Comba

Comba Telecom Systems Holdings Limited

京 信 通 信 系 統 控 股 有 限 公 司

(Incorporated in the Cayman Islands with limited liability)

(Stock Code: 2342)

Interim results announcement for the six months ended 30 June 2006

FINANCIAL HIGHLIGHTS

- Turnover increased by 42.7% to HK$589 million
- Gross profit increased by 25.9% to HK$253 million
- Profit attributable to shareholders increased by 26.8% to HK$46 million
- Basic earnings per share increased by 26.4% to 5.46 HK cents

INTERIM RESULTS

These condensed consolidated interim financial statements have not been audited, but have been reviewed by the Company's audit committee.

Condensed Consolidated Income Statement

For the six months ended 30 June 2006

	Notes	**For the six months ended 30 June** **2006** ***(Unaudited)*** ***HK$'000***	2005 *(Unaudited)* *HK$'000*
REVENUE	*3*	**589,490**	413,013
Cost of sales		**(336,702)**	(212,234)
Gross profit		**252,788**	200,779
Other income	*3*	**4,467**	4,352
Research and development costs		**(33,379)**	(21,682)
Selling and distribution costs		**(55,779)**	(43,768)
Administrative expenses		**(99,598)**	(91,429)
Other expenses		**(9,032)**	(265)
Finance costs	*5*	**(7,868)**	(9,197)
PROFIT BEFORE TAX	*4*	**51,599**	38,790
Tax	*6*	**(6,656)**	(4,534)
PROFIT FOR THE PERIOD		**44,943**	34,256
Attributable to:			
Equity holders of the parent		**45,561**	35,941
Minority interests		**(618)**	(1,685)
		44,943	34,256
EARNINGS PER SHARE ATTRIBUTABLE TO ORDINARY EQUITY HOLDERS OF THE PARENT *(HK cents)*	*7*		
Basic		**5.46**	4.32
Diluted		**5.41**	4.25
DIVIDEND PER SHARE *(HK cents)*	*8*	**Nil**	Nil

Condensed Consolidated Balance Sheet
30 June 2006

	30 June 2006	31 December 2005
	(Unaudited)	*(Audited)*
	HK$'000	*HK$'000*
NON-CURRENT ASSETS		
Property, plant and equipment	**195,590**	172,380
Prepaid land lease payments	**12,894**	13,040
Goodwill	**21,916**	21,916
Deferred tax assets	**26,106**	19,318
Other intangible assets	**6,464**	8,242
Total non-current assets	**262,970**	234,896
CURRENT ASSETS		
Inventories	**687,792**	572,948
Trade receivables	**897,461**	618,290
Notes receivables	**16,534**	35,585
Factored trade receivables	**—**	115,296
Prepayments, deposits and other receivables	**125,989**	112,807
Short term time deposits	**63,000**	178,296
Cash and cash equivalents	**180,883**	314,118
Total current assets	**1,971,659**	1,947,340
CURRENT LIABILITIES		
Trade and bills payables	**464,441**	356,753
Other payables and accruals	**241,287**	284,036
Interest-bearing bank loans	**252,345**	190,723
Bank advances on factored trade receivables	**—**	115,296
Current portion of finance lease payables	**90**	180
Tax payable	**9,491**	18,867
Provision for product warranties	**22,772**	21,066
Total current liabilities	**990,426**	986,921
NET CURRENT ASSETS	**981,233**	960,419
Net assets	**1,244,203**	1,195,315
EQUITY		
Equity attributable to equity holders of the parent		
Issued capital	**83,529**	83,302
Reserves	**1,153,635**	1,079,365
Proposed final dividend	**—**	24,991
	1,237,164	1,187,658
Minority interests	**7,039**	7,657
Total equity	**1,244,203**	1,195,315

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. ACCOUNTING POLICIES

The condensed consolidated interim financial statements are prepared in accordance with Hong Kong Accounting Standard ("HKAS") 34 "Interim Financial Reporting". The accounting policies and basis of preparation adopted in the preparation of the interim financial statements are the same as those used in the annual financial statements for the year ended 31 December 2005.

