NAM TAI ELECTRONICS INC
Form 20-F
March 15, 2005

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 20-F

o **REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR (g) OF THE SECURITIES EXCHANGE ACT OF 1934**

or

þ **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the Fiscal Year Ended December 31, 2004

or

o **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

Commission File Number: 0-16673

Nam Tai Electronics, Inc.

(Exact name of registrant as specified in its charter)

British Virgin Islands
(Jurisdiction of incorporation or organization)

116 Main Street
3rd Floor
Road Town, Tortola
British Virgin Islands
(Address of principal executive offices)

Securities registered or to be registered pursuant to Section 12(b) of the Act:
Common Shares, $0.01 par value per share

Securities registered pursuant to Section 12(g) of the Act: NONE

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act: NONE

As of December 31, 2004, there were 42,664,536 common shares of the registrant outstanding.

Indicate by check mark whether the registrant: (i) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (ii) has been subject to such filing requirements for the past 90 days. Yes þ No o

Indicate by check mark which financial statement item the registrant has elected to follow: Item 17. o Item 18. þ

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SIGNATURES AND CERTIFICATIONS

Consents of Independent Accountants (to incorporation of their report on Financial Statements into the Company s Registration Statements on Forms F-3 and S-8)

This Annual Report on Form 20-F contains forward-looking statements. These statements are subject to certain risks and uncertainties that could cause actual results to differ materially from those anticipated in the forward-looking statements. Factors that might cause such a difference include, but are not limited to, those discussed in the section entitled Risk Factors under Item 3. Key Information.

Readers should not place undue reliance on forward-looking statements, which reflect management s view only as of the date of this Report. The Company undertakes no obligation to publicly revise these forward-looking statements to reflect subsequent events or circumstances. Readers should also carefully review the risk factors described in other documents the Company files from time to time with the Securities and Exchange Commission.

FINANCIAL STATEMENTS AND CURRENCY PRESENTATION

The Company prepares its consolidated financial statements in accordance with accounting principles generally accepted in the United States of America and publishes its financial statements in United States dollars.

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PART I

Unless the context otherwise requires, all references in this annual report, or Report, to Nam Tai , or we , or our , or us , and the Company refer to Nam Tai Electronics, Inc. and its consolidated subsidiaries and their respective predecessors. References to dollars or $ are to United States dollars.

Item 1. *Identity of Directors, Senior Management and Advisors*

Not applicable.

Item 2. *Offer Statistics and Expected Timetable*

Not applicable.

Item 3. *Key Information*

Selected Financial Data

Our historical consolidated financial statements are prepared in accordance with generally accepted accounting principles in the United States and are presented in U.S. dollars. The following selected statements of income data for each of the three years in the period ended December 31, 2004 and the balance sheet data as of December 31, 2003 and 2004 are derived from our consolidated financial statements and notes thereto included in this Report. The selected statements of income data for each of the two years in the period ended December 31, 2000 and 2001 and the balance sheet data as of December 31, 2000, 2001 and 2002 were derived from our audited financial statements, which are not included in this Report. The following data should be read in conjunction with the Section of the Report entitled Item 5, Operating and Financial Review and Prospects, and our consolidated financial statements including the related footnotes. All reference to numbers of common shares, per share data and stock option data have been adjusted to give effect to a three-for-one stock split effective on June 30, 2003 on a retroactive basis and for the purposes of earnings per share calculation, all references to numbers of common shares, and per share data have been adjusted to reflect an issuance of a stock dividend to shareholders at a ratio of one dividend share for every ten shares, or a ten-for-one stock dividend, effective on November 7, 2003.

	Year ended December 31, (in thousands except per share data)				
	2000	**2001**	**2002**	**2003**	**2004**
Consolidated statements of income data:					
Net sales third parties	$ 207,456	$ 212,934	$ 228,167	$ 385,524	$ 499,680
Net sales related party	6,232	21,072	7,849	20,782	34,181
Total net sales	213,688	234,006	236,016	406,306	533,861
Cost of sales	182,096	203,974	197,956	340,016	457,385
Gross profit	31,592	30,032	38,060	66,290	76,476
Operating costs and expenses:					
Selling, general and administrative	17,646	21,974	17,983	24,866	28,053

Research and development	3,489	2,954	2,686	4,037	5,045
Impairment of goodwill			339		
Total operating expenses	21,135	24,928	21,008	28,903	33,098
Income from operations	10,457	5,104	17,052	37,387	43,378
Other income (expenses) net	13,853	2,709	(6,043)	5,525	37,397
Interest expense	(165)	(178)	(790)	(121)	(195)
Income before income taxes and minority interests	24,145	7,635	10,219	42,791	80,580

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	Year ended December 31, (in thousands except per share data)				
	2000	2001	2002	2003	2004
Income taxes benefit (expense)	33	(227)	(773)	(399)	(879)
Income before minority interests and equity in income (loss) of affiliated companies	24,178	7,408	9,446	42,392	79,701
Minority interests	12	(230)	(164)	(1,067)	(6,010)
Income after minority interests	24,190	7,178	9,282	41,325	73,691
Equity in income (loss) of affiliated companies	(189)	1,867	10,741	498	(6,806)
Discontinued operation				1,979	
Net income	$ 24,001	$ 9,045	$ 20,023	$ 43,802	$ 66,885
Earnings per share:					
Basic	$ 0.80	$ 0.27	$ 0.57	$ 1.09	$ 1.57
Diluted	$ 0.78	$ 0.26	$ 0.57	$ 1.07	$ 1.57
Weighted average shares:					
Basic	30,077	33,905	34,885	40,336	42,496
Diluted	30,938	34,298	35,430	40,839	42,548

	At December 31, (in thousands)				
	2000	2001	2002	2003	2004
Consolidated balance sheet data:					
Cash and cash equivalents	$ 58,896	$ 58,676	$ 82,477	$ 61,827	$ 160,649
Working capital	88,969	83,525	87,184	93,474	218,243
Property, plant and equipment net	44,599	70,414	75,914	77,647	97,441
Total assets	208,370	224,573	275,086	297,695	460,473
Short-term debt, including current portion of long-term debt	1,523	3,687	14,970	3,004	4,955
Long-term debt, less current portion		12,860	2,812	1,688	5,163
Total debt	1,523	16,547	17,782	4,692	10,118
Shareholders equity	162,364	169,351	202,128	217,118	305,053
Common shares	306	312	360	412	426
Total dividend per share	0.45	0.13	0.49	1.00	0.48

Risk Factors

We may from time to time make written or oral forward-looking statements. Written forward-looking statements may appear in this document and other documents filed with the Securities and Exchange Commission, in press releases, in reports to shareholders, on our website, and other documents. The Private Securities Reform Act of 1995 contains a safe harbor for forward-looking statements on which the Company relies in making such disclosures. In connection with this safe harbor , we are hereby identifying important factors that could cause actual results to differ materially from those contained in any forward-looking statements made by us or on our behalf. Any such statements are qualified by reference to the following cautionary statements:

Risks Related to Our Business

We are dependent on a few large customers, the loss of any of which could substantially harm our business and operating results.

Historically, a substantial percentage of our sales have been to a small number of customers. During the years ended December 31, 2002, 2003 and 2004, sales to our customers accounting for 10% or more of our net sales aggregated approximately 60.2%, 46.7% and 47.9%, respectively, of our net sales. The loss of Epson Precision (HK) Ltd., Sharp Corporation, Wuxi Sharp Electronic Components Co., Ltd., or Motorola Inc., each of which accounted for more than 10% of our net sales during 2004, or a substantial reduction in orders from any of them, would materially and adversely impact our business and operating results.

Our quarterly and annual operating results are subject to significant fluctuations from a wide variety of factors.

Our quarterly and annual operating results are affected by a wide variety of factors that could materially and adversely affect our business and operating results during any period. This could result from any one or a combination of factors, such as:

- the timing, cancellation or postponement of orders;
- the type of product and related margins;
- our customers announcement and introduction of new products or new generations of products;
- the life cycles of our customers products;
- our timing of expenditures in anticipation of future orders;
- our effectiveness in managing manufacturing processes, including, interruptions or slowdowns in production and changes in cost and availability of components; and
- the mix of orders filled.

The volume and timing of orders received during a quarter are difficult to forecast. From time to time, our customers encounter uncertain and changing demand for their products. Customers generally order based on their forecasts. If demand falls below such forecasts or if customers do not control inventories effectively, they may reduce, cancel or postpone shipments of orders.

As a consequence of any of the above factors, our results of operations in any period should not be considered indicative of results to be expected in any future period, and fluctuations in operating results may also result in fluctuations in the market price of our common shares. Our results of operations in future periods may fall below the expectations of public market analysts and investors. This failure to meet expectations could cause the trading price of our common shares to decline substantially.

Cancellations or delays in orders could materially and adversely affect our gross margins and operating income.

Sales to our original equipment manufacturer, or OEM, customers are primarily based on purchase orders we receive from time to time rather than firm, long-term purchase commitments. Although it is our general practice to purchase raw materials only upon receiving a purchase order, for certain customers we will occasionally purchase raw materials based on such customers rolling forecasts. Further, during times of potential component shortages, we have purchased, and may continue to purchase, raw materials and component parts in the expectation of receiving purchase orders for products that use these components. In the event actual purchase orders are delayed, are not received or are cancelled, we would experience increased inventory levels or possible write-down of raw material inventory that could materially and adversely affect our business and operating results. In 2001, we wrote down inventory for $3.8 million for slow-moving raw materials relating to cancelled, reduced or delayed orders. Subsequently, we were able to use some of these raw materials in production or we received compensation for the unused raw materials from certain of our customers, and the gain of $2.0 million was recorded in cost of sales during 2002.

If we are unable to produce our new products in a high-quality and cost-effective manner, our gross margins and business and operating results could be materially and adversely affected.

We have experienced increased costs associated with developing advanced manufacturing techniques to produce our complex products on a mass scale and at a low cost. This has negatively impacted our gross margins. For example, our initial production runs of liquid crystal display, or LCD, modules experienced low production yields and other inefficiencies. We have commenced production of Bluetooth™ wireless headset accessory, radio frequency, or RF, modules, thin film transistor liquid crystal display, or TFT LCD, modules, color LCD modules and complementary metal oxide semiconductor, or CMOS, sensor modules and flexible printed circuit, or FPC, sub-assemblies in relation to which we have relatively limited manufacturing experience. We expect that a substantial portion of our growth will come from our manufacture of these products. While we expect and plan for such increased costs in our new product manufacturing cycle, we cannot precisely predict the time and expense required to overcome initial problems and to ensure reliability and high quality at an acceptable cost. The increased costs and other difficulties associated with manufacturing RF modules, TFT LCD modules, color LCD modules, CMOS sensor modules, FPC sub-assemblies and other new products could have a negative impact on our future gross margins. In addition, even if we develop capabilities to manufacture new products, there can be no guarantee that a market will exist for such products or that such products will adequately respond to market trends. If we invest resources to develop capabilities to manufacture new products, like the investment in our new factory, for which a market does not develop, our business and operating results would be seriously harmed. Even if the market for our services grows, it may not grow at an adequate pace.

Our inability to utilize capacity at our new factory could materially and adversely affect our business and operating results.

In order to expand our production capacity, we have built a new factory consisting of approximately 265,000 square feet adjacent to our principal manufacturing facilities in Shenzhen, the People s Republic of China, or China or the PRC. The construction was completed in December 2004 and we expect full operations to commence in April 2005. As of December 31, 2004, we had spent $15.0 million to cover the cost of construction and fixtures and equipment for the new factory. The financing for these improvements to our manufacturing facilities was obtained from our internal resources. We have committed substantial expenditures and resources constructing and equipping this factory but cannot guarantee that we will be able to fully utilize such additional capacity. Our factory utilization is dependent on our success in providing manufacturing services for new or other products that we intend to produce at that factory, such as Bluetooth™ wireless headset accessory for cellular phones, CMOS sensor modules for cellular phones with built-in camera function, home entertainment products and FPC sub-assemblies at a price and volume sufficient to absorb our increased overhead expenses. Demand for contract manufacturing of these products may not be as high as we expect, and we may fail to realize the expected benefit from our investment in our new factory.

We face increasing competition, which has had an adverse effect on our margins.

Although certain barriers to entry exist in providing electronics manufacturing services, or EMS, including technical expertise, substantial capital requirements, difficulties relating to building customer relationships and a large customer base, the barriers to entry are comparatively low and we are aware that manufacturers in Hong Kong and China may be developing or have developed the required technical capability and customer base to compete with our existing business.

Competition in the EMS industry is intense and is characterized by price erosion, rapid technological change, and competition from major international companies. This intense competition has resulted in pricing pressures, lower sales and reduced margins. Continuing competitive pressures could materially and adversely affect our business and operating results. Over the last several years our margins have declined substantially, from 17.2% in 1999 to approximately 14.3% in 2004. Continuing competitive pressures could materially and adversely affect our business and operating results.

We may not be able to compete successfully with our competitors, many of which have substantially greater resources than we do.

The electronics manufacturing services we provide are available from many independent sources as well as from our current and potential customers with in-house manufacturing capabilities. Our EMS competitors include Celestica, Inc., Flextronics International Ltd., Hon Hai Precision Industry Co., Ltd., Jabil Circuit, Inc., Sanmina-SCI Corporation and Solectron Corporation. Our principal competitors in the manufacture of our traditional product lines of calculators, personal organizers and linguistic products include Kinpo Electronics, Inc. and Inventec Co. Ltd. Our competitors in the manufacturing of image capturing devices and their modules include Lite-On Technology Corporation, The Primax Group and Logitech International S.A. Our principal competitors in the manufacture of mobile phone accessories include Elcoteq Network Corp. Our competitors in the manufacturing of RF modules include Wavecom and WKK International (Holdings) Ltd. Our competitors in the manufacturing of LCD panels include Truly International Holdings Ltd. and Varitronix International Ltd. We also have numerous competitors in the telecommunication, sub-assemblies and components product lines, including Philips, Samsung, Solectron and Varitronix International Ltd. Many of our competitors have greater financial, technical, marketing, manufacturing, regional shipping capabilities and logistics support and personnel resources than we do. As a result, we may be unable to compete successfully with these organizations in the future.

We must spend substantial amounts to maintain and develop advanced manufacturing processes and engage additional engineering personnel in order to attract new customers and business.

We operate in rapidly changing industries. Technological advances, the introduction of new products and new manufacturing and design techniques could materially and adversely affect our business unless we are able to adapt to those changing conditions. As a result, we are continually required to commit substantial funds for, and significant resources to, engaging additional engineering and other technical personnel and to purchase advanced design, production and test equipment.

Our future operating results will depend to a significant extent on our ability to continue to provide new manufacturing solutions that compare favorably on the basis of time to introduction, cost, and performance with the manufacturing capabilities of OEMs and competitive third-party suppliers. Our success in attracting new customers and developing new business depends on various factors, including:

utilization of advances in technology;

development of new or improved manufacturing processes for our customer s products;

delivery of efficient and cost-effective services; and

timely completion of the manufacture of new products.

We generally have no written agreements with suppliers to obtain components and our margins and operating results could suffer from increases in component prices.

We are sometimes responsible for purchasing components used in manufacturing products for our customers. We generally do not have written agreements with our suppliers of components. This typically results in our bearing the risk of component price increases because we may be unable to procure the required materials at a price level necessary to generate anticipated margins from the orders of our customers. Accordingly, increases in component prices could materially and adversely affect our gross margins and operating results.

Our business and operating results would be materially and adversely affected if our suppliers of needed components fail to meet our needs.

At various times, we have and continue to experience shortages of some of the electronic components that we use, and suppliers of some components lack sufficient capacity to meet the demand for these components. In some cases, supply shortages and delays in deliveries of particular components have resulted in curtailed production, or delays in production, of assemblies using that component, which contributed to an increase in our inventory levels and reduction in our gross margins. We expect that shortages and delays in deliveries of some components will continue. If we are unable to obtain sufficient components on a timely basis, we may experience manufacturing delays, which could harm our relationships with current or prospective customers and reduce our sales. We also depend on a small number of suppliers for certain of the

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components that we use in our business. For example, we purchase most of our integrated circuits from Toshiba Corporation and Sharp Corporation and certain of their affiliates. If we were unable to continue to purchase components from these limited source suppliers, our business and operating results would be materially and adversely affected.

Factors affecting the electronics industry in general and our customers in particular could harm our operations.

Most of our sales are to customers in the electronics industry, which is subject to rapid technological change, product obsolescence and short product life cycles and has suffered from an industry-wide slowdown since 2000. The factors affecting the electronics industry in general, or any of our major customers or competitors in particular, could have a material adverse effect on our business and operating results. Our success will depend to a significant extent on the success achieved by our customers in developing and marketing their products, including their products that use RF modules, color straight-twisted nematic, or STN, LCD modules, TFT LCD modules, CMOS sensor modules and FPC sub-assemblies, some of which may be new and untested. If our customers products become obsolete, fail to gain widespread commercial acceptance or become the subject of intellectual property disputes, our business and operating results could be materially and adversely affected.

Future acquisitions or strategic investments may not be successful and may harm our operating results.

An important element of our strategy is to review prospects for acquisition or strategic investments that would complement our existing companies and products, augment our market coverage and distribution ability or enhance our technological capabilities.

Future acquisitions or strategic investments could have a material adverse effect on our business and operating results because of:

- possible charges to operating results for purchased technology, restructuring or impairment charges related to goodwill or amortization expenses associated with intangible assets;
- potential increase in our expenses and working capital requirements and the incurrence of debt and contingent liabilities;
- difficulties in successfully integrating any acquired operations, technologies, customers products and businesses with our operations;
- diversion of our capital and management s attention to other business concerns;
- risks of entering markets or geographic areas in which we have limited prior experience; or
- potential loss of key employees of acquired organizations or inability to hire key employees necessary for expansion.

For example, in September 2004, we made an impairment to write down our $10.0 million investment in Alpha Star Investments Ltd. to its fair value of approximately $3.0 million, based on advice from an external valuer.

Our customers are dependent on shipping companies for delivery of our products and interruptions to shipping could materially and adversely affect our business and operating results.

