chief Executive Officer and a Director of Varitronix (Malaysia) Sdn. Bhd.. Immediately after he gained his doctorate in Theoretical Physics from University of North Carolina in 1975, he did his military service as an Artillery Officer in the Singapore Armed Forces until 1978. He then joined Printed Circuits International Ltd. (Singapore) as Project Engineer and left in 1981 as Product Director responsible for the entire LCD Division. From 1981 till 1996, he held various positions in Donnelly Corporation (USA) as Applied Research Manager, Technical Director and finally General Manager of a subsidiary of Donnelly in Yantai of China. He joined Varitronix (Malaysia) Sdn. Bhd. in July 1996.

Peter T.H. Chang, 53, is the General Manager of Varitronix (Malaysia) Sdn. Bhd.. He graduated from the University of Birmingham in 1975 with an M.Sc. and worked for National Semiconductor Corp. for three years as a QA Engineering Manager followed by working as General Manager in several other corporations in Malaysia. He joined Varitronix in 1992.

5. STAFF RETIREMENT SCHEMES

A subsidiary of the Company, Varitronix Limited, operates a defined contribution retirement scheme, whose assets are separate from the Group. The scheme is formally established under trust and is approved by the Inland Revenue Department under Section 87A of the Inland Revenue Ordinance. Both the employer and the employee are required to contribute 5% of the employee's basic monthly salary to the scheme.

The total retirement scheme cost charged to the Income Statement for the year was HK\$5,879,000 (2001: HK\$6,188,000). Charges to administer the scheme are deducted from the employer's contributions. Forfeited contributions are used by the employer to offset against future contributions. The amount so utilised during the year was HK\$201,000 (2001: HK1,552,000) and no balance (2001: Nil) was available for such use at 31 December 2002.

With effect from 1 December 2000, the Group also operates a MPF Scheme which was compulsory as enforced by The Mandatory Provident Fund Schemes Authority of Hong Kong. The existing retirement scheme will be a Top-Up ORSO scheme. The MPF Scheme is a defined contribution retirement benefit scheme administrated by independent trustees. The employer and the employee have to contribute in total an amount equal to 10% of the relevant income of the employee to the MPF Scheme. Contributions from employer are 100% vested in the employees accounts as soon as they are paid to the relevant MPF Scheme but all benefits derived from the mandatory contributions must be preserved until the employee reaches the retirement age of 65 subject to a few exceptions. The vesting for retirement scheme will remain unchanged.

Varitronix (Malaysia) Sdn. Bhd. operates a staff provident fund scheme under the Employees Provident Fund Act 1951. The employer and employee are required to contribute a certain percentage of the employee's basic monthly salary according to the Act. The total employer's contributions charged to the Income Statement for the year was HK\$1,877,000 (2001: HK\$2,193,000).

REPORT OF THE DIRECTORS

The directors have pleasure in submitting their annual report together with the audited financial statements for the year ended 31 December 2002.

PRINCIPAL ACTIVITIES

The principal activity of the Company is investment holding. The principal activities of the Group are the design, manufacture and sale of liquid crystal displays and related products.

The analysis of the principal activities and geographical locations of the operations of the Company and its subsidiaries during the financial year are set out in note 26 on the financial statements.

SUBSIDIARIES

Particulars of the Company's subsidiaries at 31 December 2002 are set out in note 14 on the financial statements.

FINANCIAL STATEMENTS

The profit of the Group for the year ended 31 December 2002 and the state of the Company's and the Group's affairs at that date are set out in the financial statements on pages 20 to 54.

An interim dividend of 4.4 cents per share (2001: 6.5 cents per share) was paid on 28 November 2002. The directors now recommend the payment of a special dividend of 4.0 cents per share (2001: 4.0 cents per share) and a final dividend of 18.0 cents per share (2001: 2.5 cents per share) in respect of the year ended 31 December 2002.

SHARE CAPITAL

Details of the movements in share capital of the Company during the year are set out in note 24 on the financial statements. Shares were issued on the exercise of share options and as a result of scrip dividends.

CHARITABLE DONATIONS

No donation was made by the Group during the year (2001: HK\$332,000).

FIXED ASSETS

Movements in fixed assets during the year are set out in note 12 on the financial statements.

DIRECTORS

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

Dr Chang Chu Cheng, Chairman
Dr Yan Sze Kwan
Chung Shun Ming
Kwok Siu Kwan
James Lee Goon Nam*
Professor Charles Kao Kuen**
Anthony Lui Chi Shing**
Dr York Liao* (resigned on 1 June 2002)

* *Non-Executive Directors*

** *Independent Non-Executive Directors*

In accordance with the Bye-laws of the Company, Professor Charles Kao Kuen and Chung Shun Ming shall retire from office by rotation and are eligible for re-election at the forthcoming annual general meeting.

DIRECTORS' INTERESTS IN SHARES

The Directors who held office at 31 December 2002 had the following interests in the issued share capital of the Company and its subsidiaries at that date as recorded in the register required to be kept under Section 29 of the Securities (Disclosure of Interests) Ordinance ("SDI Ordinance"):

(a) Interests in the Company

	Shares of HK\$0.25 each	
	Personal interests	Corporate interests
Varitronix International Limited		
Dr Chang Chu Cheng	21,445	68,386,479 <i>(note 1)</i>
Dr Yan Sze Kwan	10,371,072	–
Chung Shun Ming	4,511,314	–
Kwok Siu Kwan	2,112,959	–
James Lee Goon Nam	–	4,166,978 <i>(note 2)</i>

Notes:

1. A family trust of Dr Chang Chu Cheng and his wife, Madam Iling Sieh, is the beneficial owner of the issued share capital of Colville Group Limited which holds 68,386,479 shares of the Company.
2. Mr James Lee Goon Nam is the sole beneficial owner of the entire share capital of Pressman Holdings Limited which holds 4,166,978 shares of the Company.

DIRECTORS' INTERESTS IN SHARES (Continued)

(b) Interests in subsidiaries

	Non-voting deferred shares of HK\$1,000 each in Varitronix Limited	Non-voting deferred shares of HK\$100 each in Polysources Properties Limited
Dr Chang Chu Cheng	960	78
Dr Yan Sze Kwan	123	10
Chung Shun Ming*	50	8
Kwok Siu Kwan	50	4
James Lee Goon Nam	123	10
	<hr/>	<hr/>
	1,306	110
	<hr/> <hr/>	<hr/> <hr/>

* Mr Chung Shun Ming holds 4 non-voting deferred shares in Polysources Properties Limited in trust for all non-voting deferred shareholders of that company.

DIRECTORS' SERVICE CONTRACTS

Drs Chang Chu Cheng and Yan Sze Kwan and Messrs Chun Shun Ming and Kwok Siu Kwan have entered into management agreements with the Company which may be terminated by either party to the agreements at three months' notice.

Non-Executive Directors are appointed for a period up to 31 December 2003 or such other date as agreed by the Non-Executive Directors and the Company.

No Director proposed for re-election at the forthcoming annual general meeting has an unexpired service contract which is not determinable by the Company or any of its subsidiaries within one year without payment of compensation, other than normal statutory obligations.

DIRECTORS' INTERESTS IN CONTRACTS

No contract of significance to which the Company, or any of its subsidiaries was a party, in which a Director of the Company had a material interest, whether directly or indirectly, subsisted at the end of the year or at any time during the year.

SHARE OPTION SCHEMES

The Company had a Share Option Scheme ("Old Scheme") for the employees of the Group which was adopted on 6 June 1991, subsequently amended on 8 June 1999 and expired on 5 June 2001.

A new Share Option Scheme of the Company ("New Scheme") was adopted on 22 June 2001 as an incentive to the Group's employees. The New Scheme will remain in force until 21 June 2006.

Further details of the Old Scheme and the New Scheme are set out in note 24 on the financial statements. The maximum number of shares in respect of which options may be granted (together with options exercised and options then outstanding) under the New Scheme may not exceed 10 percent of the issued share capital of the Company, excluding any shares issued on exercise of options from time to time. The total number of shares available for issue under the Share Option Schemes at 31 December 2002 represents 2.19% of the issued share capital of the Company at that date.

The share options granted are not recognised in the financial statements until they are exercised. The weighted average value per option granted in 2002 estimated at the date of grant using the Black-Scholes pricing model was HK\$2.68 (2001: HK\$2.71). The weighted average assumptions used are as follows:

	2002	2001
Risk-free interest rate	4.54%	5.72%
Expected life (in years)	10	10
Volatility	47.04	57.52

The Black-Scholes option pricing model was developed for use in estimating the fair value of traded options that have no vesting restrictions and are fully transferable. In addition, such option pricing model requires input of highly subjective assumptions, including the expected stock price volatility. Because the Company's share options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, the Black-Scholes option pricing model does not necessarily provide a reliable measure of the fair value of the share options.

