
4. RISK FACTORS

Applicants for the Public Issue Shares/Offer Shares should carefully consider the following factors, which may not be exhaustive and which may have an impact on the future performance of the Group, in addition to the other information contained elsewhere in this Prospectus, before applying for the Public Issue Shares/Offer Shares.

4.1 NO PRIOR MARKET FOR COMCORP SHARES

Prior to this IPO, there was no public market for Comcorp Shares. There can be no assurance that an active market for Comcorp Shares will develop upon its listing on the Second Board of Bursa Securities or that such market, if developed, will be sustained. The issue/offer price of RM0.85 for the Public Issue Shares/Offer Shares has been determined after taking into consideration a number of factors, including but not limited to, the Group's operating and financial history and conditions, the prospects of the industries in which the Comcorp Group operates, the management of Comcorp and the prevailing market conditions prior to the issue of this Prospectus. The price at which Comcorp Shares will trade on the Second Board of Bursa Securities after the Listing may be influenced by a number of factors including, amongst others, the depth and liquidity of the market for Comcorp Shares and investors' perceptions of the Comcorp Group. There can be no assurance that the issue/offer price of the Public Issue Shares/Offer Shares will correspond to the price at which the Shares will trade on the Second Board of Bursa Securities upon or subsequent to the Listing.

4.2 BUSINESS RISKS

The Comcorp Group is subject to certain risks inherent in the ICT, EMS and public safety industries. These include, but are not limited to, labour and supply shortages, competition, demand for its services and products, equipment and software obsolescence, changes in general economic, business and credit conditions, entry of new competitors, foreign exchange rate fluctuations, introduction of new technology, services and products and changes in industry and government policies.

Although the Group seeks to limit these risks through, inter-alia, development of new services and products, monitoring and enhancement or the use of the latest technology available, investing in R&D, diversifying its pool of suppliers and customers and expansion of both existing and new markets to countries such as China and Republic of Korea, there can be no assurance that any change in the above risk factors will not have a material adverse effect on the Group's business.

4.3 DEPENDENCE ON CUSTOMERS**4.3.1 Absence of Long-Term Contractual Agreements with Customers**

Due to the nature of the ICT, EMS and public safety industries, there are no long-term contractual agreements between the Comcorp Group and its customers as contracts are secured on a project basis. The period of its current contracts-in-hand, which include overseas contracts, is between one (1) year to three (3) years. The lack of long-term contractual agreements may affect the sustainability of the profits of the Comcorp Group.

The Group seeks to limit this risk by, amongst others, providing quality services and products to its clientele, applying relatively high level of technology specifications and know-how, which have earned the Group recognition and confidence from its customers, ensuring strict compliance with agreed customers' delivery/completion schedules and nurturing strong relationships with its existing customers via the provision of product enhancement and related after-sales service to its customers. Further, the Comcorp Group also employs various strategies to broaden its clientele base by venturing into new markets such as China and Republic of Korea, to bid for new projects.

4. RISK FACTORS (CONT'D)

The successful implementation of the above measures has enabled the Group to enjoy long and cordial working relationships with its major customers, the details of which are set out in Sections 4.3.2 and 6.4.10 of this Prospectus. Further, the numerous awards received by the Group from its customers (the details of which are set out in Section 6.4.16 of this Prospectus) as well as the securing of contracts with new customers by the Group, attest to the ability of the Group in maintaining as well as expanding its existing customer base.

Notwithstanding the above, there can be no assurance that with the above measures, the Group will be able to retain or expand its customer base or that it will be able to continue to procure projects from these customers.

4.3.2 Dependence on Key Customers

Due to the nature of the industry mix in which the Group operates, namely ICT, EMS and public safety, the Comcorp Group has a limited number of customers, ranging from local to overseas customers. The few key customers which the Group is dependent upon are Motorola Inc, Power-One, Kementerian Dalam Negeri and Kementerian Pertahanan. The contributions of these customers to the proforma revenue of the Comcorp Group are as follows:

Customers	Country	Revenue contributions in percentage (%) of total proforma revenue of the Comcorp Group for the financial year ← ended 31 January →		
		2002	2003	2004
Motorola Inc	USA	68	58	41
Power-One	USA	5	18	26
Kementerian Dalam Negeri*	Malaysia	12	8	20
Kementerian Pertahanan*	Malaysia	3	5	3

Note:

* The key customers of the Comintel Group are Kementerian Dalam Negeri and Kementerian Pertahanan. The Comintel Group is currently the main contributor to the profits of the Comcorp Group and is expected to remain so in the immediate future.

Amongst the business risks that the Group faces due to its reliance on a few key customers are the termination of business relationships, cessation of certain product lines by the customers, etc, which may result in the Group losing a substantial portion of its business and in turn, have an adverse effect on the operating and financial performance of the Group.

As explained in Section 4.3.1 above, the Group has developed long and healthy business relationships with a number of these key customers as set out below:

	Period of relationship (Approximately in years)
Kementerian Dalam Negeri	19
Motorola Inc	17
Kementerian Pertahanan	16
Power-One	3

4. RISK FACTORS (CONT'D)

The Group has strong working relationships with the above customers who are committed to mutual business support, as evidenced by the continued bi-lateral working relationships throughout the years. The Company is of the view that the probability of termination of business relationships by the Group's key customers is low due to the Group's focus on the niche market of defence and public safety communication.