Our customers rely on a variety of carriers for product transportation through various world ports. A work stoppage, strike or shutdown of one or more major ports or airports could result in shipping delays materially and adversely affecting our customers, which in turn could have a material adverse effect on our business and operating results. Similarly, an increase in freight surcharges due to rising fuel costs or general price increases could materially and adversely affect our business and operating results.

Because our operations are international, we are subject to significant worldwide political, economic, legal and other uncertainties.

We are incorporated in the British Virgin Islands and have subsidiaries incorporated in the Cayman Islands, Hong Kong, Macao, Japan and China. We have administrative offices in Hong Kong and Macao. We manufacture all of our products in China. As of December 31, 2004, approximately 86.7% of the net book value of our total fixed assets is located in China. We sell our products to customers in Hong Kong, North America, Europe, Japan, China and Southeast Asia. Our international operations may be subject to significant political and economic risks and legal uncertainties, including:

- changes in economic and political conditions and in governmental policies;
- changes in international and domestic customs regulations;
- wars, civil unrest, acts of terrorism and other conflicts;
- changes in tariffs, trade restrictions, trade agreements and taxation;
- difficulties in managing or overseeing foreign operations; and
- limitations on the repatriation of funds because of foreign exchange controls.

The occurrence or consequences of any of these factors may restrict our ability to operate in the affected region and decrease the profitability of our operations in that region.

Our operating results could be negatively impacted by seasonality.

Historically, our sales and operating results have been affected by seasonality. Sales of calculators, personal organizers and linguistic products are typically higher during the second and third quarters in anticipation of the start of the school year and the Christmas buying season. Similarly, our consumers orders for electronics products have historically been lower in the first quarter from both the closing of our factories in China for the Chinese New Year holidays and the general reduction in sales following the holiday season. These sales patterns may not be indicative of future sales performance.

Our results could be harmed if we have to comply with new environmental regulations.

Our operations create some environmentally sensitive waste that may increase in the future depending on the nature of our manufacturing operations. The general issue of the disposal of hazardous waste has received increasing attention from Chinese national and local governments and foreign governments and agencies and has been subject to increasing regulation. Currently, relevant Chinese environmental protection laws and regulations impose fines on discharge of waste materials and empower certain environmental authorities to close any facility which causes serious environmental problems. Although it has not been alleged that we have violated any current environmental regulations by China government officials, there is no assurance that the Chinese government will not amend its current environmental protection laws and regulations. Our business and operating results could be materially and adversely affected if we were to increase expenditures to comply with environmental regulations affecting our operations.

Our insurance coverage may not be sufficient to cover the risks related to our operations and losses.

We have not experienced any major accidents in the course of our operations which have caused significant property damage or personal injuries. However, there is no assurance that we will not experience major accidents in the future. Although we have purchased the necessary insurances, including a business interruption policy, a fidelity guarantee policy and policies covering losses or damages in respect of buildings machineries, equipments and inventories, the occurance of certain incidents such as earthquake, war and flood, and the consequences resulting from them, may not be covered adequately, or at all, by the insurance policies under which we are protected. We also face exposure to product liability claims in the event that any of our products is alleged to have resulted in property damage, bodily injury or other adverse effects. We only have product liability insurance for some of our products. Losses incurred or payments we may be required to make, may have a material adverse effect on our results of operations if such losses or payments are not fully insured.

We are a defendant in putative class action lawsuits and this litigation could harm our business regardless of the final outcome.

On March 11, 2003, we were served with a complaint in an action captioned *Michael Rocco v. Nam Tai, et al.*, 03 Civ. 1148 (S.D.N.Y.), or the Rocco Action. In addition to Nam Tai, certain directors are named as defendants. On or about April 9, 2003, a second complaint was filed in an action captioned *A.J. & Celine Steigler v. Nam Tai, et al.*, 03 Civ. 2462 (S.D.N.Y.) or the Steigler Action, and together with the Rocco Action, the Actions. The Actions have been consolidated since July 2003 and purport to represent a putative class of persons who purchased the common stock of Nam Tai from July 29, 2002 through February 18, 2003. Plaintiffs in the Actions assert claims under Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 and allege that misrepresentations and/or omissions were made during the alleged class period concerning the partial reversal of an inventory provision and a charge to goodwill related to Nam Tai s LCD panels and transformers segment, or LPT segment. Defendants motion to dismiss was denied on September 27, 2004. The putative class action has not been certified as a class action by the court but we expect plaintiffs to seek such certification in the near future. The court has set May 23, 2005 to hear such a certification motion. Nam Tai believes it has meritorious defenses and it intends to defend the case vigorously. Nam

Tai is aware of no other actions that have been filed which relate to these matters. The ultimate outcome of this litigation cannot be presently determined. However, this litigation could be very costly and divert our management s attention and resources. In addition, we have no insurance covering our liability, if any, or that of our officers and directors, and we will have to pay the costs of the defense. Any adverse determination in this litigation could also subject us to significant liabilities, any or all of which could materially and adversely affect our business and operating results.

We depend on our executive officers and skilled management personnel.

Our success depends to a large extent upon the continued services of our executive officers. Generally, our employees are bound by employment or non-competition agreements. However, we cannot assure you that we will retain our executive officers and other key employees. We could be seriously harmed by the loss of any of our executive officers. In order to manage our growth, we will need to recruit and retain additional skilled management personnel and if we are not able to do so our business and our ability to continue to grow could be harmed. We maintain no key person insurance on these individuals. The loss of service of any of these officers or key management personnel could have a material adverse effect on our business growth and operating results.

We may be unable to succeed in recovering on our judgment debts against Tele-Art, Inc.

We have two judgments in our favor against Tele-Art, Inc. awarded by The High Court of Justice in the British Virgin Islands for approximately $35.0 million. Because Tele-Art, Inc. is in liquidation, we may not realize the entire amount of our judgments, and the actual amount of the recovery, if any, is uncertain and dependent on a number of factors. We may incur substantial additional costs in pursuing our recovery, and such costs may not be recoverable.

We could become involved in intellectual property disputes.

We do not have any patents, licenses, or trademarks material to our business. Instead, we rely on trade secrets, industry expertise and our customers sharing of intellectual property with us. We may be notified that we are infringing patents, copyrights or other intellectual property rights owned by other parties. In the event of an infringement claim, we may be required to spend a significant amount of money to develop a non-infringing alternative or to obtain licenses. We may not be successful in developing such an alternative or obtaining a license on reasonable terms, if at all. Any litigation, even without merit, could result in substantial costs and diversion of resources and could materially and adversely affect our business and operating results.

We may not pay dividends in the future.

Although we have declared dividends during each of the last eleven years, we may not be able to declare them or may decide not to declare them in the future. Our China subsidiaries are required to reserve 10% of profits for future development, which may affect our ability to declare dividends. We will determine the amounts of the dividends when they are declared and even if dividends are declared in the future, we may not continue them in any future period.

We are subject to the risk of increased taxes.

We base our tax position upon the anticipated nature and conduct of our business and upon our understanding of the tax laws of the various countries in which we have assets or conduct activities. Our tax position, however, is subject to review and possible challenge by taxing authorities and to possible changes in law. We cannot determine in advance the extent to which some jurisdictions may assess additional tax or interest and penalties on such additional taxes.

Several places in which we are located allow for tax holidays or provide other tax incentive to attract and retain business. We have obtained holidays or other incentives where available. Our taxes could increase if certain tax holidays or incentives are retracted, or if they are not renewed upon expiration, or tax rates applicable to us in such jurisdictions are otherwise increased.

Recently enacted changes in the securities laws and regulations are likely to increase our costs.

The Sarbanes-Oxley Act of 2002 that became law in July 2002 has required changes in some of our corporate governance, securities disclosure and compliance practices. In response to the requirements of that act, the Securities and Exchange Commission, or SEC, and the New York Stock Exchange, or NYSE, have promulgated new rules on a variety of subjects. Compliance with these new rules as well as the Sarbanes-Oxley Act of 2002 has increased our legal, financial and accounting costs, and we expect these increased costs to continue indefinitely, particularly as new rules and regulations, including Section 404 of the Sarbanes-Oxley Act of 2002, come into effect. We also expect these developments to make it more difficult and more expensive for us to obtain director and officer liability insurance, and we may be forced to accept reduced coverage or incur substantially higher costs to obtain coverage. Likewise, these developments may make it more difficult for us to attract and retain qualified members of our board of directors or qualified executive officers.

Risks Related to Our Operations in China, Hong Kong, Macao and Japan

Our manufacturing facilities are located in China and some of our subsidiaries and several of our customers and suppliers are located in Hong Kong and China. Some of our subsidiaries are located in Hong Kong, Macao and Japan. As a result, our operations and assets are subject to significant political, economic, legal and other uncertainties associated with doing business in China, Hong Kong, Macao and Japan, which are discussed in more detail below.

We are exposed to risks associated with doing business in China.

Our principal manufacturing operations are located in Shenzhen, China. These operations could be severely impacted by evolving interpretation and enforcement of legal standards, by strains on Chinese energy, transportation, communications, trade and other infrastructures, by conflicts, embargoes, increased tensions or escalation of hostilities between China and Taiwan, and by other trade customs and practices that are dissimilar to those in the United States and Europe. Interpretation and enforcement of China s laws and regulations continue to evolve and we expect differences in interpretation and enforcement to continue in the foreseeable future. Further, we may be exposed to fluctuations in the value of the renminbi yuan, or RMB, the local currency of China. Recently, China has been confronted with international pressure demanding the appreciation of the RMB. Should the Chinese government allow a significant RMB appreciation, our component and other raw material costs could increase and could adversely affect our financial results.

The Chinese government could change its policies toward, or even nationalize, private enterprise, which could harm our business and operating results.

Over the past several years, the Chinese government has pursued economic reform policies including the encouragement of private economic activities and decentralization of economic regulation with a move towards a market economy. The Chinese government may not continue to pursue these policies or may significantly alter them to our detriment from time to time without notice. Changes in policies by the Chinese government resulting in changes in laws, regulations, or their interpretation, or the imposition of confiscatory taxation, restrictions on currency conversion or imports and sources of supply could materially and adversely affect our business and operating results. The nationalization or other expropriation of private enterprises by the Chinese government could result in the total loss of our investment in China.

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The Chinese legal system has inherent uncertainties that could materially and adversely impact our ability to enforce the agreements governing our factories and to do business.

We do not own the land on which our factories in China are located. We occupy our principal manufacturing facilities under land use agreements with agencies of the Chinese government and we occupy other facilities under lease agreements with peasant collectives or other companies. The performance of these agreements and the operations of our factories are dependent on our relationship with the local government. Our operations and prospects would be materially and adversely affected by the failure of the local government to honor these agreements or an adverse change in the law governing them. In the event of a dispute, enforcement of these agreements could be difficult in China. Unlike the United States, China has a civil law system based on written statutes in which judicial decisions have limited precedential value. The Chinese government has enacted laws and regulations dealing with economic matters such as corporate organization and governance, foreign investment, commerce, taxation and trade. However, its experience in implementing, interpreting and enforcing these laws and regulations is limited, and our ability to enforce commercial claims or to resolve commercial disputes in China is unpredictable. These matters may be subject to the exercise of considerable discretion by agencies of the Chinese government, and forces and factors unrelated to the legal merits of a particular matter or dispute may influence their determination.

Fire, severe weather, flood or earthquake could cause significant damage to our facilities in China and disrupt our business operations.

Our products are manufactured exclusively at our factories located in China. Fire fighting and disaster relief or assistance in China is not well developed. Material damage to, or the loss of, our factories due to fire, severe weather, flood, earthquake or other acts of God or cause may not be adequately covered by proceeds of our insurance coverage and could materially and adversely affect our business and operating results. In addition, any interruptions to our business caused by such disasters could harm our business and operating results.

Controversies affecting China s trade with the United States could harm our results of operations or depress our stock price.

While China has been granted permanent most favored nation trade status in the United States through its entry into the World Trade Organization, controversies between the United States and China may arise that threaten the status quo involving trade between the United States and China. These controversies could materially and adversely affect our business by, among other things, causing our products in the United States to become more expensive resulting in a reduction in the demand for our products by customers in the United States. Political or trade friction between the United States and China, whether or not actually affecting our business, could also materially and adversely affect the prevailing market price of our common shares.

Changes to Chinese tax laws and heightened efforts by the Chinese tax authorities to increase revenues could subject us to greater taxes.

Under applicable Chinese law, we have been afforded a number of tax concessions by, and tax refunds from, the Chinese tax authorities on a substantial portion of our operations in China by reinvesting all or part of the profits attributable to our Chinese manufacturing operations. However, the Chinese tax system is subject to substantial uncertainties with respect to its interpretation and enforcement. Following the Chinese government s program of privatizing many state-owned enterprises, the Chinese government has attempted to augment its revenues through heightened tax collection efforts. Continued efforts by the Chinese government to increase tax revenues could result in decisions or interpretations of the tax laws by the Chinese tax authorities that would increase our future tax liabilities or deny us expected concessions or refunds. For example, the tax reform of reducing the VAT tax refund from 17% to 13%, with effect from January 1, 2004, has adversely affected our margins.

Our results have been affected by changes in currency exchange rates. Changes in currency rates involving the Japanese yen, Hong Kong dollar or Chinese renminbi could increase our expenses.

Our financial results have been affected by currency fluctuations, resulting in total foreign exchange gains of $189,000 during the year ended December 31, 2004, total foreign exchange losses of $62,000 during the year ended December 31, 2003 and total foreign exchange losses of $345,000 during the year ended December 31, 2002. We sell most of our products in United States dollars and pay our expenses in United States dollars, Japanese yen, Hong Kong dollars, and Chinese renminbi. While we face a variety of risks associated with changes among the relative value of these currencies, we believe the most significant exchange risk presently results from material purchases we make in Japanese yen. Approximately 8%, 16% and 6% of our material costs have been in Japanese yen during the years ended December 31, 2002, 2003 and 2004, respectively, but sales made in Japanese yen accounted for less than 11% of sales for each of the last three years. An appreciation of the Japanese yen against the United States dollar would increase our expenses when translated into United States dollars and would materially and adversely affect our margins unless we made sufficient sales in Japanese yen to offset against material purchases made in Japanese yen.

Approximately 8% and 6% of our revenues and 12% and 12% of our expenses were in Chinese renminbi and Hong Kong dollars, respectively, during the year ended December 31, 2004. Approximately 1% and 8% of our revenues and 13% and 12% of our expenses were in Chinese renminbi and Hong Kong dollars, respectively, during the year ended December 31, 2003. An appreciation of the Chinese renminbi or Hong Kong dollar against the United States dollar would increase our expenses when translated into United States dollars and could materially and adversely affect our margins. In addition, a significant devaluation in the Chinese renminbi or Hong Kong dollar could harm our business if it destabilizes the economy of China or Hong Kong, creates serious domestic problems or increases our borrowing costs.

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We have suffered losses from hedging against our currency exchange risk.

From time to time, we have attempted to hedge our currency exchange risk. We did not engage in currency hedging transactions for fiscal year 2003 and 2004. We have experienced in the past and may experience in the future losses as a result of currency hedging.

Political and economic instability in Hong Kong could harm our operations.

Some of our subsidiaries offices and several of our customers and suppliers are located in Hong Kong, formerly a British Crown Colony. Sovereignty over Hong Kong was resumed by China effective July 1, 1997. Since then, Hong Kong has become a Special Administrative Region of China, enjoying a high degree of autonomy except for foreign and defense affairs. Moreover, China s political system and policies are not practiced in Hong Kong. Under the principle of one country, two systems , Hong Kong maintains a legal system that is based on the common law and is different from that of China. It is generally acknowledged as an open question whether Hong Kong s future prosperity in its role as a hub and gateway to China after China s accession to the World Trade Organization (introducing a market liberalization in China) will be diminished. The continued stability of political, economic or commercial conditions in Hong Kong remains uncertain, and any instability could materially and adversely impact our business and operating results.

The spread of severe acute respiratory syndrome or similar illnesses may have a negative impact on our business and operating results.

In March 2003, several economies in Asia, including Hong Kong and southern China, where our operations are located, were affected by the outbreak of severe acute respiratory syndrome, or SARS. If there is a recurrence of a serious outbreak of SARS, it may adversely affect our business and operating results. For example, the future SARS outbreak could result in quarantines or closures to some of our factories if our employees are infected with SARS and ongoing concerns regarding SARS, particularly its effect on travel, could negatively impact our China-based customers and suppliers and our business and operating results.

In addition, there has recently been an outbreak of avian influenza in humans in Asian countries, including Vietnam, South Korea and Japan, which has proven fatal in some instances. As the human death toll continues to grow, many are concerned that the virus will mutate and trigger a human pandemic. If such an outbreak were to spread to southern China, where our operation facilities are located, it may adversely affect our business operating results.

We conduct operations in a number of countries and the effect of business, legal and political risks associated with international operations could significantly harm us.

We conduct operations in number of countries. There are risks inherent in doing business in international markets, including:

- Difficulties in staffing and managing international operations;
- Compliance with laws and regulations, including environmental laws, which vary from country to country and over time, increasing the costs of compliance and potential risks of non-compliance;
- Exposure to political and financial instability, leading to currency exchange losses, collection difficulties or other losses;
- Exposure to fluctuations in the value of local currencies;

Changes in value-added tax or VAT reimbursement;

Imposition of currency exchange controls; and

Delays from customs brokers or government agencies.

Any of these risks could significantly harm our business, financial condition and operating results.

Risks Related to Our Industry

We are exposed to general economic conditions. Any slowdown in the technology products industry may affect our business and operating results adversely.

As a result of the economic downturn in the United States and internationally, and reduced capital spending, sales to OEMs in the electronics industry declined beginning in the second quarter of fiscal year 2001 and continuing through 2002. Lower consumer demand and high customer inventory levels have resulted in the delay and cancellation of orders for nearly all types of electronic products. As a result of order cancellations in 2001, we were required to write down slow-moving inventory, which materially and adversely impacted our net income in 2001. Although the industry experienced a recovery in 2003 and 2004, we cannot assure that this recovery is sustainable or that the industry will not further decline. If the economic conditions in the United States or the other markets we serve worsen, particularly in the electronics and contract manufacturing businesses particularly, or if a wider or global economic slowdown occurs, this could materially and adversely impact our business and operating results.