REPORT OF THE DIRECTORS (Continued)

SHARE OPTION SCHEMES (Continued)

	Date granted	Number of options at 1 January 2002	Granted during the year	Options lapsed during the year	Options cancelled during the year	Options exercised during the year	Number of options at 31 December 2002	Exercisable period	Price per share to be paid on exercise of option	Market value per share at date of grant of options	Market value per share on exercise of options	
<i>Director</i>												
Chang Chu Cheng	30 October 2002	-	1,000,000	-	-	-	1,000,000	31 October 2002 to 30 October 2012	4.605	4.35	N/A	
Yan Sze Kwan	30 October 2002	-	1,000,000	-	-	-	1,000,000	31 October 2002 to 30 October 2012	4.605	4.35	N/A	
Chung Shun Ming	30 October 2002	-	1,000,000	-	-	-	1,000,000	31 October 2002 to 30 October 2012	4.605	4.35	N/A	
Kwok Siu Kwan	1 January 1998	400,000	-	(400,000)	-	-	-	1 January 2000 to 31 December 2002	10.55	13.20	N/A	
	9 June 1999	150,000	-	-	-	-	150,000	9 July 1999 to 8 July 2009	10.90	15.00	N/A	
	30 October 2002	-	1,000,000	-	-	-	1,000,000	31 October 2002 to 30 October 2012	4.605	4.35	N/A	
<i>Employees</i>												
	1 January 1998	1,139,500	-	(1,096,500)	(43,000)	-	-	1 January 2000 to 31 December 2002	10.55	13.20	N/A	
	9 June 1999	472,750	-	-	(26,000)	-	446,750	9 July 1999 to 8 July 2009	10.90	15.00	N/A	
	1 June 2000	780,000	-	-	(47,000)	-	733,000	1 July 2000 to 30 June 2010	11.30	13.40	N/A	
	30 August 2001	850,000	-	-	(7,000)	(226,500)	616,500	30 August 2001 to 29 August 2011	3.06	3.68	5.72	
	13 September 2002	-	724,500	-	(7,000)	(6,000)	711,500	13 September 2002 to 12 September 2012	3.905	3.85	4.65	
		<u>3,792,250</u>	<u>4,724,500</u>	<u>(1,496,500)</u>	<u>(130,000)</u>	<u>(232,500)</u>	<u>6,657,750</u>					

Apart from the foregoing, at no time during the year was the Company or any of its subsidiaries a party to any arrangement to enable the Directors or any of their spouses or children under eighteen years of age to acquire benefits by means of the acquisition of shares in or debentures of the Company or any other body corporate.

SUBSTANTIAL INTERESTS IN THE SHARE CAPITAL OF THE COMPANY

Other than Directors of the Company, no person or corporation had any interest in the share capital of the Company as recorded in the registers required to be kept under Section 16(1) of the SDI Ordinance.

PRE-EMPTIVE RIGHTS

There is no provision for pre-emptive rights under the Company's Bye-laws and the law in Bermuda.

BANK LOANS, OVERDRAFTS AND OTHER BORROWINGS

Particulars of bank loans, overdrafts and other borrowings of the Group at 31 December 2002 are set out in notes 21 and 23 on the financial statements.

PROPERTIES

Particulars of the properties held by the Group are shown on pages 56 and 57 of the annual report.

FIVE YEAR SUMMARY

A summary of the results and the assets and liabilities of the Group for the last five financial years is set out on page 55 of the annual report.

PURCHASE, SALE OR REDEMPTION OF THE COMPANY'S LISTED SECURITIES

Neither the Company nor any of its subsidiaries has purchased, sold or redeemed any of the Company's listed securities during the year ended 31 December 2002.

COMPLIANCE WITH THE CODE OF BEST PRACTICE

The Company has complied throughout the year with the Code of Best Practice as set out by The Stock Exchange of Hong Kong Limited ("the Stock Exchange") in Appendix 14 to the Rules Governing the Listing of Securities on the Stock Exchange.

AUDITORS

KPMG retire and, being eligible, offer themselves for reappointment. A resolution for the reappointment of KPMG as auditors of the Company is to be proposed at the forthcoming annual general meeting.

By order of the board

Peter Lo Chi Lik

Secretary

Hong Kong, 3 April 2003



Auditors' report to the shareholders of

Varitronix International Limited

(Incorporated in Bermuda with limited liability)

We have audited the financial statements on pages 20 to 54 which have been prepared in accordance with accounting principles generally accepted in Hong Kong.

RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITORS

The Company's Directors are responsible for the preparation of financial statements which give a true and fair view. In preparing financial statements which give a true and fair view, it is fundamental that appropriate accounting policies are selected and applied consistently, that judgements and estimates are made which are prudent and reasonable and that the reasons for any significant departure from applicable accounting standards are stated.

It is our responsibility to form an independent opinion, based on our audit, on those financial statements and to report our opinion to you.

BASIS OF OPINION

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

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

OPINION

In our opinion, the financial statements give a true and fair view of the state of affairs of the Company and of the Group as at 31 December 2002 and of the Group's profit and cash flows for the year then ended and have been properly prepared in accordance with accounting principles generally accepted in Hong Kong and the disclosure requirements of the Hong Kong Companies Ordinance.

KPMG

Certified Public Accountants

Hong Kong, 3 April 2003

CONSOLIDATED INCOME STATEMENT

For the year ended 31 December 2002 (Expressed in Hong Kong dollars)

	Note	2002 \$'000	2001 \$'000 (restated)
Turnover	3	1,085,558	1,042,004
Other revenue	4	25,588	23,439
Other net income	4	1,744	7,526
Change in inventories of finished goods and work in progress		11,092	(51,510)
Raw material and consumables used		(539,065)	(441,919)
Write off of inventories	5	–	(42,774)
Staff costs		(205,487)	(222,915)
Depreciation		(80,552)	(89,947)
Other operating expenses		<u>(158,040)</u>	<u>(180,511)</u>
Profit from operations		140,838	43,393
Finance cost	6(a)	(3,134)	(2,901)
Share of (loss)/profit of associate		<u>(1,654)</u>	<u>5,735</u>
Profit from ordinary activities before taxation	6	136,050	46,227
Taxation	8(a)	<u>(17,704)</u>	<u>(13,749)</u>
Profit from ordinary activities after taxation		118,346	32,478
Minority interests		<u>(6,968)</u>	<u>10,803</u>
Profit attributable to shareholders	9	<u>111,378</u>	<u>43,281</u>
Dividends attributable to the year	10	<u>(80,241)</u>	<u>(38,811)</u>
Earnings per share			
Basic	11	<u>37 cents</u>	<u>15 cents</u>
Diluted	11	<u>37 cents</u>	<u>15 cents</u>

The notes on pages 26 to 54 form part of these financial statements.

CONSOLIDATED BALANCE SHEET

At 31 December 2002 (Expressed in Hong Kong dollars)

	Note	2002 \$'000	2001 \$'000 (restated)
Non-current assets			
Fixed assets	12	398,080	393,658
Goodwill	13	31,704	33,386
Interest in associate	15	16,254	19,276
Non-trading securities	16	226,765	227,861
		<u>672,803</u>	<u>674,181</u>
Current assets			
Trading securities	17	84,562	81,020
Inventories	18	198,074	213,235
Trade and other receivables	19	284,714	252,998
Cash and cash equivalents	20	466,073	368,578
		<u>1,033,423</u>	<u>915,831</u>
Current liabilities			
Bank loans and overdrafts	21	61,706	39,924
Bills payable	22	63	2,169
Trade and other payables	22	163,685	158,615
Taxation	8(b)	21,345	25,729
		<u>246,799</u>	<u>226,437</u>
Net current assets		<u>786,624</u>	<u>689,394</u>
Total assets less current liabilities		<u>1,459,427</u>	<u>1,363,575</u>
Non-current liabilities			
Bank loans	21	–	21,324
Convertible notes	23	31,200	31,200
Minority interests		28,382	22,265
NET ASSETS		<u>1,399,845</u>	<u>1,288,786</u>
CAPITAL AND RESERVES			
Share capital	24	76,023	75,619
Reserves	25	1,323,822	1,213,167
		<u>1,399,845</u>	<u>1,288,786</u>

Approved and authorised for issue by the board of directors on 3 April 2003.

Dr Yan Sze Kwan
Director

Chung Shun Ming
Director

The notes on pages 26 to 54 form part of these financial statements.

BALANCE SHEET

At 31 December 2002 (Expressed in Hong Kong dollars)

	Note	2002 \$'000	2001 \$'000
Non-current assets			
Interest in subsidiaries	14	870,122	859,065
Current assets			
Trade and other receivables		218	219
Tax recoverable	8(b)	–	8
Cash and cash equivalents	20	596	687
		<u>814</u>	<u>914</u>
Current liabilities			
Trade and other payables		8,985	4,904
Taxation	8(b)	42	–
		<u>9,027</u>	<u>4,904</u>
Net current liabilities		<u>(8,213)</u>	<u>(3,990)</u>
NET ASSETS		<u><u>861,909</u></u>	<u><u>855,075</u></u>
CAPITAL AND RESERVES			
Share capital	24	76,023	75,619
Reserves	25	785,886	779,456
		<u><u>861,909</u></u>	<u><u>855,075</u></u>

Approved and authorised for issue by the board of directors on 3 April 2003.

Dr Yan Sze Kwan
Director

Chung Shun Ming
Director

The notes on pages 26 to 54 form part of these financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the year ended 31 December 2002 (Expressed in Hong Kong dollars)

	Note	2002 \$'000	2001 \$'000
Shareholders' equity at 1 January			
As previous reported		1,295,207	1,294,816
Prior period adjustment arising from change in accounting policy for employee benefits	2	<u>(6,421)</u>	<u>(5,065)</u>
As restated		<u>1,288,786</u>	<u>1,289,751</u>
Surplus/(deficit) on revaluation of non-trading securities	25	14,090	(11,552)
Exchange differences on translation of the financial statements of foreign entities	25	<u>3,847</u>	<u>(155)</u>
Net gains/(losses) not recognised in the income statement		<u>17,937</u>	<u>(11,707)</u>
Net profit for the year			
As previously reported			44,637
Prior period adjustment arising from change in accounting policy for employee benefits			<u>(1,356)</u>
Net profit for the year (2001: as restated)		<u>111,378</u>	<u>43,281</u>
Revaluation deficit transferred to the income statement on disposal/liquidation of securities	25	<u>8,255</u>	<u>700</u>
Dividends approved during the year	10	<u>(33,014)</u>	<u>(71,727)</u>
Movements in share capital			
Shares issued		404	2,604
Share premium arising from issue of shares		6,099	36,255
Shares repurchased		<u>–</u>	<u>(371)</u>
		<u>6,503</u>	<u>38,488</u>
Shareholders' equity at 31 December		<u>1,399,845</u>	<u>1,288,786</u>

The notes on pages 26 to 54 form part of these financial statements.