The provision of the Group's ICT services are mainly to Kementerian Dalam Negeri and Kementerian Pertahanan, both of whom the Comcorp Group via the Comintel Group has served for over 19 years and 16 years respectively. This is made possible with the ability of the Group to understand and cater to the needs of its customers with high technology specifications. In addition, with the Group's high degree of technical understanding of the technology to be used and the ability to structure effective and efficient solutions for its customers, customers are assured of the quality of the Group's products and services provided. In this regard, the Group also has the flexibility of choosing to work with a number of technology providers, who have long working relationships with the Group, to provide its customers with the optimal solution to cater to their needs. In addition, the Group believes that it has established relationships with its customers via its long dealings with them.

The EMS business of the Group is focused on the niche market of high-mix with low-to-moderate volume products. The ability of the Group to operate efficiently in such a niche business as well as the reliance of customers on a limited number of suppliers, such as the Comcorp Group, further contribute to the long-term working relationships between the Comcorp Group and its key customers. The appointment of new vendors would involve high switching costs as well as a long gestation period of acceptance as there are currently no other vendors in Malaysia who are focused on the same industry mix as the Group. This is due to the lengthy period taken to carry out system specification studies, operational and quality audits on the products and systems developed by new vendors. In addition, the lead time for any required enhancements or expansions to the products produced or systems developed for the Group's existing customers is relatively fast as compared to the lead time taken should a new vendor be appointed. Moreover, the Group believes that with its long and established dealings with some of its key customers hereunder and its ability to continue to meet their stringent requirements, its key customers will continue to work with the Group.

Consequently, the Comcorp Group is confident that it will be able to retain its existing customer base as well as expand on it in the longer term.

4.4 TECHNOLOGICAL OBSOLESCENCE RISK

The Comcorp Group is subjected to inherent risks associated with the rapid development of technology. The Group's products and services are characterised by rapid technological developments, constantly evolving industry standards, swift changes in customer requirements, new product introductions and enhancements. If the Group is unable to offer technologically advanced products, solutions or manufacturing services that are cost-effective to customers, demand for the Group's services may decline.

The Group seeks to minimise these risks by actively and continuously pursuing technological innovation and advancement through R&D, adopting industry best practices and forming strategic business alliances with key technology providers to address the increasingly sophisticated needs of its customers. The Group also provides continuous staff development to align their skills and knowledge to keep abreast with the latest technology.

Although the Group has put in efforts to mitigate these risks, there is no assurance that the Group will be successful in developing and marketing new products and services or making enhancements to its existing products and services to keep up with the increasingly sophisticated technological requirements of its customers.

4. RISK FACTORS (CONT'D)

4.5 POLITICAL, ECONOMIC AND LEGISLATIVE CONSIDERATIONS

As with any other businesses, the performance of the Comcorp Group is susceptible to political, economic and legislative conditions, both locally and internationally. The impact of changes to the general political and economic environment as well as changes to legislative considerations in the domestic as well as international scene may have adverse or unfavourable effects on the Comcorp Group, depending on circumstances. These include, but are not limited to, the risks of war, terrorism, riots, expropriation, nationalisation, renegotiations or nullification of existing contracts, currency exchange controls, changes in interest rates and methods of taxation.

4.6 AVAILABILITY AND COSTS OF EQUIPMENT, COMPONENTS AND RAW MATERIALS

In the provision of ICT services, the Group will be required to purchase components and equipment from its key technology suppliers. Such purchases will be made once the terms of the contract have been determined vis-a-vis the details of the solutions or services offered by the Group. The Group seeks to fix the price and cost of these purchases at the time the contract is awarded to ensure that fluctuations in costs are minimised.

The main materials used in the EMS business of the Group include components such as PCBs, ICs, capacitors and resistors. While the Group is not dependent on any single supplier, any serious and prolonged shortage of such components may lead to loss of business opportunities which may adversely affect the Group's profits as well as possibly inhibit the expansion of the Group's business. Further, the cost of raw materials used are dependent on their prevailing demand and supply conditions which are in turn, dependent on the availability of projects. As the Group offers to undertake the purchasing of components used in its customers' products, resulting in an unavoidable time lag between the Group's commitment to its customers on the price for such components and the Group's subsequent purchase on its customers' behalf, the Group may be exposed to fluctuations in the cost of the raw materials. The Group seeks to minimise its exposure to shortages of components and price fluctuations through the purchase of such components and raw materials from long-term suppliers recommended by its customers as well as sourcing its supplies from other suppliers on a competitive basis. Generally, the customers of the Group have accommodated price increases with respect to raw materials, equipment and components in the provision of its EMS business.

Notwithstanding the above, there can be no assurance that the Group will be able to continue to minimise its exposure to shortages and cost fluctuations and/or transfer any cost revision of the equipment, components and raw materials used in the provision of its services to its customers and that any unfavourable price fluctuations or shortages may not materially and adversely affect the Group's performance and operations.

4.7 REGULATORY FRAMEWORK

The Comcorp Group's operations are subject to regulations imposed by several government ministries and agencies, such as PUKONSA for the supply of telecommunication equipment in Sabah, the Ministry of Finance for contractor licences, and MITI, MIDA and the Royal Customs and Excise Malaysia for the Group's manufacturing activities. The Comcorp Group has always worked to ensure that it complies with the rules and regulations of the legal framework in which the Group operates. Notwithstanding the above, no assurance can be given that any changes to the present regulatory framework in which the Group operates will not have any material adverse impact on the Group's businesses.