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Our business and operating results are dependent on growing global outsourcing trends.

Over the last two decades, the EMS industry experienced rapid change and growth as the capabilities of EMS companies continued to expand and consumer electronic product manufacturers adopted, and became increasingly reliant on, manufacturing outsourcing strategies to remain competitive. Despite the slow down of the EMS industry in 2001 and 2002 as a result of consumer electronic product manufacturers decreasing production requirement, growth has been renewed in 2003 and 2004 and we believe that the EMS industry has the potential for further growth as many consumer electronic product manufacturers continue to favor outsourcing over internal manufacturing, and the market for outsourcing, as a whole, continues to flourish. However, there can be no assurance that the trends of adopting manufacturing outsourcing strategies by consumer electronic product manufacturers will continue to grow. If the growing outsourcing trends discontinue, this could materially and adversely impact our business and operating results.

Risks Related to Ownership of Our Common Shares

The market price of our shares will likely be subject to substantial price and volume fluctuations.

The markets for equity securities have been volatile and the price of our common shares has been and could continue to be subject to wide fluctuations in response to variations in operating results, news announcements, trading volume, sales of common shares by our officers, directors and our principal shareholders, customers, suppliers or other publicly traded companies, general market trends both domestically and internationally, currency movements and interest rate fluctuations. Certain events, such as the issuance of common shares upon the exercise of our outstanding stock options could also materially and adversely affect the prevailing market price of our common shares.

Further, the stock markets have recently experienced extreme price and volume fluctuations that have affected the market prices of equity securities of many companies and that have been unrelated or disproportionate to the operating performance of such companies. These fluctuations may materially and adversely affect the market price of our common shares.

The concentration of share ownership in our senior management allows them to control or substantially influence the outcome of matters requiring shareholder approval.

On February 28, 2005, members of our management and Board of Directors as a group beneficially owned approximately 42.0% of our common shares. As a result, acting together, they may be able to control and substantially influence the outcome of all matters requiring approval by our shareholders, including the election of directors and approval of significant corporate transactions. This ability may have the effect of delaying or preventing a change in control of Nam Tai, or causing a change in control of Nam Tai that may not be favored by our other shareholders.

If we do not receive an unqualified opinion on the adequacy of our internal control over financial reporting as of December 31, 2006 and future year-ends as required by Section 404 of the Sarbanes-Oxley Act of 2002, investors could lose confidence in the reliability of our financial statements, which could result in a decrease in the value of our shares.

As directed by Section 404 of the Sarbanes-Oxley Act of 2002, the SEC adopted rules requiring public companies to include a report of management on the company s internal control structure and procedures over financial reporting in their annual reports on Form 20-F that contains an assessment by management of the effectiveness of the company s internal control structure and procedures over financial reporting. In addition, the public accounting firm auditing the company s financial statements must attest to and report on management s assessment of the effectiveness of the company s internal control structure and procedures over financial reporting. While we intend to conduct a rigorous review of our internal control structure and procedures over financial reporting in order to assure compliance with Section 404 requirements, if our independent auditors interpret Section 404 requirements and the related rules and regulations differently from us or if our independent auditors are not satisfied with our internal control structure and procedures over financial reporting or with the level at which it is documented, operated or reviewed, they may decline to attest to management s assessment or issue a qualified report. This could result in an adverse reaction in the financial markets due to a loss of confidence in the reliability of our financial statements, which could cause the market price of our shares to decline.

Changes to financial accounting standards may affect our reported results of operations and could result in a decrease in the value of our shares.

The Financial Accounting Standards Board recently published amendments to Statement of Financial Accounting Standards No. 123 that would require stock-based compensation issued to employees to be treated as compensation expense using the fair value method. If we are required to record an expense for our stock-based compensation plans using the fair value method, we would incur significant compensation charges. Although we currently are not required to record any compensation expense in connection with options granted that have an exercise price equal to fair market value of our common stock at the grant date, if future laws and regulations require us to treat all stock-based compensation as a compensation expense using the fair value method, our results or operations could be adversely affected. For discussion of our employee stock option and employee stock purchase plans, see Note 2 Summary of Significant Accounting Policies Stock Options and Note 11 Shareholders Equity to the Consolidated Financial Statements.

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Risks Related to Our Foreign Private Issuer Status

It may be difficult to serve us with legal process or enforce judgments against our management or us.

We are a British Virgin Islands holding corporation with subsidiaries in Hong Kong, Macao, Japan and China. We have appointed Stephen Seung, 2 Mott Street, Suite 601, New York, New York 10013 as our agent upon whom process may be served in any action brought against us under the securities laws of the United States. However, outside the United States, it may be difficult for investors to enforce judgments against us obtained in the United States in any of these actions, including actions based upon civil liability provisions of the Federal securities laws. In addition, all of our officers and most of our directors reside outside the United States, and all of our assets, and the assets of those persons who reside outside of the United States, are located outside of the United States. As a result, it may not be possible for investors to effect service of process within the United States upon those persons, or to enforce against those persons or use judgments obtained in United States courts grounded upon the liability provisions of the United States securities laws. There is substantial doubt as to the enforceability against us or any of our directors and officers located outside of the United States in original actions or in actions for enforcement of judgments of United States courts of liabilities based solely on the civil liability provisions of the securities laws of the United States.

No treaty exists between Hong Kong or the British Virgin Islands and the United States providing for the reciprocal enforcement of foreign judgments. However, the courts of Hong Kong and the British Virgin Islands are generally prepared to accept a foreign judgment as evidence of a debt due. An action may then be commenced in Hong Kong or the British Virgin Islands for recovery of this debt. A Hong Kong or British Virgin Islands court will only accept a foreign judgment as evidence of a debt due if:

- the judgment is for a liquidated amount in a civil matter;
- the judgment is final and conclusive and has not been stayed or satisfied in full;
- the judgment is not, directly or indirectly, for the payment of foreign taxes, penalties, fines or charges of a like nature (in this regard, a Hong Kong or British Virgin Islands court is unlikely to accept a judgment for an amount obtained by doubling, trebling or otherwise multiplying a sum assessed as compensation for the loss or damage sustained by the person in whose favor the judgment was given);
- the judgment was not obtained by actual or constructive fraud or duress;
- the foreign court has taken jurisdiction on grounds that are recognized by the common law rules as to conflict of laws in Hong Kong or the British Virgin Islands;
- the proceedings in which the judgment was obtained were not contrary to natural justice (i.e., the concept of fair adjudication);
- the proceedings in which the judgment was obtained, the judgment itself and the enforcement of the judgment are not contrary to the public policy of Hong Kong or the British Virgin Islands;
- the person against whom the judgment is given is subject to the jurisdiction of the Hong Kong or the British Virgin Islands court; and
- the judgment is not on a claim for contribution in respect of damages awarded by a judgment, which does not satisfy the criteria stated previously.

Enforcement of a foreign judgment in Hong Kong or the British Virgin Islands may also be limited or affected by applicable bankruptcy, insolvency, liquidation, arrangement and moratorium, or similar laws relating to or affecting creditors rights generally, and will be subject to a statutory limitation of time within which proceedings may be brought.

No treaty exists between Macao and the United States providing for the reciprocal enforcement of foreign judgments. However, the courts of Macao are generally prepared to accept a foreign judgment as evidence of a debt due. An action may then be commenced in Macao for recovery of this debt. A Macao court will only accept a foreign judgment as evidence of a debt due if:

- there is no doubt to the authenticity of the judgment documents and the understanding of the judgment;
- pursuant to the law of the place of judgment, the judgment is final and conclusive;
- the judgment was not obtained by fraud or the matter in relation to the judgment is not within the exclusive jurisdiction of Macao courts;
- the judgment will not be challenged on the ground that the relevant matter has been adjudicated by the Macao court, except matters which have first been adjudicated by courts outside Macao;
- pursuant to the law of the place of the judgment, the defendant has been summoned and the proceedings in which the judgment was obtained were not contrary to natural justice; and
- the enforcement of the judgment will not cause any orders that may result in apparent public disorder.

Enforcement of a foreign judgment in Macao may also be limited or affected by applicable bankruptcy, insolvency, liquidation, arrangement and moratorium, or similar laws relating to or affecting creditors rights generally, and will be subject to a statutory limitation of time within which proceedings may be brought.

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Future issuances of preference shares could materially and adversely affect the holders of our common shares or delay or prevent a change of control.

Our Board of Directors may amend our Memorandum and Articles of Association without shareholder approval to create from time to time and issue one or more classes of preference shares (which are analogous to preferred stock of corporations organized in the United States). While currently no preference shares are issued or outstanding, we may issue preference shares in the future. Future issuance of preference shares could materially and adversely affect the rights of the holders of our common shares, or delay or prevent a change of control.

Our status as a foreign private issuer exempts us from certain of the reporting requirements under the Securities Exchange Act of 1934 and corporate governance standards of the NYSE, limiting the protections and information afforded to investors.

We are a foreign private issuer within the meaning of rules promulgated under the Securities Exchange Act of 1934. As such, we are exempt from certain provisions applicable to United States public companies including:

- the rules under the Securities Exchange Act of 1934 requiring the filing with the SEC of quarterly reports on Form 10-Q, current reports on Form 8-K or annual reports on Form 10-K;

- the sections of the Securities Exchange Act of 1934 regulating the solicitation of proxies, consents or authorizations in respect of a security registered under the Securities Exchange Act of 1934;

- the provisions of Regulation FD aimed at preventing issuers from making selective disclosures of material information; and

- the sections of the Securities Exchange Act of 1934 requiring insiders to file public reports of their stock ownership and trading activities and establishing insider liability for profits realized from any short-swing trading transaction (i.e., a purchase and sale, or sale and purchase, of the issuer s equity securities within less than six months).

In addition, because the Company is a foreign private issuer, certain corporate governance standards of the NYSE that are applied to domestic companies listed on that exchange may not be applicable to us.

Because of these exemptions, investors are not afforded the same protections or information generally available to investors holding shares in public companies organized in the United States or traded on the NYSE.

Item 4. *Information on the Company*

History and Development of Nam Tai

Nam Tai Electronics, Inc. was founded in 1975 and moved its manufacturing facilities to China in 1980 to take advantage of lower overhead costs, lower material costs and competitive labor rates available and subsequently relocated to Shenzhen, China in order to capitalize on opportunities offered in southern China. We were reincorporated as a limited liability International Business Company under the laws of the British Virgin Islands in August 1987. Our principal manufacturing and design operations are based in Shenzhen, China, approximately 30 miles from Hong Kong. Our PRC headquarters is at Macao, China. Some of our subsidiaries offices are located in Hong Kong and Macao, which provides us access to Hong Kong s and Macao s infrastructure of communication and banking and facilitates management of our China operations. One of our subsidiaries also has an office in Japan.

Our corporate administrative matters are conducted in the British Virgin Islands through our registered agent, McW. Todman & Co., McNamara Chambers, P.O. Box 3342, Road Town, Tortola, British Virgin Islands. Our agent for service of process in the United States is Stephen Seung, 2 Mott Street, Suite 601, New York, New York 10013. Our principal executive offices are located in the British Virgin Islands at 116 Main Street, 3rd Floor, Road Town, Tortola, British Virgin Islands, and the telephone number is (284) 494-7752.

In 1978, Mr. Koo, the founder of the Company, began recruiting operating executives from the Japanese electronics industry. These executives brought years of experience in Japanese manufacturing methods, which emphasize quality, precision, and efficiency in manufacturing. Senior management currently includes Japanese professionals who provide technical expertise and work closely with both our Japanese component suppliers and customers.

For a number of years, we specialized in manufacturing large-volume, hand-held digital consumer electronic products and established a leading position in electronic calculators and handheld organizers for OEMs such as Texas Instruments Incorporated and Sharp Corporation. Over the years, we have broadened our product mix to include a range of digital products for business and personal use, as well as key components and sub-assemblies for telecommunications and consumer electronic products. In August 1999, we established Nam Tai Telecom (Hong Kong) Company Limited, which targeted the expanding market for telecommunications components including LCD modules as well as end products, including cordless phones and family radio systems. Nowadays, color and monochrome LCD modules displaying information have become one of our major products. Since December 2002, we have also produced RF modules for integration into cellular phones and other hand-held consumer electronic products, such as personal digital assistants, or PDAs, laptop computers and other products with wireless connectivity. In 2003, we further diversified our product mix by manufacturing CMOS sensor modules for integration into various image capturing devices such as digital cameras for cellular phones and home entertainment products, FPC sub-assemblies for integration into various LCD modules, front light panels for handheld video game devices and digital camera accessories for use with the cellular phones and home entertainment products. In 2004, we expanded our business on CMOS sensor modules and FPC sub-assemblies. We also further broadened our product line by manufacturing back light panels for handheld video game devices and Bluetooth™ wireless headset accessory for cellular phones.

In September 2000, we acquired for $2.0 million a 5% indirect shareholding in both TCL Mobile Communication (HK) Co., Ltd. and Huizhou TCL Mobile Communication Co., Ltd., together known as TCL Mobile, through the acquisition of 25% of the outstanding shares of Mate Fair Group Limited, or Mate Fair, a privately held investment holding company incorporated in the British Virgin Islands with a 20% shareholding interest in TCL Mobile. TCL Mobile is engaged in manufacturing, distributing and trading of digital mobile phones and accessories in China as well as in overseas markets.

In October 2000, we completed the acquisition of the J.I.C. Group (BVI) Limited. The J.I.C. Group (BVI) Limited and its subsidiaries, or the J.I.C. Group, are principally engaged in the manufacture and marketing of transformers and LCD panels, a key component for a variety of consumer electronic products. Of the purchase price of $32.8 million, we paid $11.0 million in cash and issued 3.48 million of our common shares.

In November 2002, Mate Fair sold a portion of its equity interest in Huizhou TCL Mobile Communication Co., Ltd. for which we received proceeds of approximately $10.4 million, reducing our direct equity interest (held through Mate Fair) in TCL Mobile to approximately 3%. In November 2002, we invested $5.1 million of the proceeds in TCL International Holdings Limited s 3% convertible notes that are due in November 2005. In August 2003, we disposed of those convertible notes to independent third parties and received proceeds of approximately $5.03 million in cash. TCL International Holdings Limited is another company in the TCL Group, which consists of the TCL Corporation and its subsidiaries, and is publicly listed on The Stock Exchange of Hong Kong Limited, or the Hong Kong Stock Exchange.

In January 2002, we acquired a 6% equity interest in TCL Corporation (formerly known as TCL Holdings Corporation Ltd.), for a consideration of approximately $12.0 million. TCL Corporation, an enterprise established in China, is the parent company of the TCL Group of companies. TCL Corporation changed from a limited liability company to a company limited by shares in April 2002. In January 2004, TCL Corporation listed its A-shares on the Shenzhen Stock Exchange at RMB 4.26 (equivalent to $0.52) per A-share. The Company s interest in TCL Corporation has since been diluted to 3.69% and represents 95.52 million promoter s shares of TCL Corporation after its initial public offering. Pursuant to Article 147 of the Company Law of China, the Company is restricted from transferring its promoter s shares within three years from the establishment date. The Company is, however, entitled to receive dividends and other rights similar to holders of A-shares. As these promoter s shares have a restriction on their sale prior to April 2005, the Company hired an independent valuer to determine the fair value of these shares as of December 31, 2004 and recognized an unrealized gain of $6.55 million, which has been recorded as a separate component of accumulated other comprehensive income, based on the Company s cost of $11.97 million and an estimated fair value of $20.70 million.

In January 2002, we entered into a transaction which resulted in the listing of a company holding J.I.C. Group s business on the Hong Kong Stock Exchange. To effect the transaction, we entered into an agreement with the liquidators of Albatronics, whose shares had been listed on the Hong Kong Stock Exchange and which was placed into voluntary liquidation in August 1999. Under the agreement, we agreed to transfer the J.I.C. Group into J.I.C. Technology Company Limited, a new company, for a controlling interest in J.I.C. Technology Company Limited. Albatronics listing status on the Hong Kong Stock Exchange was withdrawn and J.I.C. Technology Company Limited was listed on the Hong Kong Stock Exchange free from the liabilities of Albatronics. This arrangement was more cost effective than using an initial public offering. For our contribution to J.I.C. Technology Company Limited, we received a combination of ordinary and preference shares, which are analogous to common stock and convertible preferred stock, respectively, of companies organized under United States law and which upon their full conversion, could result in us, the creditors and the Hong Kong public owning approximately 92.9%, 5.8% and 1.3%, respectively, of the outstanding ordinary shares of J.I.C. Technology Company Limited. On June 4, 2002, the reverse merger was completed and all the shares of Albatronics were transferred to the liquidators for a nominal consideration. The preference shares are non-redeemable, non-voting shares that rank *pari passu* with ordinary shares of J.I.C. Technology Company Limited on the payment of dividends or other distribution other than on a winding-up. No holder of preference shares (including Nam Tai) may convert them if such conversion would result in the minimum public float of 25% (required under the Hong Kong Stock Exchange Listing Rules) not being met. In August 2002, we acquired an additional 7,984,000 ordinary shares of J.I.C. Technology Company Limited for a cash consideration of $437,000. During the period from June to November 2003, we disposed of a total of 42,600,000 ordinary shares for cash consideration of $4.0 million. In November 2003, we converted 175,100,000 preference shares into 170,000,000 ordinary shares of J.I.C. Technology Company Limited.

During the period from November to December 2004, we further disposed of a total of 128,000,000 ordinary shares of J.I.C. Technology Company Limited for cash consideration of $12.95 million. The disposal resulted in a net gain on partial disposal of a subsidiary of $6.25 million and the release of unamortized goodwill of $3.52 million. During the same period, we converted all 423,320,000 preference shares into 410,990,290 ordinary shares. As of December 31, 2004, we held 546,890,978 ordinary shares of J.I.C. Technology Company Limited, equivalent to 71.63% of issued ordinary shares.