CONSOLIDATED CASH FLOW STATEMENT

For the year ended 31 December 2002 (Expressed in Hong Kong dollars)

	Note	2002 \$'000	2001 \$'000 (restated)
Operating activities			
Profit from ordinary activities before taxation		136,050	46,227
Adjustments for:			
– Depreciation		80,552	89,947
– Amortisation of goodwill		1,682	254
– Finance cost		3,134	2,901
– Dividend income		(546)	(206)
– Interest income		(19,741)	(20,291)
– Realised losses on disposal/liquidation of non-trading securities		8,255	693
– (Profit)/loss on disposals of fixed assets		(2,106)	48
– Share of loss/(profit) of associate		1,654	(5,735)
– Effect of foreign exchange rates		367	442
		<u>209,301</u>	<u>114,280</u>
Operating profit before changes in working capital			
Decrease in amount due from associate		1,369	7,797
Increase in trading securities		(3,542)	(14,595)
Decrease in inventories		15,161	147,585
(Increase)/decrease in trade and other receivables		(31,791)	114,330
Decrease in bills payable		(2,106)	(4,095)
Increase/(decrease) in trade and other payables		21,179	(87,578)
		<u>209,571</u>	<u>277,724</u>
Cash generated from operations			
Tax paid			
– Hong Kong profits tax paid		(18,981)	(66)
– Overseas tax paid		(3,107)	(9,760)
		<u>187,483</u>	<u>267,898</u>
Net cash from operating activities			
Investing activities			
Proceeds from disposal of fixed assets		626	349
Payment for purchase of fixed assets		(99,145)	(98,867)
Proceeds from disposal of non-trading securities		174,213	103,446
Purchase of non-trading securities		(159,027)	(92,367)
Dividends received		546	206
Interest received		19,816	20,412
		<u>(62,971)</u>	<u>(66,821)</u>
Net cash used in investing activities			

CONSOLIDATED CASH FLOW STATEMENT (Continued)

For the year ended 31 December 2002 (Expressed in Hong Kong dollars)

	Note	2002 \$'000	2001 \$'000 (restated)
Financing activities			
New bank loans		49,601	49,811
Repayment of bank loans		(46,434)	(17,882)
Proceeds on issue of shares		717	462
Repurchase of own shares		–	(365)
Interest paid		(3,134)	(2,901)
Dividends paid		(27,229)	(58,051)
Dividend paid to minority shareholders		(942)	(3,016)
		<u>(27,421)</u>	<u>(31,942)</u>
Net cash used in financing activities		(27,421)	(31,942)
Net increase in cash and cash equivalents		97,091	169,135
Cash and cash equivalents at 1 January		360,671	192,297
Effect of foreign exchange rates changes		3,113	(761)
Cash and cash equivalents at 31 December	20	<u>460,875</u>	<u>360,671</u>

Note to the Consolidated Cash Flow Statement

(a) Major non cash transactions

During the year shares were issued as a result of scrip dividends.

The notes on pages 26 to 54 form part of these financial statements.

NOTES ON THE FINANCIAL STATEMENTS

(Expressed in Hong Kong dollars)

1. SIGNIFICANT ACCOUNTING POLICIES

(a) Statement of compliance

These financial statements have been prepared in accordance with all applicable Statements of Standard Accounting Practice and Interpretations issued by the Hong Kong Society of Accountants, accounting principles generally accepted in Hong Kong and the disclosure requirements of the Hong Kong Companies Ordinance. The financial statements also comply with the applicable disclosure provisions of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited. A summary of the significant accounting policies adopted by the Group is set out below.

(b) Basis of preparation of the financial statements

The measurement basis used in the preparation of the financial statements is historical cost modified by the marking to market of certain investments in securities as explained in the accounting policies set out below.

(c) Subsidiaries

A subsidiary is an enterprise controlled by the Company. Control exists when the Company has the power, directly or indirectly, to govern the financial and operating policies of an enterprise so as to obtain benefits from its activities.

An investment in a subsidiary is consolidated into the consolidated financial statements, unless a subsidiary is acquired and held exclusively with a view to subsequent disposal in the near future or operates under severe long-term restrictions which significantly impair its ability to transfer funds to the Group, in which case, it is stated in the consolidated balance sheet at fair value with changes in fair value recognised in accordance with the policy for investments in securities set out in note 1(h) below.

Intra-group balances and transactions, and any unrealised profits arising from intra-group transactions, are eliminated in full in preparing the consolidated financial statements. Unrealised losses resulting from intra-group transactions are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

In the Company's balance sheet, investments in subsidiaries are stated at cost less any impairment losses (see note 1(g)).

(d) Associates

An associate is an entity in which the Group has significant influence, but not control or joint control, over its management, including participation in the financial and operating policy decisions.

An investment in an associate is accounted for in the consolidated financial statements under the equity method and is initially recorded at cost and adjusted thereafter for the post acquisition change in the Group's share of the associate's net assets. The consolidated income statement reflects the Group's share of the post-acquisition results of the associates for the year, including any amortisation of positive or negative goodwill charged or credited during the year in accordance with note 1(e) and impairment losses (see note 1(g)).

1. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(e) Goodwill

Positive goodwill arising on consolidation represents the excess of the cost of the acquisition over the Group's share of the fair value of the identifiable assets and liabilities acquired. In respect of subsidiaries:

- for acquisitions before 1 January 2001, positive goodwill is eliminated against reserves and is reduced by impairment losses (see note 1(g)); and
- for acquisitions on or after 1 January 2001, positive goodwill is amortised to the consolidated income statement on a straight line basis over its estimated useful life. Positive goodwill is stated in the consolidated balance sheet at cost less any accumulated amortisation and any impairment losses (see note 1(g)).

Amortisation of positive goodwill is on a straight line basis over an estimated useful life of 20 years.

(f) Fixed assets

(i) Fixed assets are stated at cost less accumulated depreciation and impairment losses (see note 1(g)).

(ii) Land and buildings

No amortisation is provided on freehold land. Leasehold land is amortised on a straight line basis over the unexpired terms of the leases or 50 years, whichever is the lesser. Buildings are depreciated on a straight line basis over their anticipated useful lives of 40 years.

(iii) Other fixed assets

Depreciation is calculated to write off the cost of other fixed assets over their anticipated useful lives on a straight line basis as follows:

Plant and machinery	4 years
Tools and equipment	5 years
Others	2 to 5 years

(iv) Disposal of fixed assets

Gains or losses arising from the retirement or disposal of a fixed asset are determined as the difference between the estimated net disposal proceeds and the carrying amount of the asset and are recognised as income or expense in the income statement on the date of retirement or disposal.

1. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

(g) Impairment of assets

Internal and external sources of information are reviewed at each balance sheet date to identify indications that the following assets may be impaired or an impairment loss previously recognised no longer exists or may have decreased:

- fixed assets;
- investments in subsidiaries and associates; and
- positive goodwill (whether taken initially to reserves or recognised as an asset).

If any such indication exists, the asset's recoverable amount is estimated. An impairment loss is recognised whenever the carrying amount of an asset exceeds its recoverable amount.

(i) *Calculation of recoverable amount*

The recoverable amount of an asset is the greater of its net selling price and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of time value of money and the risks specific to the asset. Where an asset does not generate cash inflows largely independent of those from other assets, the recoverable amount is determined for the smallest group of assets that generates cash inflows independently (i.e. a cash-generating unit).

(ii) *Reversals of impairment losses*

In respect of assets other than goodwill, an impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss in respect of goodwill is reversed only if the loss was caused by a specific external event of an exceptional nature that is not expected to recur, and the increase in recoverable amount relates clearly to the reversal of the effect of that specific event.

A reversal of impairment losses is limited to the asset's carrying amount that would have been determined had no impairment loss been recognised in prior years. Reversals of impairment losses are credited to the income statement in the year in which the reversals are recognised.

1. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(h) Investments in securities

The Group's policies for investments in securities other than investments in subsidiaries and associates are as follows:

- (i) Non-trading securities are stated in the balance sheet at fair value. Changes in fair value are recognised in the investment revaluation reserve until the security is sold, collected, or otherwise disposed of, or until there is objective evidence that the security is impaired, at which time the relevant cumulative gain or loss is transferred from the investment revaluation reserve to the income statement.

Transfers from the investment revaluation reserve to the income statement as a result of impairments are reversed when the circumstances and events that led to the impairment cease to exist and there is persuasive evidence that the new circumstances and events will persist for the foreseeable future.

- (ii) Trading securities are stated in the balance sheet at fair value. Changes in fair value are recognised in the income statement as they arise.
- (iii) Profits or losses on disposal of investments in securities are accounted for in the income statement as they arise. In the case of non-trading securities, the profit or loss includes any amount previously held in the investment revaluation reserve in respect of that security.

(i) Inventories

Inventories are carried at the lower of cost and net realisable value.

Cost is calculated using the first-in first-out method and comprises all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition.

