MANAGEMENT DISCUSSION AND ANALYSIS

OPERATING ENVIRONMENT

The significant rebound in the overall market sentiment in Hong Kong and Mainland China during the second half of the year ended 29 February 2004 has offset the negative impact caused by the SARS outbreak earlier in the Year. With the containment of SARS and better economic performance, people's confidence in a positive economic trend returned, driving consumption.

OPERATING RESULTS

Capitalising on improved market conditions, the Group's turnover for the year ended 29 February 2004 ("the Year") increased by 49% to HK$464 million as compared with that of the previous year. In particular, the Hong Kong operations achieved outstanding performance, reporting a 33% increase in turnover and returning to profitability for the Year. The strong growth was attributable to the Group's successful capturing of the opportunities from rising consumption trend by increasing its sales volume, which led to a substantial increase of 49% in gross profit to HK$202 million.

In addition to the upsurge in gross profit, the Group had also succeeded in reducing its selling and distribution costs and general and administrative expenses by 3% and 6% respectively to HK$113 million and HK$55 million when compared with those of the previous year. The Group thus realised an operating profit of HK$36 million for the Year, against an operating loss of HK$19 million in the previous year. All these positive results had significantly contributed to bringing the Group more than back to profitability.

For the Year, the Group reported a profit attributable to shareholders of HK$36 million, as compared to a loss attributable to shareholders of HK$14 million as restated in the previous year. Such tremendous profit upturn had been achieved due to the following factors:

1. A substantial increase of HK$66 million in gross profit as mentioned above;

2. A reduction of HK$8 million in selling and distribution costs and general and administrative expenses, including HK$4 million in operating lease rentals in respect of land and buildings;

3. An increment of HK$2 million in the share of profit after tax of jointly controlled entity (2003: HK$1 million);

4. No dividend income from other investment was received for the Year (2003: HK$19 million);

5. The deferred taxation credit had been reduced by HK$7 million in the Year arising from the adoption of revised SSAP 12 "Income Taxes";

6. An overprovision of Hong Kong profits tax for prior years of HK$5 million was written back during the year (2003: Nil);

7. For the taxation in the Mainland China, there was an increase of HK$7 million as a result of increase in profits for the Year (2003: HK$4 million).

MANAGEMENT DISCUSSION AND ANALYSIS

BUSINESS REVIEW

Mainland China and Hong Kong continued to be the Group's main markets, accounting for 58% and 31% of the Group's turnover respectively during the Year. For the Year, the two geographical segments reported HK$19 million (2003: HK$3 million) and HK$8 million (2003: operating loss of HK$25 million) of operating profits respectively. As to the Group's core business – shoes operations, it reported a turnover of HK$392 million and an operating profit of HK$39 million for the Year.

Mainland China

Shoes operations

Turnover of the Group's shoes operations in Mainland China for the Year had substantially increased. Much of the increase was attributable to the outstanding sales performance achieved in the second half of the Year.

During the Year, the Group refurbished almost half of its outlets in Mainland China in a bid to promote a younger brand image to attract patrons. While this brand building measure took effect in enticing customers, the Group's strategy of maintaining sufficient quantities and styles also succeeded in timely meeting rising demand.

In addition to brand enhancement, the Group's market segmentation strategy had also contributed to the encouraging results. During the Year, the Group continued to operate its shoes business in Mainland China under the brand names of *Le Saunda 萊爾斯丹* and *Comfort and Easy (CnE)*, the former being targeted at mid to high-end market and the latter at young people. Owing to the solid foundation established by *Le Saunda萊爾斯丹*, the brand maintained stable sales, while *CnE*, which is a young brand characterised by a Japanese style, had sustained encouraging growth during the Year.

To consolidate its marketing efforts, the Group had streamlined its sales network during the Year, opening a number of self-operated stores and counters in major cities in Mainland China under the brand names of *Le Saunda 萊爾斯丹* and *CnE* while reducing some of its franchised outlets at unfavourable retail locations.

Contribution from the Group's original equipment manufacturing ("OEM") business continued to increase during the Year. The Group increased output and achieved high capacity utilisation of its production facilities in Shunde, Mainland China, in response to growing demand from both internal operation and OEM business towards the end of the Year.

Cosmetics

The Group engaged in the manufacturing and sale of cosmetics under the *Right Angle* brand in Mainland China. During the Year, this business segment reported a turnover of HK$3 million and an operating loss of HK$4 million. Owing to the highly competitive market conditions and the requirement of special technology and expertise, the Group decided to discontinue the operation of this business segment, which had been displaying unsatisfying performance since it commenced in mid 2001, and allocated the released resources to the better performed and expanding shoes business.

Property development

For the Year, the Group's jointly controlled entity in Mainland China, Shunde Shuang Qiang Property Development Company Limited, contributed a profit of HK$6 million (2003: HK$2 million). After deducting the current tax charge of HK$3 million (2003: HK$1 million), net profit after tax from it amounted to HK$3 million (2003: HK$1 million).

The Group's Shunde-based wholly-owned subsidiary, 順德市信達房地產開發有限公司, reported a turnover and operating profit of HK$70 million and HK$0.4 million from the sales of its residential project – 陽光花園 – during the Year.

Hong Kong

The local economy generally showed a strong recovery during the second half of the Year, after a widespread economic devastation from the SARS outbreak. In the face of unexpected challenges and drastic changes in market conditions, the Group proceeded with its consolidation strategy, closing under-performed outlets, while increasing stocks at each existing shop to ensure sufficient quantities and styles to meet demand at any given time. This strategy had effectively helped this market segment return to profitability during the Year.