In January 2003, we invested $10.0 million for a 25% equity interest in Alpha Star Investments Ltd., the ultimate holding company of JCT Wireless Technology Limited, or JCT. JCT is engaged in the design, development and marketing of wireless communication terminals and wireless application software and is using us to manufacture wireless communication terminals and their related modules. As of December 31, 2004, we recognized net sales of $34.2 million to JCT for the year. However, in September 2004, we made an impairment to write down our $10.0 million investment in Alpha Star to a fair value of approximately $3.0 million. As of December 31, 2004, another analysis had been conducted by an independent valuer, who determined that no further impairment to value was required.

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In January 2003, we disposed of 20% of our equity interest in Namtek Software Development Company Limited to a company that is owned by the management of Namtek Software Development Company Limited for a cash consideration of $160,000. As of the date of disposal, Namtek Software Development Company Limited was fair valued at $3.3 million.

On January 23, 2003, the listing of our shares was transferred to the NYSE from the NASDAQ National Market with symbol of NTE . On June 30, 2003, we implemented a three-for-one stock split with both the stock size and market price to be divided by three. As of December 31, 2004, there were 42,664,536 common shares outstanding.

In June 2003, one of our subsidiaries, J.I.C. Technology Company Limited, disposed of its transformers operation to a third party for a cash consideration of $2.4 million. The gain from disposal of this discontinued operation amounted to $2.0 million, net of $0.1 million shared by minority interest.

In August 2003, we set up our first subsidiary, Nam Tai Investments Consultant (Macao Commercial Offshore) Company Limited in Macao as our PRC headquarters. Macao, like Hong Kong, is a special administrative region of the China and has recently introduced an incentive program to attract investment to Macao. In March and November 2004, we further established Zastron (Macao Commercial Offshore) Company Limited and J.I.C. (Macao Commercial Offshore) Company Limited in Macao, respectively.

In November 2003, our common shares were listed in the Regulated Unofficial Market (Freiverkehr) on the Frankfurt Stock Exchange, in Germany. The stocks are being traded on Xetra, the Deutsche Borse AG electronic trading system under the stock symbol 884852 .

In December 2003, we placed approximately $5.3 million into an escrow account for an investment in Stepmind. The investment was to occur in two phases. For the first phase, approximately $2.64 million, representing 7.66% of the equity interest in Stepmind, was released to Stepmind in January 2004. The second phase amounting to approximately $2.65 million was released to Stepmind in August 2004 subject to fulfillment of certain conditions. In August 2004, we disposed of our entire interest in Stepmind to one of the shareholders of Stepmind at the original subscription price for those shares.

In April 2004, we increased our shareholding in TCL Mobile from approximately 3% to 9% through the acquisition of Jasper Ace Limited, or Jasper Ace, which directly holds a 9% equity interest in TCL Mobile, for a consideration of approximately $102.2 million. The consideration was satisfied by the exchange of our 72.2% equity interest in Mate Fair, plus cash of $25 million in cash, and the issuance of 1,416,764 new Nam Tai shares and resulted in a net investment cost of $79.5 million. In July 2004, Nam Tai transferred all its shares in TCL Mobile to TCL Communication Technology Holdings Limited, or TCL Communication, in exchange for 90 shares of TCL Communication. In August 2004, we further subscribed for 254,474,910 shares in TCL Communication at a consideration of approximately $16 million. The consideration was satisfied by the dividend receivable from TCL Communication. Together with the 90 shares it received in July 2004, Nam Tai in total holds 254,475,000 shares in TCL Communication, representing 9% of the shareholding of TCL Communication. In September 2004, shares of TCL Communication were listed on the Hong Kong Stock Exchange by way of introduction. There were no new shares issued or sold in connection with the listing, and therefore no dilution to Nam Tai s original stake in TCL Communication. As of December 31, 2004, we still hold 254,475,000 shares, representing 9% of the total issued shares of TCL Communication.

As of December 31, 2004, the Company s investment in TCL Communication was stated at fair value based on the traded market price of TCL Communication s shares. The Company recognized an unrealized loss of $58.3 million in its consolidated statements of income based on the Company s cost of $79.5 million and a fair value of $21.2 million.

In April 2004, shares of Nam Tai Electronic & Electrical Products Limited, or NTEEP, a wholly owned subsidiary of the Company, were listed on the Hong Kong Stock Exchange. Since all of the shares of NTEEP involved in the initial public offering, or IPO, were existing shares of NTEEP owned by Nam Tai, all of the proceeds raised in the IPO went to Nam Tai instead of NTEEP. The offer price of NTEEP s share was $0.497, which resulted in net proceeds of approximately $92.8 million and a gain of approximately $71.1 million to the Company. As of December 31, 2004, we held 600,000,000 shares of NTEEP, representing 75% of the total issued shares of NTEEP.

Also refer to the section of this Report entitled Item 5. Operating and Financial Review and Prospects for a further discussion of our investments and acquisitions.

An important element of our strategy is to acquire companies that would complement our existing products and services, augment our market coverage and sales ability or enhance our technological capabilities. Accordingly, we may acquire additional businesses, products or technologies in the future or make investments in related businesses for strategic business purposes.

Capital Expenditures

Our principal capital expenditures and divestitures over the last three years include the following:

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	2002	2003	2004
Property, plant and equipment (net)	$18,485,000	17,053,000	38,611,000

Our major capital expenditure in 2004 included:

- $13.8 million for new factory expansion;
- $7.7 million for the expansion of an LCD factory (which included 5.8 million paid as a deposit for fixed assets);
- $0.7 million for the expansion of our high-resolution color LCD module production capacity;
- $14.5 million for machineries used mainly for FPC sub-assemblies;
- $5.6 million for other capital equipment; and
- $2.1 million for construction work in relation to the electricity supply for Nam Tai Electronic (Shenzhen) Co., Ltd.

Our major capital expenditures in 2003 included:

- $6.0 million for machinery for manufacturing RF modules;
- $1.2 million for new factory expansion;
- $0.4 million for machinery on FPC sub-assemblies;
- $1.7 million for expansion of our high-resolution color LCD module production capacity;
- $6.7 million for other capital equipment; and
- $1.1 million for construction of a new trade union building for the use of our workers in China.

Our major capital expenditures in 2002 included:

- $12.3 million for a new STN LCD panel production line; and
- $4.0 million for completion of the new factory expansion.

In order to expand production capacity, we have built a new factory consisting of approximately 265,000 square feet adjacent to our principal manufacturing facilities in Shenzhen, China. The construction was completed in December 2004 and we expect full operations to commence in April 2005. As of December 31, 2004, we had spent $15.0 million to cover the cost of construction, fixtures and equipment for the new factory. The financing for these improvements to our manufacturing facilities were obtained from internal resources. In October 2004, our existing production facility for the LCD panels segment also relocated to new factory premises which are approximately 670,000 square feet and twice the size of the former factory premises. This new factory provides room for the future expansion of production capacity. As of December 31, 2004, we had spent $7.7 million for this relocation and financed this amount with a combination of internal resources and bank financing.

Other capital expenditures we have planned for 2005 include:

- $ 8.0 million for land purchase;

$16.5 million for new factory expansion;

$14.0 million for machinery; and

$4.5 million for other equipment.

Our plans for capital expenditures are subject to change from time to time and could result from, among other things, our consummation of any significant amount of additional acquisition or strategic investment opportunities, which we regularly explore.

Business Overview

We are an electronics manufacturing and design services provider to a select group of the world s leading OEMs of telecommunications and consumer electronic products. Through our electronics manufacturing services operations, we manufacture electronic components and sub-assemblies, including LCD panels, LCD modules, RF modules, FPC sub-assemblies and image sensors modules. These components are used in numerous electronic products, including cellular phones, laptop computers, digital cameras, copiers, fax machines, electronic toys, handheld video game devices and microwave ovens. We also manufacture finished products, including cellular phones, palm-sized PCs, personal digital assistants, electronic dictionaries, calculators, digital camera accessories and Bluetooth™ wireless headset accessory for use with cellular phones.

We assist our OEM customers in the design and development of their products and furnish full turnkey manufacturing services that utilize advanced manufacturing processes and production technologies. Our services include hardware and software design, component purchasing, assembly into finished products or electronic sub-assemblies and post-assembly testing. These services are value-added and assist us in obtaining new business but do not represent a material component of our revenue. We also provide original design manufacturing, or ODM, services, in which we design and develop proprietary products that are sold by our OEM customers using their brand name.

We were founded in 1975 as an electronic products trading company based in Hong Kong and shifted our focus to manufacturing of electronic products in 1978. We moved our manufacturing facilities to China in 1980 to take advantage of lower overhead costs, lower material costs and competitive labor rates, subsequently relocating to Shenzhen, China in order to capitalize on opportunities offered in southern China. We were reincorporated as a limited liability International Business Company under the laws of the British Virgin Islands in August 1987. Our principal manufacturing and design operations are based in Shenzhen, China, approximately 30 miles from Hong Kong. Some of our subsidiaries offices are located in Hong Kong and Macao, which provides us access to Hong Kong s and Macao s infrastructure of communication and banking and facilitates management of our China operations. One of our subsidiaries also has an office in Japan.

Our Customers

Historically, we have had substantial recurring sales from existing customers. About 89.4% of our 2004 net sales came from customers that also used our services in 2003. While we seek to diversify our customer base, a small number of customers currently generate a significant portion of our sales. Sales to our 10 largest customers accounted for 84.8%, 84.9% and 82.5% of our net sales during the years ended December 31, 2002, 2003 and 2004, respectively. Sales to customers accounting for 10% or more of our net sales in the year ended December 31, 2002, 2003 or 2004 were as follows:

		Year ended December 31,	
	2002	**2003**	**2004**
Epson Precision (HK) Ltd.	32.2%	24.8%	14.1%
Sony Ericsson Mobile Communications AB	16.9%	11.3%	*
Texas Instruments Incorporated	11.1%	*	*
Toshiba Matsushita Display Technology Co. Ltd	*	10.6%	*
Motorola Inc.	*	*	10.2%
Sharp Corporation	*	*	13.5%
Wuxi Sharp Electronic Components Co., Ltd.	*	*	10.1%

* Less than 10% of our total net sales.

Our largest OEM customers based on net sales during 2004 include the following (listed alphabetically):

Customer	**Products**
Advance Watch Co. (Far East) Ltd.	LCD panels for watches
Appeal Telecom Co., Ltd.	CMOS sensor modules
Canon Electronic Business Machines (H.K.) Co. Ltd.	Electronic dictionaries, calculators, PDAs and dictionaries, LCD panel sub-assemblies for copy machines and software development
Epson Precision (H.K.) Ltd.	LCD modules for cellular phones and FPC sub-assemblies

Goyo Paper Working Co., Ltd.	Game front light panel and back light panel assembly
JCT Wireless Technology Ltd.	RF modules and cellular phones in semi-knocked down, or SKD, form
Kanda Tsushin Kogyo Co Ltd. (affiliate of Fujitsu)	Assemblies for cordless phones
Motorola Inc.	CMOS sensor modules
Nanox Ltd.	LCD panels for cordless phones and household appliances
National Electronic & Watch Company Ltd.	LCD panels
Optrex Corporation	Assemblies for LCD modules
Polar Group	LCD panels
Seiko Instruments Inc.	Electronic dictionaries and PDAs, software development
Sharp Corporation	FPC sub-assemblies, calculators, PDAs and dictionaries
Sony Computer Entertainment Europe Ltd.	Home entertainment products
Sony Corporation	Electronic dictionaries and software development
Sony Ericsson Mobile Communications AB	Mobile phone digital camera accessories, Bluetooth™ wireless headset accessory
Stanley Electric (Asia Pacific) Ltd.	LCD panels for car audio devices
Texas Instruments Incorporated	Calculators
Toshiba Matsushita Display Technology Co. Ltd.	LCD modules for cellular phones
Uniden HK Ltd.	LCD panels
Wuxi Sharp Electronic Components Co. Ltd.	Telecom printed circuit board, or PCB, modules and FPC sub-assemblies

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At any given time, different customers account for a significant portion of our business. Percentages of net sales to customers vary from quarter to quarter and year to year and fluctuate depending on the timing of production cycles for particular products.

Sales to our OEM customers are primarily based on purchase orders we receive from time to time rather than firm, long-term purchase commitments from our customers. Although it is our general practice to purchase raw materials only upon receiving a purchase order, for certain customers we will occasionally purchase raw materials based on such customers rolling forecasts. Uncertain economic conditions and our general lack of long-term purchase commitments with our customers make it difficult for us to accurately predict revenue over the longer term. Even in those cases where customers are contractually obligated to purchase products from us or repurchase unused inventory from us, we may elect not to immediately enforce our contractual rights because of the long-term nature of our customer relationships and for other business reasons, and instead may negotiate accommodations with customers regarding particular situations.

Our Products

During 2003, our operations are generally organized in two segments, Consumer Electronics Products, or CEP, and LCD panels and transformers, or LPT. The activities of our LPT segment relate primarily to our J.I.C. subsidiary that we acquired in October 2000. In 2004, our operations were re-organized into three reportable segments consisting of consumer electronics and communication products, or CECP, telecommunication components assembly, or TCA and LCD panels, or LCDP. In 2003, CECP and TCA were classified as a single reportable segment as CEP while LCDP also comprised the transformers operations and collectively referred to as LPT as a result of the disposal of transformer business in 2003.

The dollar amount (in thousands) and percentage of our net sales by business segment and product category for the years ended December 31, 2002, 2003 and 2004 were as follows:

	Year ended December 31,					
	2002		2003		2004	
	Dollars	Percent	Dollars	Percent	Dollars	Percent
Consumer Electronics and Communication Products	$ 94,032	40%	$ 128,778	32%	$ 163,584	31%
Telecom, Components Assembly:						
Telecom, components assembly(1)	103,800	44	232,163	57	316,695	59
Software development services	2,923	1	4,041	1	4,872	1
LCD Panels and Transformers						
LCD panels	23,937	10	35,040	9	48,710	9
Transformers(2)	11,324	5	6,284	1		
Total	$ 236,016	100%	$ 406,306	100%	$ 533,861	100%

(1) Included in telecom, components assembly are our sales from our manufacture of rechargeable battery packs through a joint venture we had with Toshiba Battery Co., Ltd. We sold our interest in the joint venture to a Toshiba-related company and ceased manufacturing rechargeable battery packs as of April 30, 2002. Accordingly, revenue from sales of battery packs was not included after that date.

(2) We sold our transformers operation to a third party in June 2003.

Please refer to Note 19 Segment Information of the Consolidated Financial Statements and Item 8 Financial Information Export Sales which sets forth the information of net sales to customers by geographic area.

Consumer Electronic and Communication Products, or CECP

The consumer electronic and communication products we manufacture are primarily finished products and include:

A Bluetooth™ wireless headset accessory for cellular phones, which we began manufacturing in March 2004.

CMOS sensor modules, which we began manufacturing in June 2003, for integration into various image-capturing devices such as digital cameras for cellular phones and home entertainment products.

Digital camera accessories for use with cellular phones and home entertainment products.

Electronic calculators that include basic function calculators, desktop display style, scientific and advanced graphic calculators.

Digital management devices that include PDAs and electronic personal organizers.

Linguistic products, including electronic dictionaries, spell checkers and language translators.

Telecommunication Component Assembly, or TCA

Telecommunications Components Assembly

We manufacture the following sub-assemblies and components:

Color and monochrome LCD modules to display information as part of telecommunication products such as cellular phones and telephone systems, appliances and office automation products, such as copiers and facsimile machines. Our LCD modules could be manufactured for use in most other hand-held consumer electronic devices, such as electronic games and digital cameras.

RF modules, which we began manufacturing in December 2002, for integration into cellular phones. These modules could be manufactured for use in most other hand-held consumer electronic products, such as PDAs, laptop computers and other products with wireless connectivity.

Cellular phones in SKD form.

FPC sub-assemblies which we began manufacturing in March 2003 for integration into various LCD modules.

Front light panels for handheld video game devices.

Back light panels for handheld video game devices, which we began manufacturing in August 2004.

1.9 and 2.4 GHz high frequency cordless telephones, home feature phones, family radio systems and transceivers.

Software Development Services

We offer software development services principally for the electronic dictionary products for major Japanese customers. In addition, we focus on research and development for car navigation products which we aim to results in providing license and/or manufacturing services to the OEM customers.

LCD Panels, or LCDP

With the acquisition of the J.I.C. Group in October 2000, we began producing LCD panels.

LCD panels are found in numerous applications in electronics products, such as watches, clocks, calculators, pocket games, PDAs and mobile and cordless telephones. We are a customized LCD panel manufacturer, and we develop each product from design concept all the way to a high quality mass producible product.

Our Manufacturing and Assembly Capabilities

We utilize the following production techniques:

Chip on Film, or COF, is an assembly method for bonding integrated circuit chips and other components onto a flexible printed circuit. This process allows for greater compression of the size of a product when assembled enabling the production and miniaturization of small form factor devices like cellular phones, PDAs, digital cameras and notebook PCs. As of December 31, 2004, we had 14 COF machines. These machines connect the bump of large scale integrated, or LSI, driver onto FPC pattern with anisotropic conductive film, or ACF, and mount chip resister cap components to FPC through surface mount technology, or SMT, is available. These COF machines have the ability to pitch fine to 38 micrometers and a total production capacity of up to 4,000,000 chips per month.

Chip On Glass, or COG, is a process that connects integrated circuits directly to LCD panels without the need for wire bonding. We apply this technology to produce advanced LCD modules for high-end electronic products, such as cellular phones and PDAs. As of December 31, 2004, we had 21 COG lines in our principal manufacturing facilities. These machines provide an LCD of dimension of up to 200 millimeters (length) x 150 (width) x 2.2 (height), a process time per chip of five seconds, a pin pitch fine to 38 micrometers and a total production capacity of up to 4,000,000 chips per month. During 2004, our subsidiary, Jetup Electronic (Shenzhen) Co. Ltd., or Jetup, also started manufacturing COG LCD modules. As of December 31, 2004, Jetup had five COG lines and is capable of bonding 1,000,000 pieces of COG LCD modules a month. They are able to bond LCD panels up to sizes of 100 millimeters x 100 millimeters x 2.2 millimeters thick, with an accuracy of five microns tolerence, in a cycle time of 12-15 seconds per piece.