Net realisable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

When inventories are sold, the carrying amount of those inventories is recognised as an expense in the period in which the related revenue is recognised. The amount of any write-down of inventories to net realisable value and all losses of inventories are recognised as an expense in the period in which the write-down or loss occurs. The amount of any reversal of any write-down of inventories, arising from an increase in net realisable value, is recognised as a reduction in the amount of inventories recognised as an expense in the period in which the reversal occurs.

(j) Cash and cash equivalents

Cash and cash equivalents comprise cash at bank and on hand, demand deposits with banks and other financial institutions, and short-term, highly liquid investments that are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value, having been within three months of maturity at acquisition. Bank overdrafts that are repayable on demand and form an integral part of the Group's cash management are also included as a component of cash and cash equivalents for the purpose of the cash flow statement.

1. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(k) Revenue recognition

Provided it is probable that the economic benefits will flow to the Group and the revenue and costs, if applicable, can be measured reliably, revenue is recognised in the income statement as follows:

- (i) Revenue arising from the sale of goods is recognised on delivery of goods to customers which is taken to be the point in time when the customer has accepted the goods and the related risks and rewards of ownership. Revenue excludes value added or other sales taxes and is after deduction of returns and any trade discounts.
- (ii) Interest income from bank deposits and debt securities is accrued on a time-apportioned basis on the principal outstanding and at the rate applicable.
- (iii) Income from other securities is recognised when the Company's right to receive such income is established.

(l) Employee benefit

- (i) Salaries, annual bonuses, paid annual leave, leave passage and the cost to the Group of non-monetary benefits are accrued in the year in which the associated services are rendered by employees of the Group. Where payment or settlement is deferred and the effect would be material, these amounts are stated at their present values.
- (ii) Contributions to defined contribution plans and Mandatory Provident Funds as required under the Hong Kong Mandatory Provident Fund Schemes Ordinance are recognised as an expense in the income statement as incurred.
- (iii) When the Group grants employees options to acquire shares of the Company, no employee benefit cost or obligation is recognised at that time. When the options are exercised, equity is increased by the amount of the proceeds received.

(m) Operating leases

Rentals payable and receivable under operating leases are accounted for in the income statement on a straight line basis over the periods of the respective leases.

(n) Deferred taxation

Deferred taxation is provided using the liability method in respect of the taxation effect arising from all timing differences between the accounting and tax treatment of income and expenditure, which are expected with reasonable probability to crystallise in the foreseeable future.

Future deferred tax benefits are not recognised unless their realisation is assured beyond reasonable doubt.

1. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

(o) Translation of foreign currencies

Foreign currency transactions during the year are translated into Hong Kong dollars at the exchange rates ruling at the transaction dates. Monetary assets and liabilities denominated in foreign currencies are translated into Hong Kong dollars at the exchange rates ruling at the balance sheet date. Exchange gains and losses on foreign currency translation are dealt with in the income statement. Foreign currency assets, being equity investments or other long-term non-monetary assets, the holding or the use or the subsequent disposal of which will generate receipts in a foreign currency, hedged by foreign currency borrowings, are translated into Hong Kong dollars at the exchange rates ruling at the balance sheet date.

The results of overseas subsidiaries are translated into Hong Kong dollars at the average exchange rates for the year; balance sheet items are translated into Hong Kong dollars at the rates of exchange ruling at the balance sheet date. The resulting exchange differences are dealt with as a movement in reserves.

(p) Related parties

For the purposes of these financial statements, parties are considered to be related to the Group if the Group has the ability, directly or indirectly, to control the party or exercise significant influence over the party in making financial and operating decisions, or vice versa, or where the Group and the party are subject to common control or common significant influence. Related parties may be individuals or other entities.

(q) Segment reporting

A segment is a distinguishable component of the Group that is engaged either in providing products or services (business segment), or in providing products or services within a particular economic environment (geographical segment), which is subject to risks and rewards that are different from those of other segments.

In accordance with the Group's internal financial reporting, the Group has chosen business segment information as the primary reporting format and geographical segment information as the secondary reporting format.

Segment revenue, expenses, results, assets and liabilities include items directly attributable to a segment as well as those that can be allocated on a reasonable basis to that segment. For example, segment assets may include inventories, trade receivables and property, plant and equipment. Segment revenue, expenses, assets, and liabilities are determined before intra-group balances and intra-group transactions are eliminated as part of the consolidation process, except to the extent that such intra-group balances and transactions are between group enterprises within a single segment. Inter-segment pricing is based on similar terms as those available to other external parties.

Segment capital expenditure is the total cost incurred during the period to acquire segment assets (both tangible and intangible) that are expected to be used for more than one period.

Unallocated items mainly comprise financial and corporate assets, interest-bearing loans, borrowings, corporate and financing expenses and minority interests.

NOTES ON THE FINANCIAL STATEMENTS (Continued)

(Expressed in Hong Kong dollars)

2. CHANGE IN ACCOUNTING POLICY

With effect from 1 January 2002, in order to comply with Statement of Standard Accounting Practice 34 "Employee benefits" issued by the Hong Kong Society of Accountants, it was necessary to change the Group's accounting policy in respect of long service payments.

As a result of the new accounting policy, the Group's profit for the year is unchanged (2001: decreased by \$1,356,000) and the net assets as at the year end have been decreased by \$6,421,000 (2001: \$6,421,000). The effect of adopting the new accounting policy relating to prior periods has been adjusted to the opening balances of retained profits and the comparative information has been restated as disclosed in the consolidated statement of changes in equity.

3. TURNOVER

The principal activity of the Company is investment holding. The principal activities of the Group are the design, manufacture and sale of liquid crystal displays and related products.

Turnover represents the invoiced value of goods supplied to customers by the Group less returns and discounts.

4. INCOME

	2002 \$'000	2001 \$'000
Other revenue		
Dividend income from listed equity securities	546	206
Interest income from listed debt securities	11,856	11,268
Interest income from unlisted debt securities	360	273
Income from listed investment funds	807	43
Interest income from unlisted investment funds	440	1,033
Other interest income	6,278	7,674
Rental under operating leases	3,248	1,493
Other income	2,053	1,449
	<u>25,588</u>	<u>23,439</u>
Other net income		
Profit/(loss) on disposal of fixed assets	2,106	(48)
Loss on liquidation of non-trading mutual fund	(10,471)	-
Realised gains/(losses) on disposal of other non-trading securities	2,216	(693)
Realised and unrealised losses on trading securities	(2,680)	(5,784)
Exchange gain	10,573	14,051
	<u>1,744</u>	<u>7,526</u>

NOTES ON THE FINANCIAL STATEMENTS (Continued)

(Expressed in Hong Kong dollars)

5. WRITE OFF OF INVENTORIES

During the year ended 31 December 2001 the Group fully wrote off work in progress and finished goods inventories amounting to \$42,774,000.

6. PROFIT FROM ORDINARY ACTIVITIES BEFORE TAXATION

Profit from ordinary activities before taxation is arrived at after charging:

	2002 \$'000	2001 \$'000
(a) Finance cost:		
Interest on bank advances and other borrowings repayable within five years	1,263	1,030
Interest on convertible notes	1,871	1,871
	<u>3,134</u>	<u>2,901</u>
(b) Other items:		
Cost of inventories	746,595	737,181
Auditors' remuneration	1,234	1,339
Research and development costs	24,518	38,142
Rental charges under operating leases	2,917	3,120
Exchange loss	3,410	3,137
Contributions to defined contribution plan	5,879	6,188
Other retirement scheme costs	1,877	2,193
	<u>786,305</u>	<u>828,370</u>

7. DIRECTORS' REMUNERATION

Directors' remuneration disclosed pursuant to section 161 of the Hong Kong Companies Ordinance is as follows:

	2002 \$'000	2001 \$'000
Fees	600	400
Salaries and allowances	6,105	8,318
Retirement scheme contributions	222	224
Discretionary and performance related bonuses	6,905	3,257
	<u>13,832</u>	<u>12,199</u>

Fees in respect of independent non-executive directors for the year ended 31 December 2002 amounted to \$400,000 (2001: \$400,000).

Certain directors were granted share options in prior years under the Company's Share Option Scheme. The details of these benefits in kind are disclosed under the paragraph "Share Option Schemes" in the Directors' Report.

NOTES ON THE FINANCIAL STATEMENTS (Continued)

(Expressed in Hong Kong dollars)

7. DIRECTORS' REMUNERATION (Continued)

The Directors' remuneration, which includes the five highest individuals' remuneration, fell within the following ranges:

	Number of Directors	
	2002	2001
\$0 – \$1,000,000	4	3
\$1,500,001 – \$2,000,000	–	2
\$2,000,001 – \$2,500,000	–	2
\$3,000,001 – \$3,500,000	3	1
\$4,000,001 – \$4,500,000	1	–
	<u>1</u>	<u>–</u>

8. TAXATION

(a) Taxation in the consolidated income statement represents:

	2002 \$'000	2001 \$'000
Provision for Hong Kong Profits Tax for the year	14,049	5,248
(Over)/under provision in respect of prior years	(1,115)	2,688
	<u>12,934</u>	<u>7,936</u>
Overseas tax	4,770	5,813
	<u>17,704</u>	<u>13,749</u>

The provision for Hong Kong Profits Tax is calculated at 16% (2001: 16%) of the estimated assessable profits for the year ended 31 December 2002. Taxation for overseas subsidiaries is similarly charged at the appropriate current rates of taxation ruling in the relevant countries.