In view of the improved market sentiment, the Group conducted a joint-promotion with a local bank in November 2003 to boost sales. The marketing exercise was proved to be a success, especially in raising sales volume and public awareness of the *Le Saunda* brand. Moreover, Christmas and New Year's sales also surged tremendously, as consumers' confidence in the economic outlook increased and they were more willing to spend.

As a result of the Group's successful capitalising on the market recovery, turnover from the Hong Kong operations leapt by 33% to HK$143 million during the Year under review. On the Hong Kong's performance in the second half of the Year, turnover soared by 78% as compared to the first half of the Year. In addition, the closure of a number of stores also helped save several millions of dollars in overheads. Given an increased turnover and lower costs, the Hong Kong operations reported an operating profit of HK$8 million.

Others

Apart from Mainland China and Hong Kong, the Group has also expanded its shoes business to overseas markets. During the Year under review, the Group operated an outlet in Macau and exported sales to countries including Japan, Russia, Italy, the UK and the US. Turnover from shoes operations outside the Mainland China and Hong Kong markets rose by 1.6 times to HK$52 million when compared with that of the previous year.

MANAGEMENT DISCUSSION AND ANALYSIS

FINANCIAL POSITION

During the Year, the Group's cash position remained sound. Its cash and bank balances amounted to HK$92 million as at 29 February 2004, as compared with HK$43 million at the start of the financial year. The Group obtained total banking facilities of HK$64 million (28 February 2003: HK$177 million). The Group's investment properties and other properties with net book value amounting to HK$43 million (28 February 2003: HK$43 million) have been pledged to secure bank loan facilities of HK$64 million (28 February 2003: HK$124 million) granted to certain subsidiaries of the Group. Out of such facilities, the Group's total short term bank borrowings were HK$6 million as of 29 February 2004, compared with HK$2 million as of 28 February 2003. The Group's net worth amounted to HK$387 million (28 February 2003: HK$351 million). The Group's gearing ratio stood at 0.017 as at 29 February 2004, against 0.005 as at the start of the Year. The calculation of the Group's gearing ratio was based on the total bank borrowings of HK$6 million and net worth of HK$387 million as at 29 February 2004.

The Group's liquidity position also remained healthy, with a current ratio of 3.5 times (28 February 2003: 2.9 times) and a quick ratio of 1.6 times (28 February 2003: 0.9 times) as at 29 February 2004.

During the Year under review, the Group increased its inventory level to ensure sufficient quantities and styles were available to meet market demand. As a result, the Group's inventory turnover rose from 85 days to 88 days, and the amount of inventory increased from HK$60 million to HK$64 million during the Year.

Bank loans and overdrafts of the Group were taken out in Hong Kong dollars, Renminbi, US dollars and Euro. The annual interest rate of the borrowings during the Year under review ranged from 2.22% to 6.53%. Forward contracts were used, if necessary, for hedging of purchases from overseas, related debts and bank borrowings. During the Year, the Group was not exposed to material foreign exchange risk regarding Renminbi currency exposures on revenues generated or assets located in Mainland China as the exchange rate of Hong Kong dollars against Renminbi was relatively stable. In addition, working capital requirements for business in Mainland China were financed by local bank loans denominated in Renminbi as far as possible for hedging purpose.

The Group believes that its cash holding, liquid asset value, future revenue and available banking facilities will be sufficient to fund the working capital requirements.

During the Year under review, the Group did not have material acquisitions or disposals of subsidiaries or associated companies. For the current financial year, other than the establishment of a new apparel line and related outlets in certain parts of China, the Group does not have plan for material investments or change of capital assets.

CONTINGENT LIABILITIES

Details of contingent liabilities of the Group at the balance sheet date are set out in note 27 to the accounts.

EMPLOYEES AND REMUNERATION POLICIES

As at 29 February 2004, the Group had a total of 1,945 employees of which 165 were based in Hong Kong and 1,780 were based in Mainland China. Total staff costs including directors' emoluments and net pension contributions for the Year amounted to HK$75 million (2003: HK$75 million). The Group has structured training programmes for all employees. Outside consultants are also invited as lecturers to enrich the scope of the programmes.

Competitive remuneration packages commensurate with individual responsibilities, qualifications, experience and performance are structured. In addition, the Group has adopted a share option scheme and discretionary bonus policy for eligible employees of the Group.

PROSPECTS

In the current financial year, the Group will focus on the development of the Hong Kong and China operations in a bid to continue capitalising on the growing demand in both markets. To ensure healthy and stable growth, the Group will conduct its business expansion in a prudent manner.

With regard to its shoes operations, the Group will open a number of freestanding stores under *Le Saunda 萊爾斯丹* and *CnE* in Mainland China, and increase several franchised outlets in various cities. For the Hong Kong market, the Group intends to open a few mega stores within prestigious shopping malls. Each of these stores, which will be more spacious, is intended to enhance and rejuvenate the brand's image, and to attract more young customers. The Group intends to use its existing internal resources and available banking facilities to finance its ongoing developments so as to maintain a low gearing level.

In addition to expanding its shoes operations, the Group will diversify into the apparel business under the brand name *Antinori*. This will be a medium to high-end street wear line, with emphasis on fashion. The Group will be engaged in high profit margin activities such as design and merchandising, and will outsource the lower margin production process. Such arrangement will enable the Group to make substantial savings from heavy capital investment and overheads. A number of *Antinori* stores are expected to be unveiled in Shanghai in late 2004.

Leveraging its strong market presence and well thought out plans for expansion of existing operations and diversification into new activities, the Directors are optimistic that the Group will continue to seize market opportunities to maximise returns for the Company and its shareholders.