

## **REVIEW OF OPERATIONS**

The Group continued to enjoy business growth during the period under review. For the six-months ended 30 September 2000, unaudited consolidated profit attributable to shareholders rose 18% to HK\$171 million, on the back of a turnover of HK\$1,063 million, representing 23% growth over the same period last year. Profit from operating activities was HK\$211 million, up 27%. Earnings per share were HK29.9 cents compared with HK25.2 cents for the corresponding period last year.

Overall, Hung Hing continues to benefit from having significant economies of scale, which have been bolstered recently by expanding and upgrading production facilities. The Group's ability to vertically integrate operations, deliver value to customers, and effectively control materials costs all contributed to the satisfactory financial performance amidst keen competition and industry consolidation.

During the six months under review, the depreciation of the Euro and rising oil prices have had certain effects on the Group's business. The former has increased the costs of our products to European customers and the latter has caused operating costs to increase, thus putting pressure on profit margins. These factors are offset by an increase in customer orders from both overseas and domestic markets. Our broad customer base also means that we do not have to rely on any single market.

Adjustments in paper prices, primarily during the middle of 2000, have had both positive and negative ramifications for our business. On the positive side, the costs of obtaining raw materials are reduced; however, lower prices place pressure on our paper trading business and its ability to achieve desirable margins.

### **Paper and Carton Box Printing and Manufacturing**

This division accounted for 56% of Group turnover. Contribution to profit from operating activities was 69%. Its profit contribution increased by 32% over the same period last year.

During the last six months, we experienced increases in both domestic sales and sales to overseas customers. A majority of our sales are currently to U.S. and European customers, and the strong U.S. economy has had a positive impact on sales. Likewise, business from the China market also continued to increase as customers continue to demand for higher quality packaging.

Further, export orders for children's books and other paper products continue to be very strong. We have received very good response from overseas customers for such new items as coasters, mouse pads, and coin albums. We

plan to further penetrate the global market for these types of products by expanding into the production of other high-end novelty products with innovative features.

To accommodate the increase in demand for children's books and speciality products, the new 400,000 square feet building of the Shenzhen plant came into operation in May. In addition, a new 250,000 square feet annex to our Zhongshan factory is being built, and is expected to come into operation early 2001.

### **Paper Trading**

The paper trading division was affected by adjustments in paper prices. Its contribution to Group turnover was 19% and profit from operating activities was 12%.

Hung Hing countered the effects by taking advantage of our ability to expand our source of paper from Europe and Latin America countries and broaden its range of paper offered to customers. Our improved operational efficiencies and an increase in paper consumption from the Group's manufacturing divisions helped offset the effects of falling paper prices.

As a result, the Group has been able to maintain its paper trading business with 3% increase in profit from operating activities over the same period last year.

### **Corrugated Carton Manufacturing**

This division achieved the largest percentage increase in turnover among the three core businesses or a 27% increase over the same period last year. Its contribution to profit from operating activities rose by 28%.

The respectable performance of the division is attributable to continuing strong demand from both large original equipment manufacturers and the domestic China market. At the same time, we are reducing distribution costs by expanding our own transportation fleet.

To continue meeting increased demand for our products, we are building a new corrugated carton manufacturing plant in Shenzhen, which will ultimately provide an additional 120,000 square feet of production space. This initiative will significantly increase our capacity in this segment and ability to meet customer requirements.

## **Associates**

### **Zhongshan Rengo Hung Hing Paper Manufacturing Company Limited**

The adjustments in paper prices and the slowdown in market demand have squeezed the profit margin of the paper mill. As a result, the Group's share of profit in this 35% owned joint venture fell by 6% to HK\$9.3 million.

On the positive side, due to the upgrading of machinery and strengthening of management control, the quality of our end products has been further enhanced.

### **Zhongshan Ren Hing Paper Manufacturing Company Limited**

Under an agreement signed with our existing partners of Zhongshan Rengo Hung Hing in May 2000, this 35% owned joint venture has been established for operate a new production line for the manufacture of kraft liner and textliner. We have invested our part of share capital of HK\$40 million. The new plant is being constructed and will come into operation by end of 2001.

## **Liquidity and Capital Resources**

During the period under review, the Group has made more use of the lower cost Renminbi loan facilities as made available to its China subsidiaries. The currency exposure in our Renminbi borrowings has been hedged by our Renminbi asset and Renminbi revenue as generated by our China subsidiaries.

At 30 September 2000 we had cash on hand of HK\$146 million and bank borrowings of HK\$246 million. The net borrowings of HK\$100 million as a ratio to our shareholders fund of HK\$1,375 million was 7.3%, representing a relatively low gearing ratio.

We have adequate internal resources and banking facilities to finance our current expansion program and our working capital requirement.

## **Prospects**

Hung Hing believes that continued growth can be maintained among its core businesses of paper box printing, corrugated carton manufacturing, and paper trading. China's imminent entry into the World Trade Organization will open up more opportunities and create more demand for quality paper products. Given the Group's competitive advantages in technology, quality and vertical integration, we are optimistic about gaining a bigger share of the China market.

We expect to see continued pressure on selling prices. However, this pressure will be offset by Hung Hing's ability to timely adjust its paper storage and to continuously look for cheaper sources of paper, as well as our ongoing effective cost control measures.

Our overall spending on investment in production capacity for the first half of the financial year was around HK\$51 million. We have earmarked HK\$130 million for capital expenditure in this financial year, a majority of which has been committed. These investments will allow us to achieve greater economies of scale, improve technologies, and upgrade facilities to enable us to provide superior services to customers.

Though there are signs of a slowdown in worldwide economies, we remain cautious but optimistic about the continuous growth of the Group in the second half of the financial year.