(b) Taxation in the balance sheet represents:

	The Group		The Company	
	2002 \$'000	2001 \$'000	2002 \$'000	2001 \$'000
Provision for Hong Kong Profits Tax for the year	14,049	5,248	–	–
Provisional Profits Tax paid	(1,145)	(243)	–	(49)
Balance of Profits Tax provision relating to prior years	7,607	21,552	42	41
Overseas tax	834	(828)	–	–
	<u>21,345</u>	<u>25,729</u>	<u>42</u>	<u>(8)</u>

(c) No provision for deferred taxation has been made as the effect of all timing differences is immaterial.

NOTES ON THE FINANCIAL STATEMENTS (Continued)

(Expressed in Hong Kong dollars)

9. PROFIT ATTRIBUTABLE TO SHAREHOLDERS

The consolidated profit attributable to shareholders includes a profit of \$33,345,000 (2001: \$51,448,000) which has been dealt with in the financial statements of the Company.

10. DIVIDENDS

(a) Dividends attributable to the year

	2002 \$'000	2001 \$'000
Interim dividend declared and paid of 4.4 cents (2001: 6.5 cents) per share	13,341	19,138
Special dividend proposed after the balance sheet date of 4.0 cents (2001: 4.0 cents) per share	12,164	12,106
Final dividend proposed after the balance sheet date of 18.0 cents (2001: 2.5 cents) per share	<u>54,736</u>	<u>7,567</u>
	<u><u>80,241</u></u>	<u><u>38,811</u></u>

The dividends in respect of the years ended 31 December 2001 and 31 December 2002 are scrip dividends with a cash option.

The special and final dividends proposed after the balance sheet date have not been recognised as a liability at the balance sheet date.

(b) Dividends attributable to the previous financial year, approved and paid during the year

	2002 \$'000	2001 \$'000
Special dividend in respect of the previous financial year, approved and paid during the year, of 4.0 cents (2001: Nil) per share	12,106	–
Final dividend in respect of the previous financial year, approved and paid during the year, of 2.5 cents (2001: 18 cents) per share	<u>7,567</u>	<u>52,589</u>
	<u><u>19,673</u></u>	<u><u>52,589</u></u>

NOTES ON THE FINANCIAL STATEMENTS (Continued)

(Expressed in Hong Kong dollars)

11. EARNINGS PER SHARE

(a) Basic earnings per share

The calculation of basic earnings per share is based on the profit attributable to shareholders of \$111,378,000 (2001 (restated): \$43,281,000) and on the weighted average of 302,943,079 shares (2001: 293,623,077 shares) in issue during the year.

(b) Diluted earnings per share

The calculation of diluted earnings per share is based on the adjusted profit attributable to shareholders of \$111,378,000 (2001 (restated): \$43,281,000) and the weighted average number of shares of 303,321,313 shares (2001: 293,761,748 shares) after adjusting for the effects of all dilutive potential shares.

(c) Reconciliations

	2002 Number of shares	2001 Number of shares
Weighted average number of shares used in calculating basic earnings per share	302,943,079	293,623,077
Deemed issue of shares for no consideration arising from share options	<u>378,234</u>	<u>138,671</u>
Weighted average number of shares used in calculating diluted earnings per share	<u><u>303,321,313</u></u>	<u><u>293,761,748</u></u>

NOTES ON THE FINANCIAL STATEMENTS (Continued)

(Expressed in Hong Kong dollars)

12. FIXED ASSETS

The Group

	Land and buildings \$'000	Plant, machinery, tools and equipment \$'000	Others \$'000	Total \$'000
Cost:				
At 1 January 2002	300,500	398,310	162,123	860,933
Exchange adjustment	305	435	267	1,007
Additions	24,154	54,805	20,186	99,145
Disposals	(16,109)	(1,565)	(965)	(18,639)
At 31 December 2002	<u>308,850</u>	<u>451,985</u>	<u>181,611</u>	<u>942,446</u>
Aggregate depreciation:				
At 1 January 2002	45,911	300,130	121,234	467,275
Exchange adjustment	69	265	215	549
Charge for the year	5,911	55,175	19,466	80,552
Written back on disposals	(2,014)	(1,040)	(956)	(4,010)
At 31 December 2002	<u>49,877</u>	<u>354,530</u>	<u>139,959</u>	<u>544,366</u>
Net book value:				
At 31 December 2002	<u>258,973</u>	<u>97,455</u>	<u>41,652</u>	<u>398,080</u>
At 31 December 2001	<u>254,589</u>	<u>98,180</u>	<u>40,889</u>	<u>393,658</u>

Other fixed assets comprise mainly leasehold improvements, furniture, fixtures, office equipment and motor vehicles.

NOTES ON THE FINANCIAL STATEMENTS (Continued)

(Expressed in Hong Kong dollars)

12. FIXED ASSETS (Continued)

The analysis of the net book value of properties is as follows:

	2002 \$'000	2001 \$'000
In Hong Kong		
– under medium term leases	149,959	168,532
Outside Hong Kong		
– freehold	556	557
– under long term leases	53,236	70,486
– under medium term leases	44,579	4,070
– no specified lease term	10,643	10,944
	<u>109,014</u>	<u>86,057</u>
	<u>258,973</u>	<u>254,589</u>

The gross amount of fixed assets of the Group held for use in operating leases was \$31,418,000 (2001: \$20,573,000), the related accumulated depreciation was \$7,561,000 (2001: \$1,608,000) at 31 December 2002 and the depreciation charge for the year was \$492,000 (2001: \$166,000).

13. GOODWILL

	\$'000
Cost:	
At 1 January 2002 and 31 December 2002	33,640
Accumulated amortisation:	
At 1 January 2002	(254)
Amortisation for the year	(1,682)
At 31 December 2002	<u>(1,936)</u>
Carrying amount:	
At 31 December 2002	<u>31,704</u>
At 31 December 2001	<u>33,386</u>

NOTES ON THE FINANCIAL STATEMENTS (Continued)

(Expressed in Hong Kong dollars)

14. INTEREST IN SUBSIDIARIES

(a) The Company

	2002 \$'000	2001 \$'000
Unlisted shares, at cost	101,453	101,453
Amounts due from subsidiaries	<u>768,669</u>	<u>757,612</u>
	<u><u>870,122</u></u>	<u><u>859,065</u></u>

All of these are controlled subsidiaries as defined under note 1(c) and have been consolidated into the Group's financial statements.

Details of these subsidiaries are as follows:

Name of company	Place of incorporation/ operation	Particulars of issued/ registered capital	Percentage of equity held by		Principal activities
			Company	Subsidiaries	
Varitronix (B.V.I.) Limited	British Virgin Islands/ Hong Kong	18,480 ordinary shares of US\$1 each	100%	–	Investment holding
Varintelligent (BVI) Limited	British Virgin Islands/ Hong Kong	1 ordinary share of US\$1 each	100%	–	Holding and licensing of trademarks
Vogue Industries Limited	British Virgin Islands/ Hong Kong	100 ordinary shares of US\$1 each	100%	–	Investment holding
Varitronix Limited	Hong Kong	2 ordinary shares of \$1,000 each 1,848 non-voting deferred ordinary shares of \$1,000 each	–	100%	Design, manufacture and sale of liquid crystal displays and related products
Varitronix (Malaysia) Sdn. Bhd.	Malaysia	38,000,000 ordinary shares of Myr\$1 each	–	100%	Design, manufacture and sale of liquid crystal displays and related products
* Varitronix (Heyuan) Co. Ltd.	The People's Republic of China	Rmb62,010,789	–	80%	Manufacture of liquid crystal displays and related products

NOTES ON THE FINANCIAL STATEMENTS (Continued)

(Expressed in Hong Kong dollars)

14. INTEREST IN SUBSIDIARIES (Continued)

(a) The Company (Continued)

Name of company	Place of incorporation/ operation	Particulars of issued/ registered capital	Percentage of equity held by		Principal activities
			Company	Subsidiaries	
* Varitronix Manufacturing (BVI) Limited	British Virgin Islands/The People's Republic of China	100 ordinary shares of US\$1 each	–	100%	Subcontract and operate production plant in the People's Republic of China
* Varitronix (Singapore) Pte Ltd.	Singapore	200,000 ordinary shares of SGD 1 each	–	100%	Research development centre
* Varitronix (U.K.) Limited	United Kingdom	100 ordinary shares of £10 each	–	100%	Marketing and sales consultants
* VL Electronics, Inc.	United States	5,000 common stock of US\$10 each	–	100%	Marketing and sales consultants
* Varitronix (Canada) Limited	Canada	100 ordinary shares of C\$1 each	–	100%	Marketing and sales consultants
* Varitronix Italia, s.r.l.	Italy	25,000 ordinary shares of ITL 1,000 each	–	100%	Marketing and sales consultants
* Varitronix GmbH	Germany	100,000 shares of DM 1 each	–	60%	Marketing and sales consultants
Varitronix (France) SAS	France	2,500 ordinary shares of FF 100 each	–	100%	Marketing and sales consultants
# * Varitronix Pengyuan Limited	The People's Republic of China	Rmb8,000,000	–	51%	Marketing and sales consultants
Link Score Investment Limited	Hong Kong	100 ordinary shares of \$1 each	–	100%	Property investment and investment holding

NOTES ON THE FINANCIAL STATEMENTS (Continued)

(Expressed in Hong Kong dollars)

14. INTEREST IN SUBSIDIARIES (Continued)

(a) The Company (Continued)

