Management Discussion and Analysis

BUSINESS REVIEW

During the year ended 31st December, 2006, the Group recorded a consolidated turnover of HK$279,133,000, representing a decrease of 20% from HK$349,637,000 of the previous year. This was primarily due to a business injection into our associated company, Weilburger Manfield Limited ("WML"), together with a decrease in sales to WML after commencement of its own production activities since the second half of 2005. However, as a result of the business injection, the Group gained a substantial increase of revenue from other income sources, such as licensee fees and royalty fees.

The Group recorded a decrease of 32% in gross profit to HK$60,131,000. The net profit attributable to shareholders during the year was HK$28,966,000, a decrease of 44%, compared to the figure of HK$51,561,000 in 2005. This represented a net profit per share of HK11.6 cents (2005: HK20.6 cents).

REVIEW OF OPERATIONS

The Group was confronted with a tough operating environment in the period under review. One of the challenges was rising operating overheads. Continuing from an escalating trend in recent years, the prices of crude oil and other key raw materials remained high, thereby driving up production costs for the Group. Furthermore, labour costs were also increasing. The general labour shortage in Shenzhen and other parts of Southern China, the traditional source of our manpower supply, required us to offer higher wages to our workers in order to retain them.

A number of our competitors had adopted price-cutting measures to maintain their market shares. Responding to the challenge of growing competition, the Group continued to provide quality products and services at reasonable prices. However, customers were generally price-sensitive and cautious about placing orders. The stagnant toy industry also led to a decline in demand for coatings, one of the Group's core products.

On the whole, the Group had taken several measures to improve its profitability and operational efficiency. Stringent cost-controls were implemented, as we sought to identify less-expensive sources of raw materials as part of a larger effort to strengthen our supply network. Work processes were rationalized and streamlined internally to strengthen our production efficiency. Strengthening our competitive edge, we made persistent efforts to enhance our business flexibility. In addition, the Group introduced more responsive services and a logistic system with enhanced efficiency.

Investments were made to expand and improve the Group's factory facilities. In the second half of 2006, a new factory of WML came into operation in Wuxi, China, to meet the needs for increased production capacity. Measures were also taken to step up production safety and environmental protection in the vicinity of our manufacturing premises. Correspondingly, other positive measures taken by the company included expanding its market in Eastern China and coming up with a large range of price variations for its products to meet the budgetary requirements of customers. As a result of its satisfactory performance, WML was able to contribute substantially to the Group's profits.

The Group also launched marketing campaigns to boost the sales of its products. Efforts were made to monitor the market trend more closely. The Group's sales team also visited customers regularly in order to understand their needs better and obtain feedback. Based on such feedback, the products and services of the Group were enhanced for attaining a higher level of customer satisfaction.

OUTLOOK

Prices of crude oil and other raw materials are expected to remain high in 2007. Price fluctuations of these raw materials will continue to be a key factor influencing the chemicals industry in the Greater China region and around the world. Despite this, the demand for chemical products, such as the ones produced by the Group, is likely to increase, given the buoyant economies in Hong Kong and China. On balance, however, the Group will strive for a sustained market share amid keen competition in the mature Guangdong market.

To enhance its competitive edge, the Group has formulated a broad strategy focusing on efforts to consolidate its existing customer relationships. Measures will be taken to expand its current customer base and boost the sales of its high-yield products, such as those in high demand from the electronics market.

It will also be necessary for the Group to identify potential investment opportunities, such as those related to the purchase of additional factories or land. Plans are underway for the Group to open a factory in Changzhou, Jiangsu Province, in the coming months. The Group owns 80% in this sino-foreign equity joint venture company Changzhou Manfield Chemical Company Limited. The new plant is expected to begin production in the second half of this year to supply coatings, paints and other core products of the Group to tap the growing market demand for these items in Eastern China.

In line with this direction, WML will continue to explore potential markets in Central and Northern China, leveraging on the support of its factory operations in Wuxi.

A major priority of the Group in 2007 will be to enhance the professionalism of its workforce. As with the previous years the Group will continue to conduct internal training for its employees, including group learning sessions at an inter-department level. Internal communications will also be improved to facilitate the exchange of ideas and experience among employees.

LIQUIDITY AND FINANCIAL RESOURCES

The Group observed prudent and stable financial policies in 2006. As a result, it remained in a healthy financial situation and had no outstanding borrowings. The steady growth of its business during the year enabled it to maintain a sufficient cash surplus to finance its operations from internally generated cash flow. As at 31st December, 2006, the Group had ready cash reserves of HK$47,212,000 (2005: HK$49,712,000).

EMPLOYEE AND REMUNERATION POLICIES

As at 31st December, 2006, the Group had around 1,200 employees, including management and administrative staff as well as production workers. Most were stationed in Mainland China while the rest were in Hong Kong. Remuneration, promotion and salary increments for them were assessed according to individual performance as well as professional and working experience, and in accordance with prevailing industry practices.