4. RISK FACTORS (CONT'D)

4.8 COMPETITION

In general, the ICT and EMS industries have relatively low barriers to entry. However, in a more niche market segment involving the provision of systems engineering, integration services and solutions, and the manufacture of high-mix and low-to-moderate volume RF products for the defence and public safety communication sector in which the Group operates, potential entrants are faced with higher barriers to entry as they are required to meet stringent and complex requirements as well as the quality standards set by customers.

Notwithstanding the above, the Comcorp Group may face competition from competitors who may expand their business to emulate the same range of products and services, and from new players entering into the same industries as the Group.

In the provision of ICT services, the Comcorp Group has enjoyed close working relationships with a number of its major customers, which it had consistently provided quality services and solutions in meeting their requirements. Further, certain of its major customers have been dealing with the Comcorp Group for between sixteen (16) to nineteen (19) years. The Comcorp Group believes that its innovative abilities and strong technical understanding of the technology used, as well as the ability to work with a number of key technology providers, allow it to provide the most effective and optimal solution to its clients. The Comcorp Group also continues to monitor the latest developments in technology as a means to further enhance its provision of related services and solutions.

On the other hand, in relation to the EMS business, unlike most of its competitors, the Group has developed itself into a one-stop centre providing a range of services from design to manufacturing. The Group believes that its principal competitive advantages are its integrated synergistic operations, an experienced management team, prompt completion and delivery of customers' orders, consistent quality, and innovative designs. The EMS business is also able to take advantage of the technology know-how of the ICT business to design and structure tests and analysis for QC as well as to improve on product designs. In addition, the Comcorp Group has, through its subsidiary BCM, established itself as an EMS provider in the industry and has successfully built up a strong foundation and working relationship with its customers.

To remain competitive, the Comcorp Group has in place several strategic measures, including carrying out R&D activities to provide new solutions and enhancing existing products as well as introducing cost management measures. It also constantly monitors and assesses the actions of its competitors and where applicable, takes the necessary steps to address the effects of their actions. The Comcorp Group is always looking at ways to constantly improve its production processes in order to increase production efficiency and to ensure the continuous offering of consistent quality, promptness in delivery and competitive pricing of its products and services.

Notwithstanding the above, there can be no assurance that the Group will not be affected by the competitive strategies adopted by other players within the same industries in which the Group operates, and that the Group will be able to maintain or expand its existing market share in the future.

4.9 DEPENDENCE ON KEY PERSONNEL

The Comcorp Group believes that its continued success will depend, to a significant extent, upon the abilities and continued efforts of its existing Directors and senior management. The loss of any key member of the Board or senior management could adversely affect the Group's ability to compete effectively in both the ICT and EMS industries.

The Directors of the Comcorp Group recognise the importance of the Group's need to retain skilled personnel and have in place a management succession plan (the details of which are set out in Section 6.4.15 of this Prospectus) to provide incentives for its staff to improve their performance and productivity, and to ensure a smooth transition in the event of any change in staff.

4. RISK FACTORS (CONT'D)

Notwithstanding the above, there can be no assurance that the above measures will always be successful in retaining key personnel or in ensuring a smooth transition, should changes occur.

4.10 SHORTAGE OF HUMAN CAPITAL

The ICT industry is dependent on a broad range of human capital including hardware specialists, ICT infrastructure specialists, software specialists/programmers, networking specialists and others. Due to the growth in the ICT industry and the broad range of human capital required, the availability of suitable personnel is crucial to the operations of the players in the industry. Similarly, although the EMS industry is semi-automated, semi-skilled operators are required to operate the production lines. Hence, a stable work force is crucial to ensure that the operations of the EMS providers are not interrupted, particularly in periods of high demand.

In this regard, the Group strives to ensure that its staff force is motivated and the staff turnover rate is maintained at a manageable level. The management of the Group also ensures that existing management succession plans of the Group are maintained. These efforts aim to maintain continuity in management in the long-term and to ensure the operations of the Group are not unnecessarily interrupted. To achieve this, the Group ensures that its remuneration packages are competitive and incentives are provided to its staff force to motivate them. The Group also ensures that conscious efforts are made to retain and develop potential management staff.

In addition to the above, to ensure that the quality of the Group's services and products are maintained at high levels to meet its customers' requirements, training and development programmes, both on-the-job and classroom based, are made available to its staff force and are aimed at enhancing technical and managerial skills. Further, to provide flexibility to the Group's staff utilisation and to mitigate the effects of staff shortages, the Group ensures that its staff force is trained to handle various different tasks. This is particularly important for its EMS operations.

Notwithstanding the above, despite the above efforts made by the Group, there is no assurance that the Group will avoid situations of shortages in staff force which may affect its operations and performance.

4.11 EXCHANGE RATE RISK

The transactions of the Comcorp Group are mainly denominated in RM and USD. For the financial year ended 30 September 2003, approximately 82% of the revenue derived from its EMS business were billed in USD, whilst approximately 80% of its purchases of raw materials and components were denominated in USD. The remaining balance of the revenue and purchases of the Group's EMS business were mainly denominated in RM. On the other hand, for the financial year ended 31 January 2004, the contracts of the ICT business of the Comintel Group were mainly billed in RM, whilst approximately 50% to 60% of contract costs relating to the purchase of equipment and components were transacted in USD, with the balance mainly transacted in RM.

At present, the Comcorp Group does not hedge its foreign denominated transactions, as a significant portion of its EMS business is naturally hedged. In addition, the current pegging of the RM against the USD, to a certain extent, eliminates the risk of the foreign exchange fluctuations between the USD and RM. For the same reason, the Group does not hedge its exposure to foreign denominated transactions of the ICT business. Notwithstanding the above, the management will hedge against any foreign exchange exposure which may arise, if deemed necessary.