Name of company	Place of incorporation/ operation	Particulars of issued/ registered capital	Percentage of equity held by		Principal activities
			Company	Subsidiaries	
Polysources Properties Limited	Hong Kong	2 ordinary shares of \$100 each 154 non-voting deferred ordinary shares of \$100 each	–	100%	Property investment
* Starel Trading Limited	Republic of Cyprus/United Kingdom	1,000 shares of Cyprus £1 each	–	100%	Property investment
* Quest Industries Limited	British Virgin Islands/The People's Republic of China	100 ordinary shares of US\$1 each	–	100%	Property investment
Cadac Electronic (M) Sdn. Bhd.	Malaysia	276,002 ordinary shares of Myr\$1 each	–	100%	Property investment
Varitronix Finance Limited	British Virgin Islands/ Hong Kong	100 ordinary shares of US\$1 each	–	100%	Provision of financial co-ordination services for group companies and holding of trading securities
Varitronix Investment Limited	British Virgin Islands/ Hong Kong	5,000 ordinary shares of US\$1 each	–	100%	Investment holding
Varitronix Agencies Limited	British Virgin Islands/ Hong Kong	50,000 shares of US\$1 each	–	100%	Investment holding
* Varitronix Marketing Limited	British Virgin Islands/ United Kingdom	1,000 shares of US\$1 each	–	100%	Investment holding
* Mcalpine Management Limited	British Virgin Islands/ United Kingdom	1,000 shares of US\$1 each	–	100%	Investment holding

NOTES ON THE FINANCIAL STATEMENTS (Continued)

(Expressed in Hong Kong dollars)

14. INTEREST IN SUBSIDIARIES (Continued)

(a) The Company (Continued)

Name of company	Place of incorporation/ operation	Particulars of issued/ registered capital	Percentage of equity held by Company	Subsidiaries	Principal activities
* Varitronix Marketing (China) Limited	British Virgin Island/ The People's Republic of China	1 share of US\$1	–	100%	Investment holding
* Varitronix (Shenzhen) Limited	British Virgin Island/ The People's Republic of China	1 share of US\$1	–	100%	Investment holding
Varitronix Optech Limited	Hong Kong	100,000 ordinary shares of \$1 each	–	100%	Dormant
** Varitronix Display Technology (Shenzhen) Limited	The People's Republic of China	Rmb18,675,415	–	100%	Dormant
** Varitronix (Heyuan) Display Technology Limited	The People's Republic of China	Rmb56,102,551	–	80%	Not yet commenced business

* Companies not audited by KPMG. The financial statements of the subsidiaries not audited by KPMG reflect total assets and total turnover constituting approximately 17% (2001: 26%) and 26% (2001: 32%) respectively of the related consolidated totals.

#	Name of company	Type of legal entity
	Varitronix (Heyuan) Co. Ltd.	Sino-foreign co-operative joint venture
	Varitronix Pengyuan Limited	Sino-foreign equity joint venture
	Varitronix Display Technology (Shenzhen) Limited	Wholly foreign owned enterprise
	Varitronix (Heyuan) Display Technology Limited	Sino-foreign co-operative joint venture

NOTES ON THE FINANCIAL STATEMENTS (Continued)

(Expressed in Hong Kong dollars)

15. INTEREST IN ASSOCIATE

	The Group	
	2002 \$'000	2001 \$'000
Share of net assets	16,197	17,850
Amount due from associate	57	1,426
	<u>16,254</u>	<u>19,276</u>

Name of company	Country of incorporation and operation	Particulars of issued and paid up capital	Percentage of equity held by subsidiary	Principal activities
Varitronix EC (Malaysia) Sdn. Bhd.	Malaysia	11,324,250 class 'B' ordinary shares of Myr\$1 each	100% of class 'B' ordinary shares	Design, manufacture and sale of electrochromic mirror systems

The Group has an interest in 50% of the equity of Varitronix EC (Malaysia) Sdn. Bhd.

16. NON-TRADING SECURITIES

	The Group	
	2002 \$'000	2001 \$'000
Debt securities		
Listed		
– in Hong Kong	26,343	26,121
– outside Hong Kong	147,777	150,481
	<u>174,120</u>	176,602
Unlisted	31,223	6,750
	<u>205,343</u>	<u>183,352</u>
Equity securities		
Listed in Hong Kong	3,373	2,899
Unlisted	8,526	8,526
Investment funds listed outside Hong Kong	4,324	27,864
Unlisted investment funds	5,199	5,220
	<u>21,422</u>	<u>44,509</u>
Total	<u>226,765</u>	<u>227,861</u>

NOTES ON THE FINANCIAL STATEMENTS (Continued)

(Expressed in Hong Kong dollars)

17. TRADING SECURITIES

	The Group	
	2002 \$'000	2001 \$'000
Debt securities		
Listed outside Hong Kong	<u>58,034</u>	<u>36,008</u>
Equity securities		
Listed		
– in Hong Kong	2,747	2,112
– outside Hong Kong	<u>16,182</u>	<u>16,683</u>
	18,929	18,795
Unlisted investment funds	<u>7,599</u>	<u>26,217</u>
	<u>26,528</u>	<u>45,012</u>
Total	<u><u>84,562</u></u>	<u><u>81,020</u></u>

18. INVENTORIES

	The Group	
	2002 \$'000	2001 \$'000
Raw materials	91,845	118,098
Work in progress	46,898	43,037
Finished goods	<u>59,331</u>	<u>52,100</u>
	<u><u>198,074</u></u>	<u><u>213,235</u></u>

Raw materials and work in progress are stated after deducting a general provision. Included in finished goods are inventories of \$2,444,000 (2001: \$4,276,000) stated at estimated net realisable value.

NOTES ON THE FINANCIAL STATEMENTS (Continued)

(Expressed in Hong Kong dollars)

19. TRADE AND OTHER RECEIVABLES

Included in debtors, prepayments and deposits are trade debtors and bills receivable (net of specific provisions for bad and doubtful debts) with the following ageing analysis:

	The Group	
	2002 \$'000	2001 \$'000
Within 60 days of the invoice issue date	139,769	136,600
61 to 90 days after the invoice issue date	44,985	36,019
91 to 120 days after the invoice issue date	16,900	9,591
More than 120 days but less than 12 months after the invoice issue date	<u>35,183</u>	<u>43,659</u>
	<u><u>236,837</u></u>	<u><u>225,869</u></u>

Debts are due within 90 days from the date of the invoice.

20. CASH AND CASH EQUIVALENTS

	The Group		The Company	
	2002 \$'000	2001 \$'000	2002 \$'000	2001 \$'000
Deposits with banks and other financial institutions	402,055	291,994	–	–
Cash at bank and in hand	<u>64,018</u>	<u>76,584</u>	<u>596</u>	<u>687</u>
Cash and cash equivalents in the balance sheet	466,073	368,578	<u><u>596</u></u>	<u><u>687</u></u>
Bank overdrafts	<u>(5,198)</u>	<u>(7,907)</u>		
Cash and cash equivalents in the cash flow statement	<u><u>460,875</u></u>	<u><u>360,671</u></u>		

NOTES ON THE FINANCIAL STATEMENTS (Continued)

(Expressed in Hong Kong dollars)

21. BANK LOANS AND OVERDRAFTS

Unsecured, interest-bearing bank loans and overdrafts are repayable as follows:

	The Group	
	2002	2001
	\$'000	\$'000
Within 1 year or on demand	<u>61,706</u>	<u>39,924</u>
After 1 year but within 2 years	–	6,150
After 2 years but within 5 years	–	15,174
	<u>–</u>	<u>21,324</u>
	<u><u>61,706</u></u>	<u><u>61,248</u></u>

22. TRADE AND OTHER PAYABLES

Included in trade and other payables and bills payable are trade creditors and bills payable with the following ageing analysis:

	The Group	
	2002	2001
	\$'000	\$'000
Within 60 days of supplier invoice date	75,951	58,032
61 to 120 days after supplier invoice date	15,715	8,886
More than 120 days but within 12 months after supplier invoice date	<u>3,098</u>	<u>4,646</u>
	<u><u>94,764</u></u>	<u><u>71,564</u></u>

23. CONVERTIBLE NOTES

	Principal amount and carrying value \$'000
2001	
Balance at 1 January and 31 December 2001	<u><u>31,200</u></u>
2002	
Balance at 1 January and 31 December 2002	<u><u>31,200</u></u>

The notes in issue at 31 December 2002 may be converted up to 26 September 2010 at the option of the noteholders into shares of the Company at a conversion price, subject to adjustment in certain circumstances, of \$13.81 per share. The notes bear interest at 6 per cent per annum until conversion of any portion of the notes, and thereafter at 2 per cent per annum. In event of conversion, the noteholders are required to return to the Group the amount of interest in excess of the rate of 2 percent per annum previously received.

NOTES ON THE FINANCIAL STATEMENTS (Continued)

(Expressed in Hong Kong dollars)

24. SHARE CAPITAL

	2002		2001	
	No. of shares '000	Amount \$'000	No. of shares '000	Amount \$'000
Authorised:				
Ordinary shares of \$0.25 each	<u>400,000</u>	<u>100,000</u>	<u>400,000</u>	<u>100,000</u>
Issued and fully paid:				
At 1 January	302,477	75,619	292,160	73,040
Shares issued under share option scheme	233	59	153	38
Allotment of shares from scrip dividends	1,381	345	3,152	788
Shares issued as purchase consideration for shares in subsidiaries	–	–	7,112	1,778
Shares repurchased	–	–	(100)	(25)
At 31 December	<u>304,091</u>	<u>76,023</u>	<u>302,477</u>	<u>75,619</u>

Share Option Scheme

The Company had a Share Option Scheme ("Old Scheme") for the employees of the Group which was adopted on 6 June 1991, subsequently amended on 8 June 1999 and expired on 5 June 2001. The options are exercisable for a period of ten years following the date of grant.