Chip On Board, or COB, is a technology that utilizes wire bonding to connect large-scale integrated circuits directly to printed circuit boards. We use COB in the assembly of consumer products such as calculators, personal organizers and linguistic products. As of December 31, 2004, we had 52 COB machines. These machines are fully automatic bonding machines and use ultrasonic mounting technology. The bonding time, pressure, power and each wire loop are under machine programmable control. These machines provide a high speed chip mounting time of per 2 millimeters wire per 0.25 second, a bond pad fine to 75 micrometers and a total production capacity of up to 3,000,000 chips per month.

Outer Lead Bonding, or OLB, is an advanced technology used to connect PCBs and large-scale integrated circuits with a large number of connectors. We use this technology to manufacture complex miniaturized products, such as high-memory PDAs. As of December 31, 2004, we had three OLB machines. The machines include multi-pinned tape carrier packaged large scale integrated circuit, or TCP LSIC, bonding which is up to 280 pins, which also provide ultra thin assembly with module thickness to around one millimeter and high accuracy bonding with pin pitch to 100 micrometers. The total production capacity is 12,000 units per month.

Tape Automated Bonding with Anisotropic Conductive Film, or TAB with ACF, is an advanced heat sealing technology that connects a liquid crystal display component with an integrated circuit in very small LCD modules, such as those used in cellular phones and pagers. As of December 31, 2004, we had 35 systems of TAB with ACF machines. The machines provide process time of 24 to 25 seconds per component, a pin pitch fine to 200 micrometers and a total production capacity of up to 3,660,000 components per month. During 2004, Jetup also started manufacturing TAB LCD modules. As of December 31, 2004, Jetup had two TAB lines and is capable of bonding 250,000 pieces of TAB LCD modules a month. They are able to bond LCD panels up to sizes of 120 millimeters x 120 millimeters x 2.2 millimeters thick, with an accuracy of 10 microns tolerence in a cycle time of 20-25 seconds per piece.

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Fine Pitch Heat Seal Technology, or FPHS technology, allows us to connect LCD displays to PCBs produced by COB and outer lead bonding that enables very thin connections. This method is highly specialized and is used in the production of finished products such as PDAs. As of December 31, 2004, we had eight machines utilizing FPHS technology. The machines provide a pin pitch fine to 260 micrometers and a total production capacity of up to 268,000 units per month.

Surface Mount Technology, or SMT, is a process by which electronic components are mounted directly on both sides of a printed circuit board, increasing board capacity, facilitating product miniaturization and enabling advanced automation of production. We use SMT for products such as electronic linguistic devices. As of December 31, 2004, we had 29 SMT productions lines. The production time per chip ranges from 0.072 second per chip to 0.8 second per chip and high precision ranging from +/-0.05 millimeter to +/-0.1 millimeter. The components size ranges from 0.6 millimeter (length) x 0.3 millimeter (width) to 55 millimeters (length) x 55 millimeters (width). Ball grid array, or BGA, ball pitch is 0.5 millimeter and ball diameter is 0.2 millimeter. The total production capacity is 670,000,000 resistor capacitor chips per month.

Twisted Nematic LCDs, or TN type LCD, is the most conventional and economical and is suitable for low information content display systems such as those found in calculators, watches, car audio, car clusters and other medical instruments. As of December 31, 2004, J.I.C. had two TN LCD lines capable of total capacity of about 100,000 pairs of glass panels (each sheet of glass of 360 millimeters x 400 millimeters size) per month.

Super-Twisted Nematic LCDs, or STN, type LCDs capable of providing higher information content display systems are found in applications such as cordless phones, mobile phones, MP3 players, pocket games and PDAs. J.I.C. started producing STN LCDs in 2002 and, as of December 31 2004, was equiped with a automated line capable of capacity 50,000 pairs of glass (each sheet of glass of 360 millimeters x 400 millimeters size) panels per month.

As of December 31, 2004, we had four clean rooms at our principal manufacturing facilities, which housed COF and COG capabilities for LCD module and front light or back light panel manufacturing. We also have five clean rooms at another of our factories, which are used to manufacture LCD panels. Of our nine clean rooms as of December 31, 2004, six were class ten thousand, three were class thousand.

Quality Control

We maintain strict quality control programs for our products, including the use of total quality management, systems and advanced testing and calibration equipment. Our quality control personnel test the quality of incoming raw materials and components. During the production stage, our quality control personnel also test the quality of work-in-progress at several points in the production process. Finally, after the assembly stage, we conduct testing of finished products. In addition, we provide office space at our principal manufacturing facilities for representatives of our major customers to permit them to monitor production of their products and we provide them with direct access to our manufacturing personnel.

All of our manufacturing facilities are certified under ISO 9001 quality standards, the International Organization for Standardization s, or ISO s highest standards. The ISO is a Geneva-based organization dedicated to the development of worldwide standards for quality management guidelines and quality assurance. ISO 9000, which was the first quality system standard to gain worldwide recognition, requires a company to gather, analyze, document, monitor and make improvements where needed. Our certification under an ISO 9001 quality standard demonstrates that our manufacturing operations meet the most demanding of the established world standards. Our principal manufacturing facilities are also certified under an ISO 14001 quality standard, which was published in 1996 to provide a structured basis for environmental management control.

We started the implementation of the Six Sigma approach in 2004 and our principal manufacturing facilities have been recognized by the China Association for Quality of the Chinese Government as a National Advanced Enterprise for the Promotion of Six Sigma . Six Sigma is an internationally recognized approach that uses facts and data to develop better solutions, thereby reducing defects and production times, and improving customer satisfaction. This approach allows the Company to lower its costs due to the minimization of manufacturing defects. This results in improved profit margins and higher competitiveness.

Our Suppliers

We purchase thousands of different component parts from numerous suppliers. We are not dependent upon any single supplier for any key component. We purchase components from suppliers in Japan, China and elsewhere. We generally base component orders on received purchase orders in an effort to minimize our inventory risk by ordering components and products only to the extent necessary although for certain customers we will occasionally purchase raw materials based on such customer s rolling forecasts.

The major component parts we purchase include the following:

- off-the-shelf and custom integrated circuits or chips , most of which we purchase presently from Toshiba Corporation, Sharp Corporation and certain of their affiliates;

- LCD panels, which are available from many manufacturers. In 2004, we purchased LCD panels from Epson Hong Kong Ltd., Toshiba Matsushita Display Technology Co. Ltd., Optrex Corporation and Sharp Corporation for LCD panels and in the future we may produce some LCD supplies internally;

- CMOS sensors, which we purchase mainly from Omnivision Technologies Inc.;

- solar cells and batteries, which are standard off-the-shelf items that we generally purchase in Hong Kong from agents of Japanese manufacturers; and

- various mechanical components such as plastic parts, rubber keypads, PCBs, indium tin oxide, or ITO, glass used in the production of LCD panels, and packaging materials from various local suppliers in China.

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Whenever practical, we use domestic China suppliers who are often able to provide items at low costs and with short lead times.

Certain components may be subject to limited allocation by certain of our suppliers. During 2000, there was an industry-wide shortage of components in the electronics industry as supply was unable to satisfy growing world demand. In some cases, supply shortages and delays in deliveries of particular components have resulted in curtailed production, or delays in production of assemblies using scarce components. These supply shortages have contributed to an increase in our inventory levels and reduction in our margins. We expect that shortages and delays in deliveries of some components will continue. If we are unable to obtain sufficient components on a timely basis, we may experience manufacturing delays, which could harm our relationships with current or prospective customers and reduce our sales.

The principal raw materials used by the Company are large scale integrated, or LSI, circuits (CMOS), semiconductors, LCD panels and batteries. At times, the pricing and availability of these raw materials can be volatile, due to numerous factors beyond the Company s control, including general economic conditions, currency exchange rates, industry cycles, production levels or a supplier s tight supply. In the past, we have asked our customers to share in the increased costs of raw materials where such increased costs would adversely affect the Company s business, results of operations and financial condition. Our customers have generally agreed when so requested in the past. We cannot assure you, however, that our customers will agree to share costs in the future and that our business, results of operations and financial condition would not be adversely affected by increased volatility of raw materials.

Production Scheduling

The typical cycle for a product to be designed, manufactured and sold to an OEM customer is one to two years, which includes the production period, the development period and the period for market research and data collection (which is undertaken primarily by our OEM customers). Initially an OEM customer gathers data from its sales personnel on products for which there is market interest, including features and unit costs. The OEM customer then contacts us, and possibly other prospective manufacturers, with forecasted total production quantities and design specifications or renderings. From that information, we in turn contact our suppliers and determine estimated component and material costs. We later advise our OEM customer of the development costs, charges (including molds, tooling and software design, if applicable) and unit cost based on the forecasted production quantities desired during the expected production cycle.

Once we and the OEM customer agree to the quotation for the development costs and the unit cost, we begin the product development if we are engaged to do so. This development period typically lasts less than six months, but may be longer if software design is included. During this time we complete all molds, tooling and software required to manufacture the product with the development costs generally borne by our customer. Upon completion of the molds, tooling and software, we produce samples of the product for the customer s quality testing, and, once approved, commence mass production of the product. We recover the development costs in relation to molds, tooling and software from our customers.

The production period usually lasts approximately six to twelve months. In some cases, our OEM customer handles all product design and development and engages us only at the point of initial production. Typically, more advanced products have shorter production runs. If total production quantities change, the OEM customer often provides only limited notice before discontinuing orders for a product. At any point in time we may be in different stages of the development and production periods for the various models under development or in production for our OEM customers.

Generally, our production is based on purchase orders received from OEM customers. Purchase orders are often supported by letters of credit or written confirmation from the OEM customer and generally may not be cancelled once confirmed without the mutual consent of the parties. Even in those cases where customers are contractually obligated to purchase products from us or repurchase unused inventory from us, we may elect not to immediately enforce our contractual rights because of the long-term nature of our customer relationships and for other business reasons, and instead may negotiate accommodations with customers regarding particular situations.

We did not suffer a material loss resulting from the cancellation of OEM customer orders in 2001 to 2004. In 2001, we wrote down our inventory for $3.8 million for slow-moving raw materials relating to cancelled, reduced or delayed orders. However, subsequently we were able to use some of these raw materials in production or we received compensation for the unused raw materials from certain of our customers, and the gain of $2.0 million was recorded in cost of sales during 2002.

Sales and Marketing

We focus on developing close relationships with our customers at the development and design phases and continuing throughout all stages of production. We identify, develop and market new technologies that benefit our customers and position us well as an EMS provider.

Sales and marketing operations are integrated processes involving direct salespersons, project managers and senior executives. We direct our sales resources and activities at several management and staff levels within our customers and prospective customers. We receive unsolicited inquiries resulting from word of mouth, from public relations activities, and through referrals from current customers. We evaluate these opportunities against our customer selection criteria and assign direct salespersons.

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Seasonality

Historically, our sales and operating results are often affected by seasonality. Sales of calculators, personal organizers and linguistic products are often higher during the second and third quarters in anticipation of the start of the school year and the Christmas buying season. Similarly, our consumer services for electronics products have historically been lower in the first quarter resulting from both the closing of our factories in China for the Chinese New Year holidays and the general reduction in sales following the holiday season. As we have diversified our services for complex components, we expect that seasonality may be less of a factor affecting our business.

Transportation

Transportation of components and finished products to and from Shenzhen is by truck. Component parts purchased from Japan are generally shipped by air. To date, we have not been materially affected by any transportation problems. However, transportation difficulties affecting air cargo or shipping, such as an extended closure of ports that materially disrupts the flow of our customers products into the United States, could materially and adversely affect our sales and margins if, as a result, our customers delay or cancel orders or seek concessions to offset expediting charges they incurred pending resolution of the problems causing the port closures.

Competition

General competition in the contract EMS industry is intense and characterized by price erosion, rapid technological change and competition from major international companies. This intense competition has resulted in pricing pressures, lower sales and reduced margins. We believe that the principal competitive factors in our targeted markets are product quality, pricing, flexibility and timeliness in responding to design and schedule changes, reliability in meeting product delivery schedules, technological sophistication and geographic location. Many of our competitors have greater financial, technical, marketing, manufacturing, regional shipping capabilities and logistics support and personnel resources than we do and we may not be able to continue to compete successfully.

The EMS services we provide are available from many independent sources as well as from current and potential customers with in-house manufacturing capabilities. Our EMS competitors include Celestica, Inc., Flextronics International Ltd., Hon Hai Precision Industry Co., Ltd., Jabil Circuit, Inc., Sanmina-SCI Corporation and Solectron Corporation. Our principal competitors in the manufacture of our traditional product lines of calculators, personal organizers and linguistic products include Kinpo Electronics, Inc. and Inventec Co. Ltd. Our competitors in the manufacturing of image capturing devices and their modules include Lite-On Technology Corporation, The Primax Group and Logitech International S.A. Our principal competitors in the manufacture of mobile phone accessories include Elcoteq Network Corp. Our competitors in the manufacturing of RF modules include Wavecom and WKK International (Holdings) Ltd. Our competitors in the manufacturing of LCD panels include Truly International Holdings Ltd. and Varitronix International Ltd. We have numerous competitors in the telecommunication, sub-assemblies and components product lines, including Philips, Samsung and Varitronix International Ltd. Our competitors in our FPC sub-assemblies business include Solectron Corporation.

Research and Development

We invest in research and development for manufacturing and assembly technology that provide us with the potential to offer better and more technologically advanced services to our OEM customers or assist us in working with our OEM customers in the design and development of future products. We plan to continue acquiring advanced design equipment and to enhance our technological expertise through continued training of our engineers and further hiring of qualified system engineers. These investments are intended to improve the speed, efficiency and quality of our assembly processes.

In our ODM business, we are responsible for the design and development of new products, the rights to which we own. We sell these products to OEM customers to be marketed to end users under the customers brand names. To date, we have successfully developed a number of electronic dictionaries, cordless telephones and calculator products. Our efforts to expand or maintain the ODM business may not be successful and we may not achieve material revenues or profits from our efforts. To date, our ODM design activities have not been a material portion of our research and development budget.

Patents, Licenses and Trademarks

We do not have any patents, licenses or trademarks on which our business is substantially dependent. Instead, we rely on our trade secrets, industry expertise and long-term relationships with our customers and suppliers.

Organizational Structure

We are a holding company for Nam Tai Group Management Limited, Nam Tai Electronic & Electrical Products Limited, Zastron Precision-Tech Limited, Namtek Software Development Company Limited and J.I.C. Technology Company Limited and their subsidiaries. The chart below illustrates the organizational structure of the Company and our principal operating subsidiaries as of December 31, 2004.

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Our significant operating entities are described below:

Nam Tai Group Management Limited

Nam Tai Group Management Limited was established on March 9, 2001 in Hong Kong and provides management services to other group companies.

Nam Tai Electronic & Electrical Products Limited

Nam Tai Electronic & Electrical Products Limited, or NTEEP, was incorporated in June 2003 in the Cayman Islands, and is the holding company for Namtai Electronic (Shenzhen) Co., Ltd. and Nam Tai Investments Consultant (Macao Commercial Offshore) Company Limited. Its shares were listed on the Hong Kong Stock Exchange on 28 April 2004 and we hold 75% of the issued ordinary shares of NTEEP.

Namtai Electronic (Shenzhen) Co., Ltd.

Namtai Electronic (Shenzhen) Co., Ltd. was established as Baoan (Nam Tai) Electronic Co. Ltd. in June 1989 as a contractual joint venture company with limited liability pursuant to the relevant laws of China. The equity of Baoan (Nam Tai) Electronic Co. Ltd. was 70% owned by Nam Tai Electronic & Electrical Products Limited and 30% owned by a Chinese company. In 1992, the Chinese company transferred all of its equity interest in the contractual joint venture to Nam Tai Electronic & Electrical Products Limited, a Hong Kong subsidiary of Nam Tai, which name was subsequently changed to Nam Tai Trading Company Limited, and the company changed its name to Namtai Electronic (Shenzhen) Co., Ltd. It is the principal operating arm of NTEEP.

Nam Tai Investments Consultant (Macao Commercial Offshore) Company Limited

Nam Tai Investments Consultant (Macao Commercial Offshore) Company Limited was established in August 2003 in Macao, China. In March 2004, the equity interest of Nam Tai Investments Consultant (Macao Commercial Offshore) Company Limited was transferred from the Company to NTEEP and became its wholly owned subsidiary. Its principal business is the provision of management and sales co-ordination and marketing services to other companies within the NTEEP group.

Zastron Precision-Tech Limited

Zastron Precision-Tech Limited, or Zastron, was incorporated in June 2003 in the Cayman Islands, and is the holding company for Zastron Electronic (Shenzhen) Co., Ltd. and Zastron (Macao Commercial Offshore) Company Limited.

Zastron Electronic (Shenzhen) Co. Ltd.

Zastron Electronic (Shenzhen) Co. Ltd. was organized as Zastron Plastic & Metal Products (Shenzhen) Ltd. in March 1992 as a limited liability company pursuant to the relevant laws of China. Zastron Plastic & Metal Products (Shenzhen) Ltd. was engaged in the production of metallic parts and PVC plastic products, much of which is used in the products manufactured in our principal manufacturing facilities. In August 2002, Zastron Plastic & Metal Products (Shenzhen) Ltd. changed its name to Zastron Electronic (Shenzhen) Co. Ltd. and expanded the nature of its business to include manufacturing of telecommunication products, LCD modules, TFT LCD modules and others. It also became one of our principal manufacturing arms. Zastron Electronic (Shenzhen) Co. Ltd. is currently a wholly-owned subsidiary of Zastron.

Zastron (Macao Commercial Offshore) Company Limited

Zastron (Macao Commercial Offshore) Company Limited was established in March 2004 in Macao, China and is a wholly owned subsidiary of Zastron. Its principal business is the provision of management, sales co-ordination and marketing services to other companies within the Zastron group.

J.I.C. Technology Company Limited

J.I.C. Technology Company Limited, or J.I.C., was formed in the Cayman Islands in January 2002 in connection with a reverse merger with Albatronics, of which we owned slightly more than 50% of the outstanding capital stock. J.I.C. was listed on the Hong Kong Stock Exchange in June 2002. We currently hold 71.63% of the issued ordinary shares of J.I.C.