4. RISK FACTORS (CONT'D)

Although the Group is of the view that its exposure to foreign exchange fluctuations is largely mitigated, there can be no assurance that the Group will not be exposed to any foreign exchange fluctuations arising from its future transactions due to the upliftment or adjustments to the RM-USD peg or the change in the terms or denomination of its future contracts.

4.12 OPERATIONAL RISKS

The Group faces certain operational risks, including but not limited to fire outbreaks and disruptions to electricity supply, which would affect its business operations.

To mitigate the risks of fire outbreaks, the Group has taken precautionary steps through the installation of fire resistant walls, fire hydrants, fire extinguishers and sprinkler systems at its office and factory premises. A safety committee which comprises senior management and operational staff of the Group, is entrusted with the duty of evaluating and performing safety and security checks on the factory as well as to ensure that the security policies and control systems are strictly adhered to at all times. Factory employees are also trained on the use of fire fighting equipment as well as basic fire fighting techniques. Fire drills are conducted at regular intervals to ensure that employees are well prepared in the event a fire outbreak occurs.

In addition, the Group's production process undertaken by BCM is highly automated and is therefore dependent on a consistent supply of electricity for its smooth operations. The power supply to BCM's factory premises is provided by Tenaga Nasional Berhad ("TNB") and an independent power producer ("IPP") namely Northern Utility Resources Sdn Bhd. As such, in the event of a disruption to the power supply from either TNB or the IPP, the necessary backup power supply will be provided by the other.

However, no assurance can be given that, even with the existing risk management plan in place, the business operations of the Group will not be affected in the event such operational risk factors do occur.

4.13 CONTROL BY SUBSTANTIAL SHAREHOLDERS

Upon the Listing, the substantial shareholders of Comcorp, namely JTSB, Sagittarius, AMG, Leng Keng Hok @ Lim Keng Hock, Dato' Seri Ahmad Ramli bin Haji Mohd Nor, Mohamadon bin Abdullah and Lee Choon Bin will collectively own, directly and indirectly, approximately 67% of the Company's enlarged issued and paid-up share capital. As a result, they, if acting jointly, are likely to be able to influence the outcome of certain matters requiring the vote of the Company's shareholders, unless they are required to abstain from voting by law and/or the relevant authorities.

In addition, the management of the Comcorp Group will be under the direction of Leng Keng Hok @ Lim Keng Hock, the Managing Director of Comcorp; Lee Choon Bin, the Executive Director of Comcorp; Mohamadon bin Abdullah, the Non-Executive Director of Comcorp; and Dato' Seri Ahmad Ramli bin Haji Mohd Nor, the Non-Executive Deputy Chairman of Comcorp. Further, Leng Keng Hok @ Lim Keng Hock and Lee Choon Bin are husband and wife.

Notwithstanding the above, the structure of the Group is such that members of the Board and management have their own independent functions but overall decisions are made on a collective basis. There are also control procedures in place to ensure business decisions and outcomes are made on a rational and independent basis and not through undue influence. Such procedures include, amongst others, the requirement for the Independent Directors and the Audit Committee, formed in accordance with the provisions of the Listing Requirements of Bursa Securities, to ensure transactions involving parties related to the Group are entered into on commercially acceptable terms that are fair to the Group. Further, where a situation of conflict of interest is present, the affected party shall abstain from voting on the subject matter.

4. RISK FACTORS (CONT'D)

4.14 PROFIT FORECAST

The profit forecast set out in Sections 11.3 and 11.4 of this Prospectus has been prepared based on assumptions which the Directors of Comcorp believe to be reasonable. However, these assumptions are subject to uncertainties and contingencies. Due to the inherent uncertainties underlying the profit forecast and given that events and circumstances do not occur as expected, there can be no assurance that the profit forecast contained herein will be achieved and actual results may be materially different from the forecast. Investors are deemed to have read and understood the assumptions and uncertainties underlying the profit forecast contained herein.

4.15 BORROWINGS

As at 25 June 2004, the Group's total long-term and short-term borrowings amounted to RM15.085 million and RM65.466 million respectively, of which RM73.736 million is subject to variable interest rates. As such, any increase in interest rates will increase the burden of the Group with respect to interest payments on the loans depending on the total outstanding loans as at that point in time. Further details of the Group's total borrowings as at 25 June 2004 are set out in Section 11.2.2. The Group plans to utilise RM8.0 million of the proceeds raised from the Public Issue towards the repayment of part of its borrowings, and this is expected to contribute to the reduction in the interest expense of the Group. Notwithstanding the above, there can be no assurance that the performance of the Group will remain favourable in the event of adverse changes in interest rates.

4.16 INSURANCE COVERAGE

The management of the Group is aware of the adverse consequences arising from inadequate insurance coverage that could affect the Group's business operations. In ensuring that such risks are kept to a minimum, the management of the Group reviews and endeavours to obtain adequate insurance coverage for its assets on a continuous basis. Further details of the Group's insurance policies are set out in Section 16.9(xxii) of this Prospectus. However, there can be no assurance that the insurance coverage would be comprehensive and adequate and would reflect the replacement cost of the assets or any consequential loss arising therefrom. Such an inadequacy may adversely affect the financial performance and position, and business prospects of the Group.