A new Share Option Scheme of the Company was adopted on 22 June 2001 as an incentive to the Group's employees. The directors of the Company are authorised, at their discretion, to invite any employee or director, including executive and non-executive directors of any company in the Group, to take up options to subscribe for shares at a price determined by the board and notified to each grantee and which will not be less than 80 percent of the average of the closing prices of the shares on the Stock Exchange of Hong Kong Limited on the five trading days immediately preceding the date of offer of the option granted to such grantee or the nominal value of the shares, whichever is higher. The maximum entitlement of each employee is 25% of the aggregate of all shares subject to the Scheme. The options are exercisable for a period of up to ten years following the date of grant.

The maximum number of shares in respect of which options may be granted (together with options exercised and options then outstanding) under the new Share Option Scheme may not exceed 10 percent of the issued share capital of the Company, excluding any shares issued on exercise of options from time to time.

24. SHARE CAPITAL (Continued)

(i) **Movements in share options**

	2002 Number	2001 Number
At 1 January	3,792,250	3,992,250
Issued	4,724,500	1,033,000
Exercised	(232,500)	(153,000)
Lapsed	(1,496,500)	(883,500)
Cancelled	(130,000)	(196,500)
	<u>6,657,750</u>	<u>3,792,250</u>
At 31 December	<u>6,657,750</u>	<u>3,792,250</u>

(ii) **Terms of unexpired and unexercised share options at balance sheet date**

Date granted	Exercise period	Exercise price	2002 Number	2001 Number
1 January 1998	1 January 2000 to 31 December 2002	HK\$10.55	–	1,539,500
9 June 1999	9 July 1999 to 8 July 2009	HK\$10.90	596,750	622,750
1 June 2000	1 July 2000 to 30 June 2010	HK\$11.30	733,000	780,000
30 August 2001	30 August 2001 to 29 August 2011	HK\$3.06	616,500	850,000
13 September 2002	13 September 2002 to 12 September 2012	HK\$3.905	711,500	–
30 October 2002	31 October 2002 to 30 October 2012	HK\$4.605	4,000,000	–
			<u>6,657,750</u>	<u>3,792,250</u>

NOTES ON THE FINANCIAL STATEMENTS (Continued)

(Expressed in Hong Kong dollars)

24. SHARE CAPITAL (Continued)

(iii) Share options granted

Exercise period	Exercise price	2002 Number	2001 Number
30 August 2001 to 29 August 2011	HK\$3.06	–	1,033,000
13 September 2002 to 12 September 2012	HK\$3.905	724,500	–
31 October 2002 to 30 October 2012	HK\$4.605	4,000,000	–
		<u>4,724,500</u>	<u>1,033,000</u>

The consideration paid by each employee for the options granted was HK\$1.

(iv) Share options exercised

Exercise date	Exercise price	Market value per share at exercise date	Number	Proceeds received HK\$
2002				
7 January-26 November	HK\$3.06	HK\$3.90- HK\$6.95	226,500	693,090
26 November	HK\$3.906	HK\$4.65	<u>6,000</u>	<u>23,430</u>
			<u>232,500</u>	<u>716,520</u>
2001				
16 October-13 December	HK\$3.06	HK\$3.275- HK\$5.35	<u>153,000</u>	<u>468,180</u>

NOTES ON THE FINANCIAL STATEMENTS (Continued)

(Expressed in Hong Kong dollars)

25. RESERVES

(a) The Group

	Share premium	Exchange fluctuation reserve	Investment revaluation reserve	Other reserves <i>(note)</i>	Retained profits	Total
	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000
2001						
At 1 January 2001						
– as previously reported	537,164	(24,887)	(4,889)	–	714,388	1,221,776
– prior period adjustment in respect of employee benefits <i>(note 2)</i>	–	–	–	–	(5,065)	(5,065)
– as restated	537,164	(24,887)	(4,889)	–	709,323	1,216,711
Final dividends approved in respect of the previous year	–	–	–	–	(52,589)	(52,589)
Share premium arising from issue of shares	36,255	–	–	–	–	36,255
Premium paid on purchase of own shares	(346)	–	–	–	–	(346)
Revaluation deficit	–	–	(11,552)	–	–	(11,552)
Revaluation deficit transferred to the income statement on disposal of securities	–	–	700	–	–	700
Profit for the year (as restated)	–	–	–	–	43,281	43,281
Interim dividends declared in respect of the current year	–	–	–	–	(19,138)	(19,138)
Transfer to other reserves	–	–	–	455	(455)	–
Exchange differences	–	(155)	–	–	–	(155)
At 31 December 2001	<u>573,073</u>	<u>(25,042)</u>	<u>(15,741)</u>	<u>455</u>	<u>680,422</u>	<u>1,213,167</u>

NOTES ON THE FINANCIAL STATEMENTS (Continued)

(Expressed in Hong Kong dollars)

25. RESERVES (Continued)

(a) The Group (Continued)

	Share premium	Exchange fluctuation reserve	Investment revaluation reserve	Other reserves <i>(note)</i>	Retained profits	Total
	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000
2002						
At 1 January 2002						
– as previously reported	573,073	(25,042)	(15,741)	455	686,843	1,219,588
– prior period adjustment in respect of employee benefits <i>(note 2)</i>	–	–	–	–	(6,421)	(6,421)
– as restated	573,073	(25,042)	(15,741)	455	680,422	1,213,167
Special and final dividends approved in respect of the previous year	–	–	–	–	(19,673)	(19,673)
Share premium arising from issue of shares	6,099	–	–	–	–	6,099
Revaluation surplus	–	–	14,090	–	–	14,090
Revaluation deficit transferred to the income statement on disposal/liquidation of securities	–	–	8,255	–	–	8,255
Profit for the year	–	–	–	–	111,378	111,378
Interim dividends declared in respect of the current year	–	–	–	–	(13,341)	(13,341)
Transfer to other reserves	–	–	–	849	(849)	–
Exchange differences	–	3,847	–	–	–	3,847
At 31 December 2002	579,172	(21,195)	6,604	1,304	757,937	1,323,822

Profits are retained as follows:

	2002	2001 (restated)
By the Company and its subsidiaries	760,850	681,681
By associate	(2,913)	(1,259)
	757,937	680,422

Note: Other reserves comprise statutory reserves required in respect of the PRC incorporated subsidiaries.

NOTES ON THE FINANCIAL STATEMENTS (Continued)

(Expressed in Hong Kong dollars)

25. RESERVES (Continued)

(b) The Company

	Share premium <i>(note a)</i> \$'000	Contributed surplus <i>(note b)</i> \$'000	Retained profit \$'000	Total \$'000
2001				
At 1 January 2001	537,164	51,636	175,026	763,826
Final dividends approved in respect of the previous year	–	–	(52,589)	(52,589)
Shares premium arising from issue of shares	36,255	–	–	36,255
Premium paid on purchase of own shares	(346)	–	–	(346)
Profit for the year	–	–	51,448	51,448
Interim dividends declared in respect of the current year	–	–	(19,138)	(19,138)
	<u>573,073</u>	<u>51,636</u>	<u>154,747</u>	<u>779,456</u>
At 31 December 2001	<u><u>573,073</u></u>	<u><u>51,636</u></u>	<u><u>154,747</u></u>	<u><u>779,456</u></u>
2002				
At 1 January 2002	573,073	51,636	154,747	779,456
Special and final dividends approved in respect of the previous year	–	–	(19,673)	(19,673)
Shares premium arising from issue of shares	6,099	–	–	6,099
Profit for the year	–	–	33,345	33,345
Interim dividends declared in respect of the current year	–	–	(13,341)	(13,341)
	<u>579,172</u>	<u>51,636</u>	<u>155,078</u>	<u>785,886</u>
At 31 December 2002	<u><u>579,172</u></u>	<u><u>51,636</u></u>	<u><u>155,078</u></u>	<u><u>785,886</u></u>

Notes:

- (a) Under the Bye-laws of the Company, share premium is not distributable.
- (b) The excess value of the shares of the subsidiaries acquired pursuant to the Group reorganisation scheme in 1991 over the nominal value of the new shares of the company issued in exchange is credited to the contributed surplus account. Under the Companies Act 1981 of Bermuda (as amended) and the Bye-laws of the company, the contributed surplus is distributable to shareholders. However, the directors have no current intention to distribute this surplus.
- (c) The distributable reserves at 31 December 2002 amounted to \$206,714,000 (2001: \$206,383,000).

NOTES ON THE FINANCIAL STATEMENTS (Continued)

(Expressed in Hong Kong dollars)

26. SEGMENT REPORTING

Segment information is presented in respect of the Group's business and geographical segments. Business segment information is chosen as the primary reporting format because this is more relevant to the Group's internal financial reporting.

Business segment

As all of the Group's turnover and profits were derived from the design, manufacture and sale of liquid crystal displays and related products, accordingly no separate business segment analysis is presented for the Group.

Geographical segments

In presenting information on the basis of geographical segments, segment revenue is based on the geographical locations of customers. Segment assets and capital expenditure are based on the geographical location of the assets.