2. SEGMENT INFORMATION

The Group is principally engaged in the manufacture and sale of wireless telecommunications network enhancement system equipment and the provision of related engineering services. All of the Group's products are of a similar nature and subject to similar risks and returns. Accordingly, the Group's operating activities are attributable to a single business segment.

In addition, the Group's revenue, expenses, profit, assets and liabilities and capital expenditures are principally attributable to a single geographical region, which is the People's Republic of China (the "PRC"). Therefore, no analysis in business or geographical segment is presented.

3. REVENUE AND OTHER INCOME

Revenue, which is also the Group's turnover, represents the net invoiced value of goods sold and services rendered during the period, net of value-added tax, and after allowances for returns and trade discounts. All significant intra-group transactions have been eliminated on consolidation.

An analysis of revenue and other income is as follows:

	For the six months ended 30 June	
	2006	2005
	(Unaudited)	*(Unaudited)*
	HK$'000	*HK$'000*
Revenue		
Manufacture and sale of wireless telecommunications network enhancement system equipment and provision of related engineering services	**589,490**	413,013
Other income		
Bank interest income	**2,549**	3,208
Others	**1,918**	1,144
	4,467	4,352

4. PROFIT BEFORE TAX

The Group's profit before tax is arrived at after charging/(crediting) the followings:

	For the six months ended 30 June	
	2006	2005
	(Unaudited)	*(Unaudited)*
	HK$'000	*HK$'000*
Cost of inventories sold and services provided	**326,288**	207,266
Depreciation	**16,712**	11,859
Amortisation of prepaid land lease payments	**146**	144
Amortisation of intangible assets	**1,779**	528
Minimum lease payments under operating leases in respect of land and buildings	**15,015**	13,681
Provision for product warranties	**10,414**	4,968
Provision for/(reversal of) doubtful debts	**6,373**	(219)
Provision for obsolete inventories	**7,688**	—
Loss on disposal of items of property, plant and equipment	**—**	292
Staff costs (including directors' emoluments)		
Salaries and wages	**77,334**	72,222
Staff welfare expenses	**10,291**	6,765
Pension scheme contributions	**7,977**	6,865
Equity-settled share option expenses	**8,691**	11,902
Total staff costs	**104,293**	97,754

5. FINANCE COSTS

	For the six months ended 30 June	
	2006	2005
	(Unaudited)	*(Unaudited)*
	HK$'000	*HK$'000*
Interest on bank loans wholly repayable within five years	**5,104**	3,928
Interest on finance leases	**10**	10
Finance costs on the factored trade receivables	**2,754**	5,259
	7,868	9,197

6. TAX

	For the six months ended 30 June	
	2006	2005
	(Unaudited)	*(Unaudited)*
	HK$'000	*HK$'000*
Current period provision — Mainland China	**13,135**	4,534
Deferred tax	**(6,479)**	—
Total tax charge for the period	**6,656**	4,534

No provision for Hong Kong profits tax has been made as the Group did not generate any assessable profits arising in Hong Kong during the period (six months ended 30 June 2005: Nil). Taxes on profits assessable elsewhere have been calculated at the rates of tax prevailing in the countries in which the Group operates, based on existing legislation, interpretations and practices in respect thereof.

Comba Telecom Systems (Guangzhou) Limited ("Comba Guangzhou"), a wholly owned subsidiary of the Company operating in the Mainland China was designated as an advanced technology foreign investment enterprise by the Guangzhou Foreign Trade and Economic Cooperation Bureau in August 2004. Under the current PRC tax legislation, upon expiry of its tax holiday in 2004, a foreign investment enterprise having the status of advanced technology enterprise is entitled to the preferential tax rate at 50% of the applicable standard rate, subject to a minimum rate of 10% for another three years. During the period, provision for PRC corporate income tax for Comba Guangzhou has been made at the applicable reduced tax rate of 10%.