4.17 FAILURE/DELAY IN THE LISTING EXERCISE

The listing exercise is also exposed to the risk that it may fail or be delayed should the following events occur:

- (i) the identified investors fail to subscribe to the portion of the Public Issue Shares and/or Offer Shares allocated to them pursuant to Sections 3.5.1(ii) and 3.5.2 of this Prospectus respectively;
- (ii) the Underwriters exercising their rights to terminate the underwriting arrangement pursuant to the terms of the underwriting agreement, thereby discharging themselves from their obligations thereunder. The salient terms of the underwriting agreement are set out in Section 3.10 of this Prospectus;
- (iii) the Company and/or the Underwriters fail to honour their obligations under the underwriting agreement; or
- (iv) the Company is unable to meet the public spread requirement i.e. at least 25% of the issued and paid-up share capital of the Company must be held by a minimum number of 1,000 public shareholders holding not less than 100 shares each upon the completion of the IPO and at the point of listing.

4. RISK FACTORS (CONT'D)

Although the Directors of Comcorp and the Offeror will endeavour to ensure compliance by Comcorp of the listing requirements by the various authorities, no assurance can be given that the abovementioned factors will not cause a delay in or failure of the listing exercise. In the event of failure of the listing exercise, any proceeds so received for the application of the Comcorp Shares shall be refunded to the applicants without interest at their own risk.

4.18 FORWARD-LOOKING STATEMENTS

Certain statements in this Prospectus are based on historical data which may not be reflective of future results, and others are forward-looking in nature which are subject to uncertainties and contingencies.

All forward-looking statements are based on estimates and assumptions made by the Directors of the Company, and although believed to be reasonable by the Directors, are subject to known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements to differ materially from future results, performance or achievements expressed or implied in such forward-looking statements.

Such factors include, inter-alia, general economic and business conditions, competition, the impact of new laws and regulations affecting the Group and the industries in which the Group operates and changes in interest rates and foreign exchange rates. In light of the above factors and other uncertainties, there is no assurance that forward-looking statements in this Prospectus will eventually materialise in the manner which such statements may have been expressed or implied.

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5. INDUSTRY OVERVIEW

5.1 OVERVIEW OF THE MALAYSIAN ECONOMY

Economic expansion strengthened further, with growth in real gross domestic product ("GDP") rising at the pace of 7.6% in the first quarter of 2004 from 6.6% in the fourth quarter of 2003. Growth was broad-based across all sectors. The key contributor to the strong GDP performance was the strengthening in growth of the manufacturing and services sectors. Growth in the manufacturing sector strengthened to 12.5%, contributing 3.8 percentage points to GDP. The expansion was supported by stronger growth in export-oriented industries and sustained growth in domestic-oriented industries. The growth reflected stronger external demand, in particular for electronics, and the improving domestic demand and continued recovery in the investment cycle.

(Source: Economic and Financial Developments in the Malaysian Economy in the First Quarter of 2004 - Bank Negara Malaysia)

5.2 OVERVIEW OF THE ICT, EMS, AND DEFENCE AND PUBLIC SAFETY INDUSTRIES

The Comcorp Group operates in the ICT industry through the Comintel Group mainly in the area of systems integration, with a focus on defence and public safety communication. Through BCM, it is also involved in the EMS industry, which is a sub-sector or supporting industry of the E&E manufacturing industry. The following sections provide an overview of each of the ICT, EMS and public safety industries.

5.2.1 ICT Industry

Malaysia is one of the ASEAN countries that is experiencing positive growth in terms of both its economy and the ICT industry. The growth of the ICT industry can be measured in terms of personal computer and internet penetration rates. The Malaysian Communications and Multimedia Commission's industry statistics put the total number of internet subscribers at 3.15 million, with 9.4 million internet users as at Quarter 1 of 2004. Additionally, the growth rate of internet subscribers in 2003 as compared with 2002 was 10.8%. The number of personal computers installed increased from 610,000 in 1995 to 4.2 million in 2003.

The Networked Readiness Index ("NRI"), which is defined as a nation's or community's degree of preparation to participate in and benefit from ICT developments, ranks Malaysia at 26th amongst 102 countries. The NRI captures key factors relating to the environment, the readiness and the usage of the three (3) stakeholders in the Networked Readiness Framework (individuals, businesses, and government). This index can be used to understand the performance of a nation or a region with regards to ICT readiness and usage and is useful as a relative indicator of a nation's ICT excellence. It is expected that the spending on ICT software and services would rise to 63.9% as a percentage of total IT expenditure worldwide by 2005, based on an annual growth rate of 12.1%. The demand for ICT products and services has generated a global market that reached nearly USD1 trillion in 2001 and is projected to surpass the USD1.4 trillion mark by 2005. Statistics show that the ICT industry in Malaysia has grown and is on an upward trend.

5. INDUSTRY OVERVIEW (CONT'D)

During the period of the 7th Malaysia Plan (1996 to 2000) as well as in the 8th Malaysia Plan period (2001 to 2005), the Malaysian Government set forth several growth initiatives in relation to the ICT industry. A summary of these initiatives which assisted in the exponential growth experienced by the industry is as follows:

- (i) Ensure the widespread application of ICT within and across sectors to stimulate productivity and competitiveness as well as improving quality of life;
- (ii) Increase awareness in ICT among the population with the implementation of the MSC, as well as the continuing provision of new and/or the upgrading of the present telecommunication infrastructure;
- (iii) The expansion of ICT education and training in line with the anticipated demand for ICT related skills, knowledge and expertise;
- (iv) The review of legislation that might impede the development of ICT;
- (v) The promotion and development of the ICT industry, in terms of design and production of innovative products, systems and services. To generate new growth opportunities as well as skills and employment in high-tech areas and developing Malaysia into an ICT hub with international ICT companies operating in Malaysia; and
- (vi) Expand ICT infrastructure, particularly to the rural areas to bridge the digital divide and enable all citizens to have equitable access to knowledge and information.