	Hong Kong and PRC		Rest of Asia		Europe		North America		Others	
	2002 \$'000	2001 \$'000	2002 \$'000	2001 \$'000	2002 \$'000	2001 \$'000	2002 \$'000	2001 \$'000	2002 \$'000	2001 \$'000
Revenue from external customers	<u>282,684</u>	<u>121,973</u>	<u>113,201</u>	<u>122,460</u>	<u>548,795</u>	<u>566,346</u>	<u>122,470</u>	<u>221,823</u>	<u>18,408</u>	<u>9,402</u>
Segment assets	<u>1,394,855</u>	<u>1,237,046</u>	<u>152,687</u>	<u>190,133</u>	<u>86,056</u>	<u>87,184</u>	<u>24,669</u>	<u>22,987</u>		
Capital expenditure incurred during the year	<u>87,511</u>	<u>65,772</u>	<u>9,941</u>	<u>32,357</u>	<u>1,667</u>	<u>415</u>	<u>26</u>	<u>49</u>		

Revenue from external customers located in Europe is analysed as follows:

	2002 \$'000	2001 \$'000
France	<u>151,288</u>	<u>150,175</u>
United Kingdom	<u>104,754</u>	<u>111,756</u>
Germany	<u>94,290</u>	<u>82,420</u>
Other European countries	<u>198,463</u>	<u>221,995</u>
	<u>548,795</u>	<u>566,346</u>

There is no major disparity in the ratios between turnover and profit in relation to the above geographical locations, hence no analysis is given of the profit contributions from the above geographical locations.

NOTES ON THE FINANCIAL STATEMENTS (Continued)

(Expressed in Hong Kong dollars)

27. CAPITAL AND OTHER COMMITMENTS

- (a) Capital commitments outstanding at 31 December 2002 not provided for in the financial statements were as follows:

	The Group	
	2002	2001
	\$'000	\$'000
Contracted for	<u>29,022</u>	<u>25,703</u>

- (b) At 31 December 2002, the total future minimum lease payments under non-cancellable operating leases for properties are payable as follows:

	2002	2001
	\$'000	\$'000
Within 1 year	1,144	1,762
After 1 year but within 5 years	<u>–</u>	<u>3,633</u>
	<u>1,144</u>	<u>5,395</u>

- (c) At 31 December 2002, the Group had commitments in respect of forward foreign exchange contracts in the next year as follows:

	2002	2001
	\$'000	\$'000
Within 1 year	<u>11,704</u>	<u>–</u>

28. CONTINGENT LIABILITIES

At 31 December 2002, the Company had contingent liabilities for guarantees given to banks in respect of banking facilities granted to certain subsidiaries, which were utilised to the extent of \$57,086,000 (2001: \$12,895,000).

29. MATERIAL RELATED PARTY TRANSACTIONS

There were no material related party transactions during the year (2001: Nil).

30. COMPARATIVE FIGURES

The presentation and classification of items in the consolidated cash flow statement have been changed due to the adoption of the requirements of SSAP 15 (revised 2001) "Cash flow statements". As a result, certain advances from banks have been excluded from the definition of cash equivalents, cash flow items from taxation, returns on investments and servicing of finance have been classified into operating, investing and financing activities respectively and a detailed breakdown of cash flows from operating activities has been included on the face of the consolidated cash flow statement. Comparative figures have been reclassified to conform with the current year's presentation.

FIVE YEAR SUMMARY

(Expressed in Hong Kong dollars)

	Year ended 31 December				
	1998	1999	2000	2001 (restated)	2002
	\$'000	\$'000	\$'000	\$'000	\$'000
Results:					
Turnover	<u>909,059</u>	<u>846,138</u>	<u>1,254,629</u>	<u>1,042,004</u>	<u>1,085,558</u>
Profit from operations (note)	327,957	299,482	215,886	43,393	140,838
Finance cost	(5,114)	(1,221)	(1,382)	(2,901)	(3,134)
Share of profit/(loss) of associate	<u>–</u>	<u>(12,956)</u>	<u>1,871</u>	<u>5,735</u>	<u>(1,654)</u>
Profit from ordinary activities before taxation	322,843	285,305	216,375	46,227	136,050
Taxation	(14,601)	(26,003)	(9,887)	(13,749)	(17,704)
Minority interests	<u>(7,394)</u>	<u>(3,086)</u>	<u>(6,145)</u>	<u>10,803</u>	<u>(6,968)</u>
Profit attributable to shareholders	<u>300,848</u>	<u>256,216</u>	<u>200,343</u>	<u>43,281</u>	<u>111,378</u>
Assets and liabilities:					
Fixed assets	342,231	334,498	385,288	393,658	398,080
Goodwill	–	–	–	33,386	31,704
Interest in associate	20,678	20,465	21,241	19,276	16,254
Non-trading securities	302,669	288,798	250,486	227,861	226,765
Net current assets	<u>693,680</u>	<u>832,435</u>	<u>696,350</u>	<u>689,394</u>	<u>786,624</u>
Total assets less current liabilities	1,359,258	1,476,196	1,353,365	1,363,575	1,459,427
Convertible notes	(5,522)	–	(31,200)	(31,200)	(31,200)
Minority interests	(26,543)	(29,556)	(27,349)	(22,265)	(28,382)
Other non-current liabilities	<u>–</u>	<u>–</u>	<u>–</u>	<u>(21,324)</u>	<u>–</u>
Net assets	<u>1,327,193</u>	<u>1,446,640</u>	<u>1,294,816</u>	<u>1,288,786</u>	<u>1,399,845</u>

Note: In order to comply with Hong Kong Statement of Standard Accounting Practice No. 34 "Employee benefits", the Group adopted a new accounting policy for long service payments in 2002. Figures for the year 2001 have been adjusted and it is not practicable to restate earlier years for comparison purposes.

PROPERTIES HELD BY THE GROUP

	Location	Existing use	Percentage holding
1.	Tseung Kwan O Town Lot No. 39 Kowloon.	Industrial	100%
2.	4th Floor and the attached flat roofs, Liven House, Nos. 61-63 King Yip Street, Kwun Tong, Kowloon.	Warehouse	100%
3.	6th Floor & 9th Floor, Liven House, Nos. 61-63 King Yip Street, Kwun Tong, Kowloon.	Warehouse	100%
4.	10th Floor, Liven House, Nos. 61-63 King Yip Street, Kwun Tong, Kowloon.	Warehouse	100%
5.	11th Floor, Liven House, Nos. 61-63 King Yip Street, Kwun Tong, Kowloon.	Leased	100%
6.	Flat F & G, 22nd Floor, Tower 1, Yue Man Centre, Nos. 300 and 302 Ngau Tau Kok Road, Kwun Tong, Kowloon.	Staff quarters	100%
7.	Flat B, 13th Floor, Tower 1, Yue Man Centre, Nos. 300 and 302 Ngau Tau Kok Road, Kwun Tong, Kowloon.	Staff quarters	100%
8.	Rooms 1003 and 1004, 10th Floor, Tower B Hungohm Commercial Centre, No. 37 Ma Tau Wai Road, Kowloon.	Leased	100%

PROPERTIES HELD BY THE GROUP *(Continued)*

	Location	Existing use	Percentage holding
9.	Plot 40, Phase 4, Bayan Lepas Free Trade Zone, 11900 Bayan Lepas, Penang, Malaysia.	Industrial	100%
10.	Plot 3, Phase 4, Bayan Lepas Free Trade Zone, 11900 Bayan Lepas, Penang, Malaysia.	Industrial	100%
11.	Sri Penang 6-2, Lega Road, Penang, Malaysia.	Staff quarters	100%
12.	Dongpu Town, Yuancheng District, Heyuan City, Guangdong, The People's Republic of China.	Industrial	80%
13.	Tangliaoxiacun, Xintang, Administrative Region, Dongpu Town, Yuancheng District, Heyuan City, Guangdong, The People's Republic of China.	Industrial	100%
14.	128 Heyuan Road, Yuancheng District Heyuan City, Guangdong, The People's Republic of China.	Industrial	80%
15.	Flat C601-604, 6th Floor, Block 10, Nam Wai Centre, Buket, Baoan County, Guangdong Province, The People's Republic of China.	Staff quarters	100%
16.	Unit 3 Milbanke Court, Milbanke Way, Bracknell, Berkshire, United Kingdom.	Office	100%

Note: The above properties are either freehold, held on long or medium term leases or have no specified lease term.

NOTICE OF ANNUAL GENERAL MEETING

NOTICE IS HEREBY GIVEN that an annual general meeting of the Company will be held at Ritz-Carlton Hong Kong, 3 Connaught Road, Central, Hong Kong on Monday, 12 May 2003 at 10:00 a.m. for the following purposes:–

1. To receive and consider the financial statements and the reports of the directors and auditors for the year ended 31 December 2002.
2. To declare a special dividend and a final dividend.
3. To re-elect directors and to fix the remuneration of directors.
4. To re-appoint auditors and authorise the directors to fix their remuneration.

By Order of the Board
Peter LO Chi Lik
Secretary

Hong Kong, 3 April 2003

Notes:–

1. A member of the Company entitled to attend and vote at the meeting is entitled to appoint one or more proxies to attend and vote in his stead. A proxy need not be a member of the Company.
2. To be valid, a proxy form, together with the power of attorney or other authority (if any) under which it is signed or a notarially certified copy thereof, must be deposited at the head office and principal place of business of the Company at 22 Chun Cheong Street, Tseung Kwan O Industrial Estate, Tseung Kwan O, Hong Kong not less than forty-eight hours before the appointed time for holding the meeting or any adjournment thereof.
3. The register of members of the Company will be closed from Tuesday, 6 May 2003 to Monday, 12 May 2003, both days inclusive, during which period no transfer of shares will be effected. To determine entitlements to the special dividend and the final dividend, all completed transfer forms accompanied by the relevant share certificates must be lodged with the Company's Hong Kong Branch Registrars, Computershare Hong Kong Investor Services Limited, 17th Floor, Hopewell Centre, 183 Queen's Road East, Hong Kong not later than 4:00 p.m. on Monday, 5 May 2003.