According to Income Tax Law of the PRC for Foreign Investment Enterprises and Foreign Enterprises, Comba Telecom Technology (Guangzhou) Limited ("Comba Technology"), another subsidiary of the Company established in the PRC, was entitled to an exemption from the PRC corporate income tax for the two years commencing from its first profit-making year 1 January 2003 to 31 December 2004 and thereafter was entitled to a 50% reduction in the PRC corporate income tax for the subsequent three years from 1 January 2005 to 31 December 2007.

7. EARNINGS PER SHARE ATTRIBUTABLE TO ORDINARY EQUITY HOLDERS OF THE PARENT

The calculation of basic earnings per share for the period is based on the profit attributable to equity holders of the parent of HK$45,561,000 (six months ended 30 June 2005: HK$35,941,000), and the weighted average number of 834,705,000 (six months ended 30 June 2005: 832,816,000) ordinary shares in the issue during the period.

The calculation of diluted earnings per share is based on the profit attributable to equity holders of the parent of HK$45,561,000 (six months ended 30 June 2005: HK$35,941,000). The weighted average number of ordinary shares used in the calculation is the 834,705,000 (six months ended 30 June 2005: 832,816,000) ordinary shares in issue during the period, as used in the basic earnings per share calculation; and the weighted average of 7,541,000 (six months ended 30 June 2005: 13,444,000) ordinary shares assumed to have been issued at no consideration on the deemed exercise of all share options during the period.

8. DIVIDEND

At a meeting of the Board of Directors held on 8 September 2006, the Directors resolved not to pay any interim dividend to shareholders (six months ended 30 June 2005: Nil).

9. COMPARATIVE AMOUNTS

Certain comparative amounts have been reclassified to conform with the current period's presentation.

MANAGEMENT DISCUSSION AND ANALYSIS

Business and Financial Review

Revenue

The Group's revenue for the six months ended 30 June 2006 (the "Period") was HK$589,490,000, representing an increase of approximately 42.7% from the same period in the previous year (being the six months ended 30 June 2005, the "Prior Year Period"). The Group benefited from continued economic growth and urban and rural development in the PRC, which resulted in increased wireless enhancement capital expenditure. In addition, it recorded remarkable revenue growth in new businesses such as base transceiver station ("BTS") subsystems and antennas, and digital microwave systems ("DMS") in the Period. International market also delivered a robust growth in revenue during the Period.

By customers

Revenue generated from China Mobile Communications Corporation and its subsidiaries (the "China Mobile Group") increased remarkably by 93.7% and accounted for 65.2% of the Group's revenue in the Period. Such strong growth is primarily due to increased wireless enhancement capital expenditure by the China Mobile Group for network optimisation amid strong subscriber growth. The Group's broadened product and solution portfolio also helped generate more revenue. During the Period, revenue generated from the GSM network of China United Telecommunications Corporation and its subsidiaries (the "China Unicom Group") decreased by 22.9% while revenue generated from its CDMA network decreased by 15.6%. Revenue generated from China Unicom Group accounted for 21.9% of the Group's revenue in the Period, with GSM and CDMA accounting for 8.5% and 13.4% respectively.

Revenue from other customers including agents in the PRC and international customers accounted for 12.9% of the Group's revenue in the Period. Among them, export sales (including sales to core equipment manufacturers) nearly tripled and accounted for 7.2% of the Group's revenue in the Period, compared to 3.6% in the Prior Year Period. The Group's international expansion effort has achieved initial success as demonstrated by the strong growth, which is contributed by addition of new customers and repeat orders from existing customers.

By solutions/products

Revenue generated from wireless enhancement (both indoor and outdoor) solutions increased by 35.6% and accounted for 85.0% of the Group's revenue in the Period, compared to 89.4% in the Prior Year Period. Revenue from indoor and outdoor solutions increased by 35.1% and 37.9% respectively and accounted for 69.6% and 15.4% respectively of the Group's revenue in the Period.

Apart from providing turnkey solutions in wireless enhancement to mobile operators, the Group strategically developed two major product areas in BTS subsystems and antennas and DMS. Revenue from BTS subsystems and antennas more than doubled and accounted for 7.6% of the Group's revenue in the Period, compared to 4.7% in the Prior Year Period. Revenue from DMS increased more than eightfold and accounted for 3.4% of the Group's revenue in the Period, compared to 0.5% in the Prior Year Period. Others including extended maintenance services increased by 8.1% and accounted for 4.0% of the Group's revenue in the Period.