For the remaining 8th Malaysia Plan period of 2004 to 2005, the government had set aside RM2.5 billion in terms of development expenditure for ICT-related programmes, where the focus will be on the computerisation of schools and government agencies.

The entire ICT industry is still very much in the developmental stage, with new technologies being introduced almost every 3 to 6 months, globally. Within Malaysia, newer technologies take a longer time to catch on due to availability of equipment, infrastructure and human resources.

As such, there is still a largely untapped market in the country for many of the ICT-related products and services. The development of the industry is also dependent on the speed in which Malaysians are able to embrace technology and utilise ICT in their daily activities. The demand for ICT products and services are not subject to any seasonal fluctuations, but however thrive on stable political conditions and a prosperous economy for accelerated growth.

By the end of 2005, over 2 billion people will be connected by networked systems. This will create a huge demand for the introduction of new technologies and innovative ICT products and services.

ICT, in particular the telecommunication market in Malaysia, has developed over the years at a rate much higher than the world's rate. The government has placed emphasis on the growth of ICT as the competitiveness of any corporation is driven by its information resources and the skills and competence of its managers and staff in using and exploiting these resources.

5. INDUSTRY OVERVIEW (CONT'D)

The 8th Malaysia Plan will focus on further strengthening the human resource capabilities in the ICT industry as well as building a critical mass of small-medium enterprises and internet users to enable Malaysia to transform itself into a developed nation with a knowledge-based society. During the years from 2001 to 2005, a total of RM5.2 billion will be allocated for ICT-related programmes and projects, with 35.4% used to rollout MSC flagship applications.

In addition, the Deputy Finance Minister on 9 September 2002, launched a Knowledge-based Economy Masterplan. This plan outlines 7 strategic thrusts that would drive the transformation of the country's economy from a largely production-based economy to a knowledge-based economy. The plan contains 136 recommendations for the development of human resources, institutional frameworks, info-structure and infrastructure, science and technology capacity, role of the public sector, a knowledge-based civil service, as well as efforts to bridge the knowledge and digital divides.

The Energy, Communications and Multimedia Ministry and the Association of the Computer and Multimedia Industry of Malaysia (PIKOM) have also announced a third package for the PC Gemilang programme, which seeks to make available affordable personal computers to the Malaysian public. Among its primary objectives are to increase the number of personal computer and Internet users in the country, particularly in rural areas and lower-income groups.

Further, the second phase of the MSC, to take the project nationwide and create more knowledge workers, was launched by the former Malaysian Prime Minister, Tun Dr Mahathir Mohamad on 5 September 2003. It will involve expanding the MSC to other cyber cities in the country, and later, various parts of the world. The move will see an increase in the number of Malaysians working in high-skilled jobs with better pay. By training the people and creating opportunities for them to work in higher paid jobs, the MSC will then contribute towards the progress of the country and make it a developed nation. The second phase, which is to last until 2010, will also involve the participation of 250 world-class companies in the MSC, the setting of global standards in the MSC's Flagship Applications, and the development of a harmonized global framework of cyber laws. The Government is also considering extending the incentives currently enjoyed by MSC-status companies to other cyber cities in Malaysia. The rules governing the involvement of public university researchers in R&D initiatives with the private sector would have to be relaxed in order to encourage greater university-industry collaboration.

(Source: Independent Market Research Report by ACN dated 21 November 2003 and the Executive Summary Report by ACN dated 20 July 2004)

5.2.2 EMS Industry

EMS providers have become critical to the success of technology OEMs by acting as expert manufacturing partners to OEMs (such as Cisco Systems, Inc, Motorola and Nortel Networks) and adding value through management of customers' supply chains.

The concept of EMS providers as a source of end-to-end solutions developed in the early 1990s. During the 1990-91 recession, OEMs sought to slash operating costs and turned to outside manufacturing as a logical answer. The industry's momentum increased as OEMs became comfortable outsourcing manufacturing, which allowed them to re-focus resources from in-house manufacturing to their core competencies of R&D and product marketing. While the bulk of outsourcing still consists of PCB and print wiring board assembly, other value-added services include global supply chain management, design-for-manufacturing, quick-turn prototyping, system enclosure manufacturing, sub-system and full system assembly, and logistics management.

5. INDUSTRY OVERVIEW (CONT'D)

Established OEMs face pressure from smaller, nimble competitors and need to focus the R&D process on quick time-to-market. Partnering with an EMS provider gives these companies access to state-of-the-art manufacturing equipment, an expert partner to plan the manufacturing process during the R&D phase and produce prototypes, and the ability to scale rapidly into mass production. EMS providers are often closely involved in customers' R&D processes and the larger EMS companies employ hundreds of in-house engineers. During the production phase, the EMS partner handles inventory procurement, and is often able to obtain better pricing and better access to components than OEMs due to their volume purchases for multiple customers.

EMS providers often minimise inventory risk by requiring a "take or pay" arrangement with customers in that the customers may cancel the order, but they would have to pay for the raw materials. EMS providers are expert manufacturing forecasters and can scale headcount to meet a particular OEM programme need and rotate new programmes into their facilities as older ones wind down.

