MANAGEMENT DISCUSSION AND ANALYSIS

The Group continued to achieve steady growth in China as well as other overseas markets during the period under review.

During the six months ended 30 September 2004, the Group achieved a total turnover of HK$1,207 million, an increase of 8 per cent over the comparable period last year, with turnover increasing in its major business divisions. This increase was attributable to steady growth in the Group's geographic markets in mainland China, Europe and the US.

As a result of macro-economic factors such as adjustments in oil prices and a shortage of water in Southern China, the Group's operating efficiencies and cost of sales were impacted. Other factors including price pressure due to competition, and a start-up loss associated with the Wuxi plant contributed to increased cost of sales, leading to a decline of 4 per cent in the Group's profit from operating activities.

The Group's new facility at Wuxi became fully operational and the Group's printing plant at Shenzhen reached full capacity during the period under review. The Group invested in future growth by signing a contract for the purchase of a 3.5 million sq. ft. plot of land for building an additional facility in Heshan to supplement the Shenzhen facility. The first phase of the new facility is targeted for completion by mid-2005. The Group also signed an equity transfer contract to increase its stake in the two 35 per cent owned joint ventures in Zhongshan to reach an effective ownership of approximately 58.5 per cent of the associates.

The Group received a one-time tax refund of HK$6.9 million from the mainland Chinese government as a result of profits reinvested into its two Chinese subsidiaries in past years.

The Board of Directors has declared an interim dividend of HK$9.5 cents per share in cash with a script option for the current financial year.

Gaining share in China and export markets

The Group continued to derive benefits from the overall improvement of the global and mainland China economies, and specifically the strong currency in Europe, by increasing its revenues from these two regions.

China: The mainland Chinese economy continued to grow steadily, and the Group diversified its business by expanding its customer base. The Group's facilities in Wuxi, Zhongshan and Shenzhen have all been successful in securing revenue from new domestic customers. As a result, the Group achieved overall revenue growth of 31 per cent on the mainland. Increases in material costs and competition in the market continued to exert pressure on margins but the Group's strong reputation for quality, service and reliability enabled it to win share from its competitors during the period under review. The Group's Wuxi company opened a new marketing office in Shanghai to further improve its level of customer service and marketing to customers in mainland China.

Gaining share in China and export markets *(continued)*

The US: The Group continued to make steady progress in the US, especially for innovative children's books, to achieve a growth of 9 per cent in this market. The Group continued to work with strategic partners in the US to develop packaging programs for companies who are doing more outsourcing in China.

Europe: During the period under review the Group increased its revenues from the European Union countries by about 30 per cent. This growth was in part due to a strong Euro which resulted in increased order flows to mainland China, and enabled the Group to stay competitive on a cost basis. The Group also strengthened its marketing activities in the UK, Germany and Italy, with new contacts established in these key markets.

Paper and Carton Box Printing and Manufacturing

This division continued its trend of steady volume growth in both mainland China and overseas export markets to record an increase of 12 per cent in turnover. This growth was driven in part by orders from new customers.

The first half year saw a water shortage in Southern China, which resulted in a temporary decrease in operating efficiencies. The Group has acted to counter this by expanding production facilities, sourcing materials from cheaper locations and building additional facilities at Heshan, away from the core industrialized areas of Shenzhen. As worldwide oil prices stabilize, it is expected that this division's efficiency would improve.

The division recorded an increase in volume of 16 per cent over the same period last year and accounted for 67 per cent of the Group's turnover for the period. The division's contribution to the Group's profit from operating activities was the largest among the three key business divisions, at 80 per cent.

Paper Trading

This division was in a transitional stage during the period under review, with stock levels being built up in the Group's Shenzhen distribution and logistic facility, and the continued gradual reduction in stock levels in Hong Kong. Competition, combined with the impact of this transition on operation, led to a drop in external sales of this division of 18 per cent.

With the grant of an import permit in July 2004 for the Shenzhen facility, this division is expected to do increasing volume of business. The growing number of paper mills in mainland China created pricing pressure, and resulted in this division recording a contribution to the Group's profit of HK$15 million.

Corrugated Carton Manufacturing

This division recorded an increase in turnover of 16 per cent, largely driven by growth in volume of 12 per cent. This division successfully expanded its customer base during the period under review to achieve increased domestic sales in the mainland China market. The growth was driven by increased capacity in the Group's Shenzhen facility and aggressive marketing.

The Group is now further augmenting its capacity by installing a new corrugator at its Zhongshan facility. The corrugator is presently being installed and is expected to become operational by early 2005.

Associates

Zhongshan Rengo Hung Hing Paper Manufacturing Company Limited
Zhongshan Ren Hing Paper Manufacturing Company Limited

Foreseeing increased demand for corrugated materials from the domestic China market and internal consumption within the Group, the Group entered into a contract, subject to shareholders' approval, to increase its stake in its two 35 per cent owned joint ventures in Zhongshan to effectively 58.8 per cent. The associates improved their profit contribution to the Group by 14 per cent as a result of increased demand in the domestic China market.

Liquidity and Capital Resources

Capital expenditure during the period amounted to HK$125 million, of which HK$42 million was spent on land and buildings and HK$83 million was spent on machinery and equipment.

To support our capacity expansion, we sought to arrange more term loan facilities. Of our total bank borrowings of HK$487 million as of 30 September 2004, HK$300 million was in long-term borrowings with a repayment schedule falling within two to five years.

To take advantage of the low interest rate environment in Hong Kong, most of our bank borrowings were in Hong Kong dollars. Of the total bank borrowings of HK$487 million, 95 per cent was in Hong Kong dollars and 5 per cent was in U.S. dollars.

With a higher level of borrowings, our interest expenses increased by 17 per cent to HK$3.5 million.

As of 30 September 2004, we had cash on hand of HK$299 million, of which HK$198 million was placed in short-term deposits primarily in U.S. dollars and RMB. Our cash position and available banking facilities are adequate to support our ongoing expansion plan.

Prospects

The Group expects the global economic environment to continue on its trend of steady growth, resulting in steady business performance for the remainder of the year.

During the period under review, many manufacturers in China were caught off-guard by the power and water supply problem and their operations have been disrupted. Rising oil and coal prices served to erode the profits of many factories, leading to a slowdown in business. However, these factors have served to benefit those who survived this period for the year ahead. The Group has planned for these developments by diversifying its production base geographically. The Group will continue to emphasize delivery of value-added services and build upon its reputation for quality and reliability while retaining cost controls.

The Group continues to invest in facilities for the future, with plans in place for a new facility in Heshan. The new corrugator in the Zhongshan facility is expected to commence operation in early 2005.

With the well-established trend of outsourcing to China combined with the continued recovery of the global economy, the Group is optimistic that its high quality and emphasis on end-to-end service will give it an advantage in capturing the opportunities of the future.