Gross profit

The Group is facing continuous pressure on the average selling price and hence gross profit margin of its products and solutions for the maturing 2G mobile communications market in the PRC. In view of this, the Group implemented various measures to mitigate this downward trend. It optimised its product portfolio by focusing on products with higher margin, optimised the product design, and continued to negotiate better pricing in materials. In addition, the Group improved its logistics management, thereby enhancing production efficiency and lowering costs. Gross profit margin was 42.9% in the Period compared to 48.6% in the Prior Year Period. Gross profit of the Group for the Period was HK$252,788,000, representing an increase of 25.9% over the Prior Year Period.

Research and development costs

The Group has increased its resources considerably in the research and development ("R&D") of its products and solutions including those related to 3G. For instance, the Group continued to expand its R&D team in the PRC during the Period. On the other hand, the R&D centre in the West Coast of the US was established in the third quarter of 2005 and so there were no such expenses in the Prior Year Period. R&D costs therefore increased by 53.9% to HK$33,379,000 and accounted for 5.7% of revenue in the Period compared to 5.2% in the Prior Year Period.

Selling and distribution costs

Selling and distribution costs were HK$55,779,000 in the Period, representing an increase of 27.4% over the Prior Year Period. With more focused sales and marketing efforts on markets with high demand and a broader product portfolio supported by an established sales platform, the Group achieved better efficiency in selling and distribution costs which accounted for 9.5% of the Group's revenue in the Period, compared to 10.6% in the Prior Year Period.

Administrative expenses

Administrative expenses were HK$99,598,000 in the Period, representing an increase of 8.9% over the Prior Year Period. This slight increase was primarily a result of the Group's strengthened budgetary control. Economies of scale were therefore achieved amid strong revenue growth in the Period. Administrative expenses accounted for 16.9% of the Group's revenue in the Period, compared to 22.1% in the Prior Year Period.

Finance costs

Finance costs were HK$7,868,000 in the Period, representing a decrease of 14.5% over the Prior Year Period. In view of rising interest rates, the Group managed to reduce the bank borrowing level for working capital purposes during the Period.

Tax

Effective tax rate was 12.9% in the Period, compared to 11.7% in the Prior Year Period.

Net profit

Profit attributable to shareholders ("Net Profit") for the Period was HK$45,561,000, representing an increase of 26.8% over the Prior Year Period. This is largely due to the increase in the Group's revenue in the Period. The decrease in gross profit margin was largely offset by the economies of scale achieved in administrative expenses. Net profit margin was 7.7% in the Period compared to 8.7% in the Prior Year Period.

Prospect

Businesses — solutions/products

Wireless enhancement solutions

The Directors believe that the future development of the Group's 3G operations represents an excellent business opportunity to the Group in the medium term. The Group has continuously invested in R&D to enhance its product portfolio and capabilities for different 3G standards. It participated in various 3G network trials and testing and is well prepared for 3G in all aspects. During the Period, the Group became a member of the TD-SCDMA Industry Alliance which was established to perfect and promote the TD-SCDMA standard.

The Directors also believe that 2G and 3G networks will coexist for a long period of time, operators will still need to invest in the construction of 2G network, given a continuous and strong growth in subscribers and an extension in coverage to rural areas. The international market provides a lot of growth potential because of the continuous investment in wireless infrastructure around the world. The 2G network built in developing countries and the 3G network upgrade in the developed world offer a lot of opportunities for this product area.

Subsystems and antennas

The Group has actively expanded its capabilities on BTS subsystems and antennas. Production capacity for BTS antennas have more than tripled since 2005. The Group's continuous investment in R&D has enabled it to develop a complete product portfolio including smart antennas, multi-band antennas with 3G capabilities, camouflaged antennas and a full range of tower top solutions to address the PRC market as well as the global operators market. The Group has recently been evaluated and has passed the supplier audit process of a leading global mobile operator. These demonstrate the Group's leading technical and operations position in this market segment.