Another challenge for OEMs is the increasingly global environment, which requires them to maintain physical locations near customers and respond quickly to region or country-specific equipment demands. EMS providers help with this process by maintaining manufacturing presence worldwide and aiding with global distribution. Financial considerations are another challenge for OEMs. By outsourcing manufacturing, OEMs are able to reduce working capital needs and capital expenditures, thereby strengthening the balance sheet. Also, given the efficiencies of using an expert manufacturing partner (and not expensing as much depreciation on physical assets), OEMs often have a lower cost of goods for outsourced products, giving them greater pricing flexibility in the marketplace.

Asian-based EMS providers have been instrumental in providing contract manufacturing services to many of their MNC customers in the USA which include value-added services such as component procurement, concurrent engineering, product design, production of sub-assemblies, product assembly, testing and distribution.

MIDA Chairman, Tan Sri Zainal Abidin Sulong recently said that domestic investment in the electronics industry has also increased from 15.2% (RM1.03 billion) in 1999 to 26.3% (RM1.3 billion) in 2003. He added that many MNCs were increasingly outsourcing their manufacturing activities to EMS companies. The global EMS market in 2003 was about RM342 billion and is expected to increase to RM547.2 billion by 2007. The EMS industry in the Asia Pacific region is forecast to grow at 20% per annum and the presence of many EMS companies here will surely see the growth in the electronic industry. This will in turn increase opportunities for the local supporting industries.

In Malaysia, the growth potential for EMS providers can be approximated by growth in the E&E manufacturing sector. The unfilled orders of electronic products and communication devices in the USA have also risen steadily since early 2003. Growth in the electronics industry would be driven mainly by the wireless and personal computer market, due to rising demand for wireless application as well as the personal computer replacement cycle, as companies invest again following their huge spending prior to the Y2K period. This would be further augmented by the growth in the consumer electronics products segment as demand for new technology and multi-functional devices such as camera phones, personal digital assistants and DVDs gain momentum.

5. INDUSTRY OVERVIEW (CONT'D)

With MNCs progressively outsourcing more and more of the manufacturing of their products, the role of EMS providers is growing in importance and they are increasingly a strategic long-term option for the MNCs. As such, it is believed that the EMS industry should continue to experience rapid growth. By outsourcing production to EMS providers, MNCs can focus on their core competencies, such as R&D and product innovation, and achieve greater flexibility in capacity and faster product time to market. This tends to lower production costs, optimise working capital utilisation, and instantly increases production capacities for the MNCs who are then able to properly allocate resources for their key competencies. As such, it is believed that MNCs are increasingly considering EMS providers to be their strategic partners in sharpening their competitive edge and those leading the trend in outsourcing among MNCs presently are the communications and medical equipment/instrumentation sectors, which should have a higher than average trend towards outsourcing over the next few years.

(Source: Independent Market Research Report by ACN dated 21 November 2003 and Executive Summary Report dated 20 July 2004)

5.2.3 Defence and Public Safety Industries

With respect to the defence industry, the Government sector is generally the key market and spending in relation to this industry is largely driven by the public sector budget.

The public safety industry encompasses both private and internal safety and security. The private security industry has moved forward rapidly from the mere use of a watchman, to a competitive one supplemented largely by advanced technological equipment. Security equipment has by and large become an integral part of the business environment where security aspects are necessary to ensure protection and safety of individuals and assets. Since the terrorist attack in the USA on 11 September 2001, large multinational organisations and public access places have increased their security requirements, especially in detection of unsolicited goods and monitoring/surveillance systems.

Internal security mainly relates to the activities of the police department, which has over 80,000 uniformed personnel in the country. As crime and the threat of terrorist activity increases, police are increasing their efforts to address the situation. The table below provides an indication of the crime trends in Malaysia, the numbers of which are providing an impetus to the internal security agencies to invest further in public safety communication equipment in an effort to provide better monitoring and surveillance activities.

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5. INDUSTRY OVERVIEW (CONT'D)**Malaysia : Crime Statistics for 1999 to 2004 (as at February 2004)**

	1999	2000	2001	2002	2003	2004
Violent Crimes						
Murder	588	551	608	516	565	102
Attempted Murder	52	43	68	64	77	22
Armed Gang Robbery	74	89	65	73	45	7
Unarmed Gang Robbery	1,482	1,681	1,697	1,704	1,920	307
Armed Robbery	700	722	566	425	381	62
Unarmed robbery	11,494	12,204	11,333	12,203	13,963	2,179
Rape	1,457	1,210	1,354	1,418	1,471	307
Bodily Harm	5,310	5,104	4,699	4,440	4,368	685
Total	21,157	21,604	20,390	20,843	22,790	3,671
Property Related Crimes						
Housebreaking and Theft (Daytime)	9,401	8,675	7,449	6,821	6,928	995
Housebreaking and Theft (Nighttime)	26,535	24,238	21,003	18,444	18,861	3,023
Lorry / Van Theft	3,485	3,698	4,306	4,570	5,551	777
Car Theft	6,196	7,278	8,520	8,544	8,537	1,370
Motorcycle Theft	41,905	45,903	47,223	47,137	50,212	8,204
Snatch Theft	-*	15,082	14,368	14,640	15,798	2,273
Other Theft	60,436	54,881	33,210	28,043	27,638	4,833
Total	147,958	159,755	136,079	128,199	133,525	21,475
GRAND TOTAL	169,115	181,359	156,469	149,042	156,315	25,146

Note:

* The snatch theft cases for the year 1999 has not been separated from other cases of theft.