Jetup Electronic (Shenzhen) Co., Ltd.

Jetup Electronic was incorporated in 1993 in China and handles the manufacturing and processing works of LCD panels through its factory plants in Baoan County, Shenzhen.

J.I.C. (Macao Commercial Offshore) Company Limited

J.I.C. (Macao Commercial Offshore) Company Limited was incorporated in November 2004 in Macao, China and is a wholly-owned subsidiary of J.I.C. Technology Company Limited. Its principal business is the provision of management, sales co-ordination and marketing services to other companies with the J.I.C. Group.

Namtek Software Development Company Limited

Namtek Software Development Company Limited was incorporated in May 2002 in the Cayman Islands and was established as the holding company for Shenzhen Namtek Co., Ltd. and Namtek Japan Company Limited.

Shenzhen Namtek Co., Ltd.

Shenzhen Namtek Co., Ltd. was organized in December 1995 as a limited liability company pursuant to the relevant laws of China. Shenzhen Namtek Co., Ltd. commenced operations in early 1996 developing and commercializing software for the consumer electronics industry, particularly for our customers and for products we manufacture or we will manufacture in the future. At December 31, 2004, Shenzhen Namtek Co., Ltd employed approximately 93 software engineers and provides the facilities and expertise to assist in new product development and research, enabling us to offer our customers program design for microprocessors, enhanced software design and development services, and strengthening our ODM capabilities.

Namtek Japan Company Limited

Namtek Japan Company Limited was incorporated in June 2003 in Tokyo, Japan and is the sales and marketing arm of software business of Namtek Group in Japan.

Property, Plant and Equipment

Our registered office in the British Virgin Islands is located at McNamara Chambers, P.O. Box 3342, Road Town, Tortola. Our principal executive office in the British Virgin Islands is located at 116 Main Street, 3rd Floor, Road Town, Tortola. Corporate administrative matters are conducted at this office through our registered agent, McNamara Corporate Services Limited. We do not own any property in the British Virgin Islands. The table below lists the locations, square footage, principal use and lease expiration dates of the facilities used in our principal operations.

Location	Square Footage	Principal Use	Owned or lease expiration date(1)
Hong Kong	24,200	Offices	Owned(2)
Macao	1,875	Offices	2005
Macao (for J.I.C. Macao)	964	Offices	2006
British Virgin Islands	300	Offices	2005
Principal Manufacturing Facilities	557,835	Manufacturing	2043/2049 (3)
Shenzhen, China	87,462	Offices	2043/2049 (3)
	189,952	Dormitories	2043/2049 (3)
	26,939	Cafeteria	2043
	33,826	Recreational	2049
Other facilities			
	383,547	Manufacturing LCD panels	2012
Other facilities Shenzhen, China			
	32,005	Offices	2012
	221,666	Dormitories	2012
	22,259	Cafeteria	2012
	14,548	Recreational	2012
Shekou, Shenzhen, China	12,374	Software development	2005
Tokyo, Japan	904	Software development	2005

(1) Only the Chinese government and peasant collectives may own land in China. Our principal manufacturing facilities are located on land in which we have entered into a land lease agreement with the Chinese government that gives us the right to use the land for 50 years. Based on our understanding of the practice as it exists today, at the expiration of the land lease we may be given the right to renew the lease. However, at the end of the lease term, all improvements we have made will revert to the government. For our other facilities, we have entered into factory building lease agreements with peasant collectives or other companies for 10 years or less.

(2) Although we own the office space, the land on which the building is located is subject to a 75-year lease with the government that expires in 2055, with a right to renew for 75 more years.

(3) Our principal manufacturing facilites occupy two pieces of land with 50-year leases which we acquired in 1993 and 1999, respectively.

In order to expand our production capacity, we have built a new factory consisting of approximately 265,000 square feet adjacent to our principal manufacturing facilities in Shenzhen, China. The construction completed in December 2004. We expect full operations can commence in April 2005. As of December 31, 2004, we had spent $15.0 million to cover the cost of construction and fixtures and equipment for the new factory. The financing of these improvements to our manufacturing facilities were obtained from internal resources.

In October 2004, our existing production facility for the LCD panels segment also relocated to new factory premises which are approximately 670,000 square feet and twice the size of the former factory premises. This new factory provides room for future expansion of production capacity. As of December 31, 2004, we had spent $7.7 million for this relocation and financed this amount with a combination of internal resources and bank financing.

Hong Kong

In 2001, our Hong Kong offices relocated to 15/F, China Merchants Tower, Shun Tak Centre, 168-200 Connaught Road, Central, Hong Kong. The office is conveniently located above the ferry terminal and beside the highway, permitting easy transportation by sea or by land to and from the manufacturing facilities in Shenzhen. The purchase and renovation of the 24,200 square feet of contiguous prime office space, including transaction fees, cost $13.0 million.

As of December 31, 2004, we own one residential flat in Hong Kong purchased for total consideration of $1,108,000. This property is occupied by one member of senior management and forms a part of his compensation.

Until 1996, we owned approximately ten acres of land in Hong Kong carried on our books at a cost of approximately $523,000. Between 1997 and 2004, we sold approximately 7.7 acres of land for net proceeds of $7.28 million; realizing a gain of $7.03 million. We plan to sell the remaining land and, pending the sale, to continue to carry the land at a cost of approximately $134,000.

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Macao

In August 2003, we established our PRC headquarters in Macao, China and set up Nam Tai Investments Consultant (Macao Commercial Offshore) Company Limited in Macao, China. Macao, like Hong Kong, is a special administrative region of China and has recently introduced an incentive program to attract investments to Macao. In March and November 2004, we further established Zastron (Macao Commercial Offshore) Company Limited and J.I.C.(Macao Commercial Offshore) Company Limited in Macao, China, respectively. We currently lease three offices and all of them under two-year leases expiring in July 2005 and December 2006, respectively. The monthly rental cost is approximately $905 per office.

Shenzhen, China

Principal Manufacturing Facilities

Our principal manufacturing facilities are located in Baoan County, Shenzhen, China. In December 1993, we acquired a 50-year lease for the first piece of land for approximately $2.45 million. The first phase facility consisted of 160,000 square feet of manufacturing space, 39,000 square feet of offices, 212,000 square feet of new dormitories, 26,000 square feet of full service cafeteria, recreation facilities and a swimming pool. The total cost of this addition to our complex, excluding land, was approximately $21.8 million. In November 2000, we began construction of another addition to our factory complex. We completed construction in October 2002, adding a new five-story factory with 138,000 square feet of production facilities, including one floor for assembling, one floor of office space, one floor for warehouse use and two floors of class thousand clean room facilities. Prior to this addition, we had only one floor of class ten thousand clean room facilities at our factory complex. As of December 31, 2002, we had spent $9.1 million to complete the construction of the new facility. With this new addition, we had approximately 626,000 square feet of manufacturing space at our manufacturing facilities as of December 31, 2002, with only minimal additions in 2003.

In July 1999, we purchased another vacant lot of approximately 280,000 square feet (approximately 6.5 acres) bordering our current manufacturing complex located in Shenzhen, China at a cost of approximately $1.2 million. We have built another factory consisting of approximately 265,000 square feet of space. Construction started in September 2003 and completed in December 2004. We expect full operation can commence in April 2005. With this new addition, our principal manufacturing facilities now consists of 557,835 square feet of manufacturing space, 87,462 square feet of offices, 189,952 square feet of dormitories and 60,765 square feet of cafeteria space and a full services recreational building. As of December 31, 2004, we had spent $15.0 million to cover the cost of construction and fixtures and equipment for the new factory. The financing for these improvements to our manufacturing facilities was obtained from internal resources.

LCD Factory

In October 2003, Jetup Electronic (Shenzhen) Co., Ltd. entered into a tenancy agreement for new factory premises, which is also located in Baoan County, Shenzhen, China, and relocated to the new factory premises in October 2004. The new factory premises are about twice the size of the former factory premises and consist of 383,547 square feet of manufacturing space, 32,005 square feet of offices, 221,666 square feet of dormitories, and 36,807 square feets of cafeteria and recreational spaces. This new factory provides room for the future expansion of production capacity. As of December 31, 2004, we had spent $7.7 million for this relocation and financed this amount with a combination of internal resources and bank financing.

Software Development

We currently lease two offices in which we conduct software development. Our Shekou, Shenzhen, China office is approximately 12,374 square feet, which we lease under two one-year leases expiring in July 2005. The monthly rental is approximately $7,667. In July 2003, we opened an office in Tokyo, Japan to further expand our sales and marketing team in Japan for our software development business. The Tokyo office has approximately 904 square feet, which we lease under a two-year lease expiring in June 2005. The monthly rental for the Tokyo office is approximately $1,975. *See Item 3. Key Information Risk Factors. Risks Related to Our Operations in China, Hong Kong, Macao and Japan.*

Item 5. *Operating and Financial Review and Prospects*

Except for statements of historical facts, this section contains forward-looking statements involving risks and uncertainties. You can identify these statements by forward-looking words including expect , anticipate , believe , seek estimate , intends , should , or may . Forward-looking statements are not guarantees of our future performance or results and our actual results could differ materially from those anticipated in these forward-looking statements as a result of certain factors, including those set forth under the section of this Report entitled Item 3. Key Information Risk Factors. This section should be read in conjunction with our Consolidated Financial Statements included as Item 18 of this Report.

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Operating Results

Overview

We are an electronics manufacturing and design services provider to a select group of the world s leading OEMs of telecommunications and consumer electronic products. Through our electronics manufacturing services operations, we manufacture electronic components and sub-assemblies, including LCD panels, LCD modules, RF modules, FPC sub-assemblies and image sensors modules. These components are used in numerous electronic products, including cellular phones, laptop computers, digital cameras, copiers, fax machines, electronic toys, handheld video game devices and microwave ovens. We also manufacture finished products, including cellular phones, palm-sized PCs, PDAs, electronic dictionaries, calculators, and digital camera accessories and Bluetooth™ wireless headset accessory for use with cellular phones.

We assist our OEM customers in the design and development of their products and furnish full turnkey manufacturing services that utilize advanced manufacturing processes and production technologies. Our services include hardware and software design, component purchasing, assembly into finished products, or electronic sub-assemblies and post-assembly testing. These services are value-added and assist us in obtaining new business but do not represent a material component of our revenue. We also provide ODM services, in which we design and develop proprietary products that are sold by our OEM customers using their brand name.

Net Sales and Cost of Sales

We derive our net sales principally from manufacturing services that we provide to OEMs of telecommunications and consumer electronic products. The market for the products we manufacture is generally characterized by declining unit prices and short product life cycles. Sales to our OEM customers are primarily based on purchase orders we receive from time to time rather than firm, long-term purchase commitments from our customers. We recognize sales, net of product returns and warranty costs, typically at the time of product shipment or, in some cases, as services are rendered.

Our production is typically based on purchase orders received from OEM customers. However, for certain customers, we will occasionally purchase raw materials based on such customers rolling forecasts. Purchase orders are often supported by letters of credit or written confirmation from our OEM customers. We generally do not obtain firm, long-term commitments from our customers. Uncertain economic conditions and our general lack of long-term purchase commitments with our customers make it difficult for us to accurately predict our revenue over the longer term. Even in those cases where customers are contractually obligated to purchase products from us or to repurchase unused inventory from us, we may elect not to immediately enforce our contractual rights because of the long-term nature of our customer relationships and for other business reasons, and instead may negotiate accommodations with customers regarding particular situations.

Gross Margins

Complex products generally have relatively high material costs as a percentage of total unit costs and accordingly our strategic shift to produce more of such products has historically been a factor that has adversely affected our gross margins. This is the primary reason for the decline in our gross margins between 1999 and 2001. During this period, we diversified our product mix from predominantly low complexity electronic products, including calculators and electronic dictionaries, to include more complex components and sub-assemblies, like LCD modules and RF modules. We believe our gross margin improved in 2002 and 2003 as a result of the experience we acquired in manufacturing these more complex products as we changed our strategic focus. Despite the lower gross margin on more complex products, we believe that the opportunity for growth in the demand for these complex products justifies the shift in our strategic focus. Furthermore, we believe that the experience in manufacturing processes and know-how that we have developed from producing more complex products are a competitive advantage for us relative to many of our competitors.

The increased costs associated with developing advanced manufacturing techniques to produce complex products on a mass scale and at a low cost have also negatively impacted our gross margins. For example, in our initial production runs of LCD modules and RF modules, we experienced low production yields and other inefficiencies that caused our gross margin to decrease. Although we believe we have improved the efficiency and quality of our manufacturing processes relating to LCD modules and RF modules, we may not be able to improve or maintain our gross margin for these products. Furthermore, in January 2003, we began to produce color and TFT LCD modules, each a complex component used in a variety of devices. The increased costs associated with manufacturing these products and other new complex products could have a negative impact on our future gross margins. The complex manufacturing processes involved in the production of complex products is also capital intensive, thereby increasing our fixed overhead costs. It has been our strategy to shift our focus more to the business of key components sub-assembly. The key components sub-assembly business generally accounts for relatively lower gross profit margin business. Nam Tai has been very successful in shifting its focus to key components sub-assembly, which accounted for 59% of our sales in 2004. We believe that the strong growth of this business will offset the impact of lower gross profit margins and we can continue to achieve strong growth in our overall profits. In the long run, we expect to achieve an overall gross profit margins of around 12%.

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Income Taxes

Under current BVI law, our income is not subject to taxation. Subsidiaries operating in Hong Kong and China are subject to income taxes as described below, and our subsidiary operating in Macao is exempted from income taxes. This would be valid unless the Macao government changes its policy towards offshore companies.

Under current Cayman Islands law, Nam Tai Electronic & Electrical Products Limited, Zastron Precision-Tech Limited, J.I.C. Technology Company Limited and Namtek Software Development Company Limited are not subject to profit tax in the Cayman Islands as they have no business operations in the Cayman Islands. However, they may be subject to Hong Kong income taxes as described below if they are registered in Hong Kong.

The provision for current income taxes of the subsidiaries operating in Hong Kong has been calculated by applying the current rate of taxation of 16% for 2002 and 17.5% for both 2003 and 2004 to the estimated taxable income earned in or derived from Hong Kong during the applicable period.

The basic corporate tax rate for Foreign Investment Enterprises in China, such as our Chinese subsidiaries, is currently 33% (30% state tax and 3% local tax). However, because all of our Chinese subsidiaries are located in Shenzhen and are involved in production operations, they qualify for a special reduced state tax rate of 15%. In addition, the local tax authorities in the regions in which our subsidiaries operate in Shenzhen are not currently assessed any local tax, though that could change at any time. Moreover, several of our Chinese subsidiaries are entitled to certain tax benefits and certain of our Chinese subsidiaries have qualified for tax refunds as a result of reinvesting their profits earned in previous years in China.

Efforts by the Chinese government to increase tax revenues could result in decisions or interpretations of the tax laws by the Chinese tax authorities that are unfavorable to us and which increase our future tax liabilities, or deny us expected refunds. Changes in Chinese tax laws or their interpretation or application may subject us to additional Chinese taxation in the future.

Our effective tax rates were 8%, 1% and 1% for 2002, 2003 and 2004, respectively. The significant factors that caused our effective tax rates to differ from the applicable statutory rates of 15% were as follows:

	2002	**2003**	**2004**
Applicable statutory tax rates	15%	15%	15%
Effect of loss / income for which no income tax benefit/expense is receivable/payable	6%	(2%)	(10%)
Tax losses not recognised			1%
Tax holidays and incentives	(5%)	(5%)	(3%)
Effect of China tax concessions, giving rise to no China tax liability	(21%)	(8%)	(3%)
Under / (over) provision of income tax expense in prior years	5%		
Other items which are not assessable (deductible) for tax purposes	8%	1%	1%
Effective tax rates	8%	1%	1%

Strategic Investments

An important element of our strategy is to make investments in companies that provide the potential to complement our existing products and services, become new customers, augment our market coverage and sales ability, enhance our technological capabilities and expand our service offerings. We account for investments of less than 20% under the cost method and we account for investments between 20% and 50% under the equity method. Our material investments over the last five years include:

Stepmind. In December 2003, we placed approximately $5.3 million into an escrow account for an investment in Stepmind. The investment was to occur in two phases. For the first phase, approximately $2.64 million, representing 7.66% of the equity interest in Stepmind, was released to Stepmind in January 2004. The second phase amounting to $2.65 million was released to Stepmind in August 2004 subject to fulfillment of certain conditions. In August 2004, we disposed of our entire interest in Stepmind to one of the shareholders of Stepmind at the original subscription price for those shares.

Alpha Star/JCT. In January 2003, we invested $10.0 million for a 25% equity interest in Alpha Star Investments Ltd., the ultimate holding company of JCT. JCT is engaged in the design, development and marketing of wireless communication terminals and wireless application software and is using us to manufacture wireless communication terminals and their related modules. In September 2004, we made an impairment to write down our $10.0 million investment in Alpha Star to a fair value of approximately $3.0 million. As of December 31, 2004, another analysis had been conducted by an independent valuer, who determined that no further impairment to value was required.

TCL Group. Over the period from September 2000 through November 2002, we made three investments in the TCL Group of companies and disposed of a portion of the investment in 2002 and 2003. In 2004, we further increased our investment in TCL Mobile from holding approximately 3% to 9% through the acquisition of Jasper Ace. The TCL group of companies is a leading OEM for numerous consumer electronic and telecommunications products in the domestic Chinese market.

In September 2000, we made a strategic investment of $2.0 million to acquire a 5% indirect equity interest (through a 25% direct equity interest in Mate Fair) in both TCL Mobile Communication (HK) Co., Ltd. and Huizhou TCL Mobile Communication Co., Ltd., together known as TCL Mobile. TCL Mobile is engaged in manufacturing, distributing and trading of digital mobile phones and accessories in China and overseas markets. In October 2002, we began to provide TCL Mobile with LCD modules used in its mobile phones.

In January 2002, we acquired a 6% equity interest in TCL Corporation (formerly known as TCL Holdings Corporation Ltd.), the parent of the TCL Group of companies, for approximately $12.0 million.