Wireless transmissions — DMS

The Group has now completed the portfolio of Point-to-Point DMS solutions. This is the core product line for the Group's Wireless Transmissions Business Unit and its products have been gaining acceptance by its PRC and international customers. Its products provide a quick and cost effective solution for operators in their high speed data and backhaul services especially in the developing countries like South East Asia, India, Caribbean and Latin America ("CALA") and Africa. In addition, the licensing of 3G services in the PRC is another good growth opportunity for this business unit as there will be a huge demand in BTS backhaul services.

Businesses — markets

The Directors believe the PRC market is offering a lot of opportunities. The 2G network is going to grow continuously as long as there are new subscribers and new capacity growth. Hence 2G and 3G networks are going to coexist. The continuous growth of the PRC economy facilitates demand for the Group's products and solutions in the urban areas while the network extension to rural areas under the "Village-Connected Project" is also driving the demand upwards.

The Group continues to expand its effort on international growth with the establishment of the CALA regional headquarters in Sao Paulo, Brazil. The international operators are also investing in 2G network expansion in the developing countries while 3G network build out in various developed countries allow the Group to generate commercial 3G revenue while waiting for the 3G licensing in the PRC.

The Directors also view the core equipment manufacturer market as an important strategy for expansion. With established R&D and manufacturing capabilities, the Group has developed products catering to the needs of core equipment manufacturers both inside and outside the PRC.

Operations

The Group has focused on expanding its addressable markets by extending its product offerings and geographical coverage. The diversification into the subsystems & antennas and wireless transmissions businesses has created new contribution to the Group's revenue.

In order to facilitate continuous growth of its existing businesses, the Group has implemented a corporate wide resources realignment effort and created three separate business units. The Wireless Enhancement Business Unit focuses on the indoor and outdoor enhancement markets; the Subsystems & Antennas Business Unit provides BTS subsystems and antennas products; and the Wireless Transmissions Business Unit offers DMS and other new transmission products.

The Group has recently relocated the sales and marketing and the R&D departments, among others, to the new headquarters in Guangzhou Science City, Guangzhou, the PRC. The existing plant in the Guangzhou Economic and Technology Development District will mainly be used for production. The increase in production floor space will enable the Group to meet business demand flexibly in the next few years.

Conclusion

The Directors believe that the demand for 2G products in the PRC continues to be strong given the increasing number of mobile subscribers and infrastructure projects as well as the extension of coverage to the rural areas. In addition, the Directors remain cautiously optimistic about the opportunities arising from the future development of the 3G mobile market in the PRC as the Group has been offering 3G products to its global customers.

The international market expansion and the development of BTS subsystems and antennas and DMS products for wireless transmissions are all important diversification strategies to fuel the Group's long term growth. Following the expansion to CALA market, the Group will continue to expand its geographical coverage to serve more customers. The Group has also recently realigned its resources at the headquarters level by forming three separate business units.

The Directors believe that the wireless industry is still at high growth rate and technologies are evolving daily. The Group needs to follow diligently the industry trend and analyse market risks and threats to maintain its leadership position. To cope with the ever changing market needs, the Group will continue to invest in products and technology based research and development. With the opening of the new headquarters in the PRC, the Group provides an inspiring working environment and state of the art equipment for new ideas and products. In addition, the Group has an expanded production platform that allows it to meet the future demand for its products and solutions. Capital expenditure of the Group is expected to be funded by various means of financing. Finally, the Group will endeavour to maintain a solid and healthy financial position and consolidate its leading market position, while pursuing a balanced and carefully planned growth strategy in order to maximize the shareholders' value.