(Source: http://www.rmp.gov.my/rmp03/statjsjindeks97_02.htm; <http://www.rmp.gov.my/rmp3/statjsjindeks04.htm>)

With regards to public security, the Government is the driver of growth for this industry. The Government has allocated RM12.16 billion for defence and internal security during the years 2001-2005, of which at least 60% are allocated to defence spending. Exporting countries to Malaysia are varied; the main criteria being that the equipment meets with the required specification and application; notable sources are the UK, USA, Europe, Japan and Australia. The tables below show the trends relating to the Malaysian Federal Government's spending on security which provides an indication of the growth potential in this segment.

5. INDUSTRY OVERVIEW (CONT'D)

**Malaysia: Federal Government Operating Expenditure for Security
(RM Million)**

	2000	2001	2002 ^{*i}	2003 ^{*ii}	2004 ^{*iii}
Defence	3,972	4,779	5,119	5,840	6,482
Year On Year Growth	N/A	20.3%	7.1%	14.1%	11.0%
Internal Security	2,987	3,531	3,910	4,171	4,622
Year On Year Growth	N/A	18.2%	10.7%	6.7%	10.8%
Total Security Expenditure	6,959	8,310	9,029	10,011	11,104
Year On Year Growth	N/A	19.4%	8.7%	10.9%	10.9%

**Malaysia: Federal Government Development Expenditure for Security
(RM Million)**

	2000	2001	2002 ^{*i}	2003 ^{*ii}	2004 ^{*iii}
Defence	1,854	2,572	3,385	3,326	2,089
Year On Year Growth	N/A	38.7%	31.6%	(1.7%)	(37.2%)
Internal Security	478	715	948	737	594
Year On Year Growth	N/A	49.6%	32.6%	(22.3%)	(19.4%)
Total Security Expenditure	2,332	3,287	4,333	4,063	2,683
Year On Year Growth	N/A	41.0%	31.8%	(6.2%)	(34.0%)

Notes:^{*i} Estimated Actual^{*ii} Revised Estimate^{*iii} Budget Allocation (In relation to the Federal Government's development expenditure for security, the amount excludes RM2.0 billion contingency reserve)

(Source: Department of Statistics; Economic Report 2003/2004)

With respect to the public safety and defence industries, there has recently been a spate of hijacking, piracy and gangsterism, including "tonto" activities as well as robberies and thefts including snatch thefts. To overcome these problems, the Government will increase and strengthen security and enforcement. The police force will step up their security surveillance throughout the country. The Government will review the operations of several departments of the Royal Malaysian Police with a view to increasing their capacity and effectiveness through the provision of equipment and special training. Apart from this, the Government has also established the Malaysian Maritime Enforcement Force (APMM) in its efforts to increase surveillance in our waters, such as the Straits of Malacca.

A sum of RM4.6 billion for operating expenditure is provided for internal security while RM6.5 billion is allocated to the Ministry of Defence for 2004. For development expenditure, allocations of about 600 million and RM2.1 billion have been provided, respectively to equip and modernise the defence and security systems of the nation. Generally, relating to these two categories of expenditure, there has been an overall uptrend.

(Source: Independent Market Research Report by ACN dated 21 November 2003 and Executive Summary Report dated 20 July 2004)

5. INDUSTRY OVERVIEW (CONT'D)

5.3 RELEVANT LAWS AND REGULATIONS GOVERNING THE ICT INDUSTRY

In the Government's efforts to promote the use of ICT and to encourage the growth of the Malaysian ICT industry, various laws and regulations were enacted. The following are some of such legislations:

(i) Digital Signature Act 1997

Enforced on 1 October 1998, it enables the development of electronic-commerce, by providing an avenue for secure and legally recognised online transactions through the use of digital signatures. It serves as a framework for the licensing and regulation of certification authorities, and the recognition of digital signatures. There are currently 2 certification authorities that have been appointed, namely Digicert Sdn Bhd and MSC Trustgate Sdn Bhd.

(ii) The Copyright (Amendment) Act 1997

This Copyright (Amendment) Act 1997 amended the Copyright Act 1987 and came into force on 1 April 1999. It makes unauthorised transmissions of copyright works over the internet an infringement of copyright. It is also an infringement of copyright to circumvent any effective technological measures aimed at restricting access to works, thus protecting intellectual property rights for companies investing in the ICT industry.

(iii) Computer Crimes Act 1997

This Computer Crimes Act 1997 was brought into effect on 1 June 2000. It governs activities relating to the misuse of computers, for example, unauthorised access to computer materials, unauthorised access with the intent to commit other offences, and unauthorised modification of computer contents.

(iv) Telemedicine Act 1997

Provides a framework for licensed medical practitioners to provide telemedical services using audio, visual and data communications. The Telemedicine Act 1997 has not yet come into effect.

(v) Communications and Multimedia Act 1998

This Communications and Multimedia Act 1998 came into effect in stages, commencing on 1 April 1999. It provides a regulatory framework to cater for the convergence of the telecommunications, broadcasting and computing industries. This will assist in making Malaysia a major global hub for communications and multimedia information and content services. The Communications and Multimedia Act 1998 repealed the Telecommunications Act 1950 and the Broadcasting Act 1988. The Malaysian Commission for Communications and Multimedia, appointed on 1 November 1998 is the sole regulator of the new regulatory regime.

(Source: Independent Market Research Report by ACN dated 21 November 2003)