In November 2002, Mate Fair sold a portion of its equity interest in Huizhou TCL Mobile Communication Co. Ltd. for which we received proceeds of approximately $10.4 million, reducing our direct equity interest (held through Mate Fair) in TCL Mobile to approximately 3%.

In November 2002, we invested $5.1 million in the 3% convertible notes of TCL International Holdings Limited that are due in November 2005. TCL International Holdings Limited is another company in the TCL Group and is publicly listed on the Hong Kong Stock Exchange. Those convertible notes of TCL International Holdings Limited were disposed of in August 2003 for approximately $5.03 million.

In April 2004, we increased our shareholding in TCL Mobile from approximately 3% to 9% through acquiring Jasper Ace, which directly holds 9% equity interest in TCL Mobile, at a consideration of approximately $102.2 million. The consideration was satisfied, by the exchange of our 72.2% equity interest in Mate Fair, plus cash of $25 million and the issuance of 1,416,764 new Nam Tai shares and resulted in a net investment cost of $79.5 million.

Deswell Industries. In September 2000, we purchased 500,000 common shares in Deswell Industries Inc., a Nasdaq-listed company, representing approximately 9% of the outstanding shares of Deswell at the time of the purchase for an aggregate of $7.5 million. Deswell is a manufacturer of injection-molded plastic parts and components, electronic products and sub-assemblies and metallic molds and accessory parts for OEMs and contract manufacturers. During the first quarter of 2002, we sold our Deswell shares in the open market for aggregate proceeds of $10.1 million.

The following details the impact of our strategic investments on our income statements for each of the years ended 2002, 2003 and 2004:

	2002	2003	2004
		(in thousands)	

Cost Investments				
Included in other income:				
Deswell	Realized gain on disposal of marketable securities	$ 642	$	$
Deswell	Dividend income received from marketable securities	114		
TCL Corporation	Dividend income received from investment	803	1,696	926
Huizhou TCL	Dividend income received from investment		2,018	17,369
		$ 1,559	$3,714	$18,295
Equity Investments				
Included in equity in income (loss) of affiliated companies:				
Mate Fair		$10,741	$	$
Alpha Star Investments Limited		$	$ 498	$ (6,806)
Equity in income (loss) of affiliated companies		$10,741	$ 498	$ (6,806)
Included in other income:				
Mate Fair	Release of unamortized goodwill of affiliated companies	$ (520)	$	$
		$10,221	$ 498	$ (6,806)

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Toshiba Joint Venture

In March 2000, we formed a joint venture with Toshiba Battery Company Ltd. called BPC (Shenzhen) Co., Ltd., or BPC, to manufacture rechargeable lithium ion battery packs at our manufacturing complex in Shenzhen, China. Toshiba Battery Company Ltd. owned a 13% interest in BPC and we owned the balance of BPC for a cash investment of $1.3 million. During 2000 and 2001 and from January 1 to April 30, 2002, we recognized net sales of $6.2 million, $21.1 million, and $7.8 million, respectively, from Toshiba and its related companies. In 2002, we sold our 87% joint venture interest in BPC and a related manufacturing license to a Toshiba-related company for an aggregate of $2.9 million, resulting in a gain of $77,000.

Based on the 2001 full year results of BPC, we estimate that the sale of BPC will result in a reduction of annual revenues for 2002 of approximately $21.1 million and a reduction in profits of $1.3 million for 2002. We further estimate that the BPC sale will result in a reduction of annual operating expenses of approximately $600,000 for 2002. Cash flows from operations for 2002 would decline by approximately $1.7 million.

J.I.C. Group

We acquired the J.I.C. Group in October 2000 for $32.8 million. We paid a portion of the purchase price to the seller by issuing approximately 3.48 million of our common shares and paid $11.0 million in cash. The J.I.C. Group is principally engaged in the manufacture and marketing of transformers and LCD panels, a key component for a variety of consumer electronic products. We accounted for the acquisition of the J.I.C. Group under the purchase method of accounting and the results of the J.I.C. Group s operations have been consolidated with our results since the date of its acquisition.

In June 2002, through a reverse merger, we arranged for the listing of the J.I.C. Group on the Hong Kong Stock Exchange. To effect the listing, we entered into an agreement with the liquidators of Albatronics to effect the restructuring proposal of Albatronics and the listing of J.I.C. Technology Company Limited as this arrangement was more cost effective than using an initial public offering.

Due to the reverse merger, our effective interest in the J.I.C. Group was reduced from 100% to 92.9%. As a result of this reduction in interest during 2002, we have released unamortized goodwill of $1.5 million, representing 7.1% of the goodwill that had previously been recorded upon purchasing the J.I.C. Group in October 2000. The release of unamortized goodwill is included as part of the loss on the reverse merger of the J.I.C. Group.

In August 2002, we acquired an additional 7,984,000 ordinary shares of J.I.C. Technology Company Limited for a cash consideration of $437,000, resulting in additional goodwill of $253,000. As of December 31, 2002, we held 93.97% of effective interest in J.I.C. Group, which represented 74.78% of the existing ordinary shares and 93.97% of the outstanding ordinary shares upon full conversion of the 598,420,000 preference shares.

During the period from June to November 2003, we disposed of a total of 42,600,000 ordinary shares of J.I.C. Technology Company Limited for cash consideration of $4.0 million. The disposal resulted in a net gain on partial disposal of a subsidiary of $1.8 million and the releasing of unamortized goodwill of $1.2 million. The release of unamortized goodwill is netted off with the gain on the partial disposal of a subsidiary. In November 2003, we converted 175,100,000 preference shares into 170,000,000 ordinary shares of J.I.C. Technology Company Limited.

In June 2003, in order to concentrate its effort on its LCD panels reporting unit, J.I.C. Technology Company Limited disposed of its transformers reporting unit to a third party for a cash consideration of $2.4 million. Sales of the transformers reporting unit for the years ended December 31, 2002 and 2003 were $11.3 million and $6.3 million, respectively, and were insignificant compared to the sales as a whole. The net income from this discontinued operation for the years ended December 31, 2002 were also immaterial. In 2003, the net income from discontinued operation represented the gain of $2.0 million, being the proceeds from the disposal less the carrying value of the net assets of the transformers reporting unit, and minority interests. Excluding this gain, the basic and diluted earnings per share for the year ended December 31, 2003 would have been $1.04 and $1.02, respectively.

During the period from November to December 2004, we further disposed of a total of 128,000,000 ordinary shares of J.I.C. Technology Company Limited for cash consideration of $12.95 million. The disposal resulted in a net gain on partial disposal of a subsidiary of $6.25 million. During the same period, we converted all 423,320,000 preference shares into 410,990,290 ordinary shares. As of December 31, 2004, we held 546,890,978 ordinary shares of J.I.C. Technology Company Limited, equivalent to 71.63% of issued ordinary shares.

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Summary of Results

Net sales for 2004 increased 31% to $533.8 million compared to $406.3 million for 2003. The increase in sales was primarily due to an increase in the sales in telecom components sub-assemblies and optical devices. The increase in our net sales base year-over-year represents stronger demand from existing customers, as well as organic growth from new and existing customers.

The following table sets forth key operating results (in thousands, except per share data) for the years ended December 31, 2002, 2003 and 2004:

	Year Ended December 31,		
	2002	**2003**	**2004**
Net sales	$ 236,016	$ 406,306	$ 533,861
Gross profit	38,060	66,290	76,476
Operating income	17,052	37,387	43,378
Net income	20,023	43,802	66,885
Basic earnings per share	0.57	1.09	1.57
Diluted earnings per share	0.57	1.07	1.57

Key Performance Indicators

The following table sets forth, for the quarterly periods indicated, certain of management s key financial performance indicators that management utilizes to assess the Company s operating results:

	Three Months Ended			
	December 31, 2003	**September 30, 2003**	**June 30 2003**	**March 31, 2003**
Sales cycle (1)	27 days	23 days	27 days	32 days
Inventory turns (2)	13 turns	17 turns	16 turns	9 turns
Days in accounts receivable (3)	58 days	61 days	60 days	61 days
Days in accounts payable (4)	60 days	60 days	55 days	69 days

	Three Months Ended			
	December 31, 2004	**September 30, 2004**	**June 30 2004**	**March 31, 2004**
Sales cycle (1)	9 days	29 days	41 days	29 days
Inventory turns (2)	20 turns	15 turns	11 turns	10 turns
Days in accounts receivable (3)	62 days	54 days	86 days	56 days
Days in accounts payable (4)	72 days	49 days	79 days	64 days

(1) The sales cycle is calculated as the sum of days in accounts receivable and days in inventory, less the days in accounts payable.

(2) Inventory turns are calculated as the ratio of four times our year to date cost of sales divided by inventory, net, at period end divided by numbers of quarters.

(3) Days in accounts receivable is calculated as the ratio of accounts receivable, net, at period end divided by year to date average daily net sales.

(4) Days in accounts payable is calculated as the ratio of accounts payable, net, at period end divided by year to date average daily net cost of sales.

Critical Accounting Policies and Estimates

The preparation of our financial statements and related disclosures in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and judgments that affect our reported amounts of assets and liabilities, revenues and expenses, and related disclosures of contingent assets and liabilities. On an on-going basis, we evaluate our estimates and assumptions based upon historical experience and various other factors and circumstances. Management believes that our estimates and assumptions are reasonable under the circumstances; however, actual results may vary from these estimates and assumptions under different future circumstances. We have identified the following critical accounting policies that affect the more significant judgments and estimates used in the preparation of our consolidated financial statements. For further discussion of our significant accounting policies, refer to Note 2 Summary of Significant Accounting Policies to the Consolidated Financial Statements.

Marketable securities

Marketable securities at December 31, 2004 are principally equity securities and are classified as available-for-sale. Securities classified as available-for-sale are stated at fair value with unrealized gains and losses recorded as a separate component of accumulated other comprehensive income (loss). Fair value is determined by reference to market price or analysis conducted by independent valuer. In the event where the fair value of the securities has been below the carrying value for a period of time, we will assess whether this decline in value is other-than-temporary.

Our assessment includes the consideration of the duration and severity of the decline in values and our ability and intent to hold the investments for a reasonable period of time sufficient for a forecasted recovery of the fair value up to or beyond the cost of the investment, and an assessment of the evidence indicating that the cost of the investment is recoverable within a reasonable period of time which outweighs the evidence to the contrary. If it is determined that the decline is other-than-temporary, an impairment charge to the income statement will be made.

Valuation of long-lived assets, including goodwill and purchased intangible assets

The Company reviews the carrying value of its long-lived assets, including goodwill and purchased intangible assets, for impairment whenever events or changes in circumstances indicate that the carrying value may not be recoverable. The Company assesses the recoverability of the carrying value of long-lived assets, other than goodwill and purchased intangible assets with indefinite useful lives, by first grouping its long-lived assets with other assets and liabilities at the lowest level for which identifiable cash flows largely independent of the cash flows of other assets and liabilities (the asset group) and, secondly, estimating the undiscounted future cash flows that are directly associated with and expected to arise from the use of and eventual disposition of such asset group. The Company estimates the undiscounted cash flows over the remaining useful life of the primary asset within the asset group. If the carrying value of the asset group exceeds the estimated undiscounted cash flows, the Company records an impairment charge to the extent the carrying value of the long-lived asset exceeds its fair value. The Company determines fair value through quoted market prices in active markets or, if quoted market prices are unavailable, through the performance of internal analysis of discounted cash flows or external appraisals. The undiscounted and discounted cash flow analyses are based on a number of estimates and assumptions, including the expected period over which the asset will be utilized, projected future operating results of the asset group, discount rate and long-term growth rate.

To assess goodwill for impairment, the Company performs an assessment of the carrying value of its reporting units at least on an annual basis or when events and changes in circumstances occur that would more likely than not reduce the fair value of the Company s reporting units below their carrying value. If the carrying value of a reporting unit exceeds its fair value, the Company would perform the second step in its assessment process and would record an impairment charge to earnings to the extent the carrying amount of the reporting unit goodwill exceeds its implied fair value. The Company estimates the fair value of its reporting units through internal analysis and external valuations, which utilize income and market valuation approaches through the application of capitalized earnings, discounted cash flow and market comparable methods. These valuation techniques are based on a number of estimates and assumptions, including the projected future operating results of the reporting unit, discount rate, long-term growth rate and appropriate market comparables.

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The Company s assessments of impairment of long-lived assets, including goodwill and purchased intangible assets, and its periodic review of the remaining useful lives of its long-lived assets are an integral part of the Company s ongoing strategic review of its business and operations. Therefore, future changes in the Company s strategy and other changes in the operations of the Company could impact the projected future operating results that are inherent in the Company s estimates of fair value, resulting in impairments in the future. Additionally, other changes in the estimates and assumptions, including the discount rate and expected long-term growth rate, which drive the valuation techniques employed to estimate the fair value of long-lived assets and goodwill could change and, therefore, impact the assessments of impairment in the future.

In performing the annual assessment of goodwill for impairment, the Company determined that none of the reporting units carrying values were close to exceeding their respective fair values.

Revenue recognition

The Company recognizes revenue when all of the following conditions are met:

- Persuasive evidence of an arrangement exists;
- Delivery has occurred or services have been rendered;
- Price to the customer is fixed or determinable; and
- Collectibility is reasonably assured.

Revenue from sales of products is recognized when the title is passed to customers upon shipment and when collectibility is assured. The Company does not provide its customers with the right of return (except for quality), price protection, rebates or discounts. There are no customer acceptance provisions associated with the Company s products, except for quality. All sales are based on firm customer orders with fixed terms and conditions, which generally cannot be modified.

Deferred Income Taxes

We provide deferred income taxes using the asset and liability method. Under this method, we recognize deferred income taxes for all significant temporary differences and classified as current or non-current based upon the classification of the related asset or liability in the financial statements. We provide a valuation allowance to reduce the amount of deferred tax assets if it is considered more likely than not that some portion, or all, of the deferred tax asset will not be realized.

When considering whether a valuation allowance is necessary, we will assess the history of operating losses and unexpired tax credit, losses expected in the future and any unsettled circumstances that, if unfavorably resolved, would adversely affect future operations and profit levels on a continuing basis in future years. Therefore, any changes in our assessment of the above would impact our estimation of the amount of valuation allowance.

Accruals and Provisions for Loss Contingencies

We make provisions for all loss contingencies when information available to us prior to the issuance of the financial statements indicates that it is probable that an asset had been impaired or a liability had been incurred at the date of the financial statements and the amount of loss can be reasonably estimated.

For provisions or accruals related to litigations, we make provisions based on information from legal counsels and the best estimation of management. As discussed in Note (19b) to our consolidated financial statements, we are involved in various legal proceedings and contingencies. We have recorded a liability for the Tele-Art matter in accordance with Statement of Financial Accounting Standards No. 5, Accounting for Contingencies , or FAS 5. FAS 5 requires a liability to be recorded based on our estimate of the probable cost of the resolution of a contingency. The actual resolution of this contingency may differ from our estimates. If the contingency were settled for an amount greater than our estimate, a future charge to income would result. Likewise, if the contingency were settled for an amount that is less than our estimate, a future credit to income would result.

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Results of Operations

The following table presents selected consolidated financial information stated as a percentage of net sales for the years ended December 31, 2002, 2003 and 2004 (certain amounts may not calculate due to rounding and amounts may not add due to rounding).

	Year Ended December 31,		
	2002	**2003**	**2004**
Net sales	100.0%	100.0%	100.0%
Cost of sales	(83.9)	(83.7)	(85.7)
Gross profit	16.1	16.3	14.3
Selling, general and administrative expenses	(7.6)	(6.1)	(5.2)
Research and development expenses	(1.1)	(1.0)	(1.0)
Impairment of goodwill	(0.2)		
Income from operations	7.2	9.2	8.1
Other (expenses) income, net	(2.9)	0.7	3.2
Gain on partial disposal of subsidiaries		0.5	14.5
Unrealised loss on marketable securities			(10.9)
Interest income	0.3	0.2	0.2
Interest expense	(0.3)		
Income before income taxes and minority interests	4.3	10.6	15.1
Income taxes	(0.3)	(0.1)	(0.2)
Income before minority interests and equity in income (loss) of affiliated companies	4.0	10.5	14.9
Minority interests	(0.1)	(0.3)	(1.1)
Equity in income (loss) of affiliated companies	4.6	0.1	(1.3)
Income after minority interests and equity in income (loss) of affiliated companies	8.5	10.3	12.5
Discontinued operation		0.5	
Net income	8.5%	10.8%	12.5%

Year Ended December 31, 2004 Compared to Year Ended December 31, 2003

Net Sales. Our net sales increased 31.4% to $533.9 million for 2004, up from $406.3 million in 2003. The increase was due to increased sales levels across all business segments. Specific increases include a 27.0% increase in the sales of consumer electronics and communication products, a 36.4% increase in the sales of telecommunication components assembly, a 17.9% increase in the sales of LCD panels and a 20.6% increase in the sales of software development services. The increased sales levels were due to the addition of new customers, and organic growth in these business segments. The increase in the consumer electronics and communication products was primarily attributable to the increased sales levels in optical devices. The increase in telecom, components assembly was primarily attributable to sales of FPC sub-assemblies in 2004 and the increase in sales of levels of mobile phone handsets in SKD forms and lighting panels for hand-held devices.

The following table sets forth, for the periods indicated, revenue by business segments expressed as a percentage of net sales. The distribution of revenue across our business segments has fluctuated, and will continue to fluctuate, as a result of numerous factors, including but not limited to the following: increased business from new and existing customers, fluctuations in customer demand and seasonality.

	Year Ended December 31,		
	2002	**2003**	**2004**
Consumer Electronics and Communication Products	40%	32%	31%
Telecommunication Components Assembly :			
Telecommunication components assembly(1)	44%	57%	59%
Software development services	1%	1%	1%
LCD Panels and Transformers			
LCD panels	10%	9%	9%
Transformers(2)	5%	1%	
	100%	100%	100%

(1) Included in telecommunication components assembly are our sales from our manufacture of rechargeable battery packs through a joint venture we had with Toshiba Battery Co., Ltd. We sold our interest in the joint venture to a Toshiba-related company and ceased manufacturing rechargeable battery packs as of April 30, 2002. Accordingly, revenue from sales of battery packs was not included after that date.