Liquidity, Financial Resources & Capital Structure

The Group generally finances its operations from cashflow generated internally and bank loans. As at 30 June 2006, the Group had net current assets of HK$981,233,000. Current assets comprised inventories of HK$687,792,000, trade receivables of HK$897,461,000, notes receivables of HK$16,534,000, prepayments, deposits and other receivables of HK$125,989,000, short term time deposits of HK$63,000,000 and cash and cash equivalents of HK$180,883,000. Current liabilities comprised trade and bills payables of HK$464,441,000, other payables and accruals of HK$241,287,000, interest-bearing bank loans of HK$252,345,000, current portion of finance lease payables of HK$90,000, tax payable of HK$9,491,000 and provision for product warranties of HK$22,772,000.

The average receivable turnover for the Period was 233 days compared to 230 days for the Prior Year Period. The Group's trading terms with its customers are mainly on credit. The contractual credit period is generally for a period of three to six months except for those retention money receivables with payment ranging from six to twenty-four months. The average payable turnover for the Period was 221 days compared to 249 days for the Prior Year Period. The average inventory turnover for the Period was 339 days compared to 476 days for the Prior Year Period.

As at 30 June 2006, the Group's cash and bank balances were mainly denominated in Renminbi ("RMB"), Hong Kong dollars ("HK$") and United States dollars ("US$") while the Group's bank borrowings were mainly denominated in RMB, HK$ and US$. The interest rates on the Group's bank borrowings are principally on a floating basis at prevailing market rates. The Group's revenue and expenses, assets and liabilities are mainly denominated in RMB, HK$ and US$. Since the exchange fluctuations among these currencies are low, the Directors consider that there is no significant exchange risk.

The Group's gearing ratio, calculated as total interest-bearing debts (including bank loans and advances, and finance lease payables) over total assets, was 11.3% as at 30 June 2006 (31 December 2005: 14%).

Charge on Assets

The Group's bank loans were secured by a charge on a time deposit amounted to HK$63,000,000 (31 December 2005: HK$63,000,000).

Contingent Liabilities

As at 30 June 2006, the Group had no significant contingent liabilities (31 December 2005: Nil).

Employees and Remuneration Policies

As at 30 June 2006, the Group had approximately 3,600 staff. The total staff costs for the Period was HK$104,293,000. The Group offers competitive remuneration schemes to its employees based on industry practices as well as the employees' and the Group's performance. In addition, share options and discretionary bonuses are also granted to eligible staff based on the performance of each such employee as well as the Group. The Group also provides training to staff to improve their skills and develop their respective expertise.

PURCHASE, REDEMPTION OR SALE OF LISTED SECURITIES OF THE COMPANY

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

CODE OF CORPORATE GOVERNANCE PRACTICES

The Company has complied with the code provisions as set out in Appendix 14 to the Listing Rules throughout the Period, except for the deviation from Code Provision A.2.1 which stipulates that the roles of chairman and chief executive officer should be separate and should not be performed by the same individual and that the division of responsibilities between the chairman and chief executive officer should be clearly established and set out in writing. The Company currently has not complied with Code Provision A.2.1 as the Company considers that through the supervision of its Board of Directors, a balancing mechanism exists so that the interests of the shareholders are fairly represented. Nevertheless, the Company will be reviewing its situation regularly and will comply with this code at an appropriate time in the future should it consider appropriate and necessary.

AUDIT COMMITTEE

The unaudited interim results of the Group for the six months ended 30 June 2006 have been reviewed by the audit committee of the Company.

PUBLICATION OF INTERIM REPORT ON THE WEBSITE OF THE STOCK EXCHANGE

A copy of interim report containing all information required by relevant paragraphs of Appendix 16 of the Listing Rules will be published on the Stock Exchange's website (http://www.hkex.com.hk) in due course.

By order of the Board
Fok Tung Ling
Chairman and President

Hong Kong, 8 September 2006

As at the date of this announcement, the Board comprises the following executive Directors: Mr FOK Tung Ling, Mr ZHANG Yue Jun, Mr CHAN Kai Leung, Clement, Mr WU Jiang Cheng, Mr YAN Ji Ci, Mr ZHENG Guo Bao and Mr YEUNG Pui Sang, Simon; and the following independent non-executive Directors: Mr YAO Yan, Mr LAU Siu Ki, Kevin and Mr LIU Cai.

Please also refer to the published version of this announcement in ***The Standard.***