(2) We sold our transformers operation to a third party in June 2003.

Gross Profit. Gross profit decreased to 14.3% of net sales in 2004 from 16.3% in 2003. Generally, the gross margin for box-built products is higher than key components assembly. Our target was to shift our business to the high-growth and high-technology key components assemblies sector, and we succeeded in increasing net sales in the TCA segment. The percentage decrease in gross profit was primarily due to a higher proportion of TCA segment revenue. Additionally, we have been impacted by the reduction of input credit in respect of value-added tax related to domestic purchase materials by the PRC government during 2004.

In terms of dollar values, gross profit for 2004 increased by $10.2 million from 2003, due to the increased revenue base.

Selling, General and Administrative Expenses. Selling, general and administrative expenses increased to $28.1 million, or 5.2% of net sales in 2004 from $24.9 million, or 6.1% of net sales in 2003. The $3.2 million increase was primarily attributable to the increase in sales commission paid to marketing staff as a result of increased revenue, and the commission paid to external agents for particular products during 2004. The decrease as a percentage of net sales was due primarily to the increased revenue base in 2004.

Research and development Expenses. Research and development expenses in 2004 increased to $5.0 million from $4.0 million in 2003 but remained at 1.0% of net sales for each of 2004 and 2003. The absolute dollar increase was primarily attributable to the recruitment of more engineers to support our R&D activities, including design of production process, development of new products and products associated with customer design-related programs.

Other (Expenses) Income. During 2004, other income was $17.3 million. We received $17.4 million and $0.9 million dividend income from our investment in TCL Communication and TCL Corporation, respectively. This income was partially offset by $0.2 million in bank charges and $0.9 million in other non-operating charges.

During 2003, other income was $2.9 million. The amount included dividend income of $2.0 million from our indirect investment in TCL Communication, dividend income of $1.7 million from TCL Corporation, and income of $0.5 million related to the recovery of a non-trade receivable which had been written off previously. This income was partially offset by $0.3 million in bank charges during 2003.

Gain on Partial Disposal of Subsidiaries. In April 2004, one of the previously wholly-owned subsidiaries of the Company, NTEEP, completed a public offering of its common stock on The Hong Kong Stock Exchange. As a result, the Company disposed of a 25% interest in this subsidiary, resulting in a gain on partial disposal of US$71.1 million.

In November and December 2004, the Company disposed of 128 million ordinary shares of J.I.C. for cash consideration of $12.9 million. The disposal resulted in a net gain on partial disposal of interest in J.I.C. of $6.3 million after deducting the release of unamortized goodwill of $3.5 million.

During 2003, we recorded a $1.8 million gain on partial disposal of interest in J.I.C.

Unrealized Loss of Marketable Securities. At December 31, 2004, the Company s investment in TCL Communication was stated at fair value based on the traded market price of TCL Communication s shares and the Company recognized an unrealized loss of $58.3 million, based on the Company s cost of $79.5 million and a fair value of $21.2 million. As the loss is considered to be other-than-temporary, it has been recorded in the consolidated statements of income.

Interest Income. Interest income increased to $1.1 million in 2004 from $0.8 million in 2003. The increase was primarily due to higher average cash balances, partially offset by lower interest yields on cash deposits.

Interest Expense. Interest expense increased to $195,000 in 2004 from $121,000 in 2003. This increase was primarily a result of the draw-down of a $7.0 million fixed-term loan by J.I.C.

Income Taxes. Income tax expenses of $879,000 for 2004 compares to $399,000 for 2003. The increase was primarily the result of not receiving full tax refunds for several of our PRC entities for taxes paid in previous years that we have normally been eligible to receive full tax refunds in the past as a result of the strict enforcement of certain regulations.

Minority Interests. Minority interest increased to $6.0 million in 2004 from $1.1 million in 2003. The increase was primarily the result of the increase in minority shareholders share of NTEEP s profit of approximately $4.9 million since its listing in April 2004. In addition, the minority shareholders share of profits of the J.I.C. Group for 2004 increased to $254,000 from $211,000 in 2003, and the minority shareholders share of profits of Namtek Software Development Company Limited for 2004 increased to $472,000 from $296,000 in 2003. The minority shareholders share of profits of Mate Fair for 2004 decreased to $405,000 from $560,000.

Equity in Income (Loss) of Affiliated Companies. We recorded an equity in loss of $6.8 million for 2004 of Alpha Star but recognized $0.5 million in equity in income for 2003. The amount in 2004 included an impairment charge of approximately $5.6 million upon careful assessment of various factors relevant to the affiliate, including the competitive handset market in the PRC and $1.2 million share of loss of Alpha Star. For additional information, see Note 8 Investment in Affiliated Companies, Equity Method Alpha Star to the Consolidated Statements of Income.

Year Ended December 31, 2003 Compared to Year Ended December 31, 2002

Net Sales. Our net sales increased significantly by 72.2% to $406.3 million for 2003 compared to $236.0 million for 2002. The increase was primarily attributable to sales of the telecommunication components assembly products of approximately $232.2 million in 2003 compared to $103.8 million in 2002, an increase of $128.4 million. This increase was mainly as a result of an increase in sales of telecom LCD and PCB modules and the launch of new products in 2003, like RF modules, SKD handsets, front light panel assembly, and flash light for cellular phones.

In addition, we also experienced increased sales in consumer electronics and communication products. Sales of consumer electronics and communication products amounted to approximately $128.8 million in 2003 compared to $94.0 million in 2002, an increase of $34.8 million. This increase was mainly driven by the PC camera, which was first launched in 2003.

Sales of LCD panels and transformers increased by 17.2% to $41.3 million for 2003 compared to $35.3 million for 2002. The primary reason for the increase in sales of LCD panels and transformers was the increase in the sales of LCD panels of approximately $35.0 million for 2003 compared to $23.9 million for 2002, which was partially offset by a decrease in the sales of transformers due to the disposal of the transformers operation in June 2003.

Gross Profit. Our gross profit increased by 74.2% to $66.3 million for 2003 compared to $38.1 million for 2002. Our gross profit margin also increased slightly in 2003 to 16.3% from 16.1% in 2002.

The primary reason for this increase was the increase in sales as described above in the explanation of fluctuation of Net Sales . We were also able to keep our product gross margin relatively stable in 2003. The increase in gross profit margin was offset by the gain of a $2.0 million due to the recovery of inventory written down to cost of sales in 2002. In addition to these specific factors, our gross profit margin increased in 2003 due to our ability to negotiate advantageous price terms with certain of our suppliers and our focus on reducing overhead costs.

In addition, the gross profit of the LPT segment also increased. This increase was as a result of increases in the sales proportion of high margin products and the disposal of the transformers operation in June 2003. The impact of the discontinued operations of transformers on gross profit contribution was insignificant as the margin of transformers products was low.

Selling, General and Administrative Expenses. SG&A expenses for 2003 increased by approximately $6.9 million to $24.9 million, or 6.1% of net sales, from $18.0 million, or 7.6% of net sales, in 2002.

This increase was primarily due to an approximately $5.1 million increase in salaries and benefits expenses, due to an increase in headcount, an approximately 10% increase in salary for certain employees and a $3.9 million incentive bonus due to the implementation of a new incentive bonus scheme in January 2003, which was calculated based on operating profit, as well as a $0.9 million increase in selling expenses, which was primarily due to more sales commissions paid as sales increased.

Our SG&A expenses include provisions for bad debt expenses, which decreased from $138,000 in 2002 to $91,000 in 2003. The decrease in allowance has been attributable to the implementation of tighter credit controls.

Research and Development Expenses. Research and development expenses for 2003 increased to $4.0 million, or 1.0% of net sales, from $2.7 million, or 1.1% of net sales, in 2002. The increase was due to an increase in the number of staff related to the expansion of our production capacity and the products we manufacture.

Goodwill Impairment. In 2002, we determined that $339,000 of unamortized goodwill related to our 1999 acquisition of a telecommunications company was impaired as the technology of the acquired company had become obsolete.

Other (Expenses)/Income, Net. Other income, net, during 2003 was $2.9 million. This amount included dividend income of $2.0 million from our indirect investment in Huizhou TCL Mobile Communication Co., Ltd., dividend income of $1.7 million from TCL Corporation and income of $0.5 million related to the recovery of a non-trade receivable which had been written off previously. This income was partially offset by a $0.3 million bank charge during 2003.

Gain on Partial Disposal of Subsidiaries. Gain on partial disposal of subsidiaries in 2003 of $1.8 million represented gain on partial disposal of interests in J.I.C. Technology while the amount in 2002 of $17,000 represented the gain on disposal of a subsidiary, BPC (Shenzhen) Co. Ltd.

Interest income. Interest income decreased to $788,000 in 2003 from $799,000 in 2002 due to lower average cash balances and lower interest yields on cash deposits.

Interest Expense. Interest expense decreased to $121,000 for 2003 compared to $790,000 for 2002. The decrease in interest expenses is the result of the early repayment of a $12.9 million bank loan in January 2003.

Income Taxes. Income tax expenses decreased to $399,000 for 2003 compared to $773,000 for the prior year. The decrease is primarily the result of our receipt of tax refunds for several of our PRC entities for taxes paid in previous years.

Minority Interests. Minority interests increased by $903,000, or 550.6%, to $1,067,000 in 2003 from $164,000 in 2002. Minority interests in 2003 included $211,000 from the minority shareholders share of profits of the J.I.C. Group for 2003, $560,000 from the minority shareholders share of profits of Mate Fair for 2003 and $296,000 from the minority shareholders share of profits of Namtek Software Development Company Ltd. for 2003.

Equity in Income of Affiliated Companies. Equity in income of affiliated companies was $0.5 million in 2003 compared to $10.7 million in 2002. The income in 2003 represents our share of the net earnings of our proportional 25% investment in Alpha Star Investments Limited for the twelve months ended December 31, 2003. The income in 2002 represents our proportional share of the net earnings of our 25% investment in Mate Fair.

Discontinued Operation. Discontinued operation in 2003 represented $2.0 million gain on disposal of our entire transformers operation, net of $0.1 million shared by minority interest.

Liquidity and Capital Resources

Liquidity

We have financed our growth and cash needs to date primarily from internally generated funds, proceeds from the sale of our strategic investments, sales of our common stock and bank debt. We do not use off-balance sheet financing arrangements, such as securitization of receivables or obtaining access to assets through special purpose entities, as sources of liquidity. Our primary uses of cash have been to fund expansions and upgrades of our manufacturing facilities, to make strategic investments in potential customers and suppliers and to fund increases in inventory and accounts receivable resulting from increased sales.

We had positive net working capital of $218.2 million at December 31, 2004 compared to positive net working capital of $93.5 million at December 31, 2003. Our working capital requirements and capital expenditures could continue to increase in order to support future expansions of our operations through acquisition of land, construction of a new factory and machinery purchases. It is possible that future expansions may be significant and may require the payment of cash. Future liquidity needs will also depend on fluctuations in levels of inventory and shipments, changes in customer order volumes and timing of expenditures for new equipment.

We currently believe that during the next twelve months, our capital expenditures will be in the range of $35 million to $55 million, principally for land, machinery and equipment, and expansion in China. We believe that our level of resources, which include cash and cash equivalents, marketable securities, accounts receivable and available borrowings under our credit facilities, will be adequate to fund these capital expenditures and our working capital requirements for the next twelve months. Should we desire to consummate significant additional acquisition opportunities or undertake significant expansion activities, our capital needs would increase and could possibly result in our need to increase available borrowings under our revolving credit facilities or access public or private debt and equity markets. There can be no assurance, however, that we would be successful in raising additional debt or equity on terms that we would consider acceptable.

The following table sets forth, for the year ended December 31 2002, 2003 and 2004, selected consolidated cash flow information (in thousands):

	Year Ended December 31,		
	2002	2003	2004
Net cash provided by operating activities	$ 39,502	$ 44,272	$ 75,210
Net cash (used in) provided by investing activities	(33,760)	(21,669)	37,729
Net cash provided by (used in) financing activities	18,085	(43,253)	(14,117)
Effect of foreign currencies on cash flows	(26)		
Net increase (decrease) in cash and cash equivalents	$ 23,801	$ (20,650)	$ 98,822

Net cash provided by operating activities for 2004 was $75.2 million. This consisted primarily of $66.9 million of net income, $13.9 million of depreciation and amortization, $58.3 million unrealized loss on marketable securities, $6.8 million equity in loss of an affiliated company and $6.0 million in minority interests offset by $6.2 million in gain on partial disposal of J.I.C., $71.1 million gain on partial disposal of NTEEP and $15.9 million in dividend income. Our working capital related to operating activities increased, driven by an increase of $33.9 million in accounts payable and $3.0 million in accrued expenses and others payables, a decrease of $2.6 million in amount due from a related party, $3.9 million in inventories and $2.6 million in prepaid expenses and other receivables, offset by increases in accounts receivable of $28.3 million. The increase in accounts receivable and accounts payable was due to increased levels of business during 2004.

Net cash provided by investing activities of $37.7 million for 2004 consisted primarily of proceeds from partial disposal of subsidiaries and investments of $95.4 million and $5.6 million, respectively, proceeds from disposal of property, plant and equipment of $4.5 million, offset by capital expenditures of $38.6 million and increase in deposits for property, plant and equipment of $4.4 million and acquisition of marketable securities of TCL Communication of $25.1 million. Capital expenditure in 2004 mainly consisted of the construction of a new factory and purchases of machinery and equipment which were used to expand our manufacturing capacity and to upgrade our equipment to produce increasingly complex products.

Net cash used in financing activities of $14.1 million for 2004 resulted primarily from $19.4 million paid to shareholders as dividends, $5.4 million in repayment of bank loans, offset by proceeds of bank loans of $10.6 million.

Net cash provided by operating activities was $44.3 million in 2003. Cash provided by operating activities in 2003 was primarily attributable to net income of $43.8 million plus depreciation and amortization expense of $12.2 million, offset by the gain on disposal of transformers operation, net of minority interests of $2.0 million and a gain on the partial disposal of our J.I.C. Group for $1.8 million. Our working capital related to operating activities net of the effect of the disposal of a subsidiary decreased, driven by an increase of $11.1 million in accounts receivable, $3.0 million in prepaid expenses and other receivables, $2.7 million in the amount due from a related party and $8.5 million in inventories, which was offset by increases in accounts payable of $18.0 million, and accrued expenses and other payables of $1.2 million.

Our inventories increased in 2003 as a result of our anticipation of increases in sales. Accounts receivable increased due to an increase in sales in the fourth quarter relative to sales in the prior year. Accounts payable increased due to increased inventory purchases. Accrued expenses increased due to the provision of an incentive bonus in 2003.

Net cash used in investing activities was $21.7 million in 2003. Cash used in investing activities primarily related to our $10.0 million and $0.4 million strategic investments in Alpha Star Investments Limited and iMagic Infomedia Technology Limited, respectively, and $5.3 million prepayment for a long-term investment in Stepmind, as well as capital expenditures of $17.1 million and an increase in deposits for property, plant and equipment of $3.1 million, offset by $2.6 million proceeds on disposal of property, plant and equipment, $2.4 million proceeds on disposal of transformers operation to a third party, $4.0 million proceeds on the partial disposal of our J.I.C. Group, and $5.0 million proceeds on the disposal of convertible notes of TCL International Holdings Ltd.

Net cash used in financing activities was $43.3 million in 2003. Cash used in financing activities for 2003 primarily resulted from $37.8 million paid to shareholders as dividends and $14.0 million in bank loans repayment offset by $8.5 million received from the exercise of options.

Except as discussed above, there are no material transactions, arrangements and relationships with unconsolidated affiliated entities that are reasonably likely to affect liquidity.

For the years ended December 31, 2003 and 2004, the Company has made guarantees for debt, loans and credit facilities held by various wholly owned subsidiaries aggregating up to a maximum guarantee of $49,756,000 and $49,205,000, respectively. The terms of the guarantees correspond with the terms of the underlying debt, loan and credit facility agreements.

Capital Resources

As of December 31, 2004, we had $160.6 million in cash and cash equivalents, consisting of cash and short-term deposits, compared to $61.8 million as of December 31, 2003. Our long-term bank borrowing was $8.0 million and $2.8 million as of December 31, 2004 and December 31, 2003, respectively.

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As of December 31, 2004, we had in place general banking facilities with two financial institutions aggregating $87.9 million. The maturity of these facilities is generally up to 90 days. These banking facilities are guaranteed by us and there is an undertaking not to pledge any assets to any other banks without the prior consent of our bankers. However, these covenants do not have any impact on our ability to undertake additional debt or equity financing. Interest rates are generally based on the banks reference lending rates. Our facilities permit us to obtain overdrafts, lines of credit for forward exchange contracts, letters of credit, import facilities, trust receipt financing, shipping guarantees, working capital and revolving loans. No significant commitment fees are required to be paid for the banking facilities. These facilities are subject to annual review and approval. As of December 31, 2004, we had utilized approximately $3.4 million under such general credit facilities and had available unused credit facilities of $84.5 million.

As of December 31, 2004, we had two four-year term loans, which allowed us to borrow up to a maximum amount of $4.5 million and $7.0 million. The outstanding balance amounted to $8.1 million as of December 31, 2004 and $2.8 million as of December 31, 2003. Here is an analysis of the term loans:

	Date of draw down	Amount drawn (in million)	No. of installments	Amount per installment (in million)	Interest rate	First repayment	Outstanding balance at December 31, 2004 (in million)	Outstanding balance at December 31, 2003 (in million)
Term loan 1	May 2002	$ 4.5	16	$ 0.3	1.5% over LIBOR changed to 0.75% over LIBOR in August 2004	August 2002	$ 1.7	$ 2.8
Term loan 2								
	April 2004	$ 1.6	16	$ 0.1	0.75% over LIBOR	July 2004	$ 1.4	
	June 2004	$ 3.6	16	$ 0.2	0.75% over LIBOR	September 2004	$ 3.2	
	December 2004	$ 1.8	16	$ 0.1	0.75% over LIBOR	March 2005	$ 1.8	