Managing Director's Report

William FUNG Kwok Lun

Year 2000 was the second year of the Group's 1999-2001 three-year plan. It turned out to be one of the best years the Group has ever enjoyed with a dramatic increase in both turnover and profits.

Trading

With a robust 32% increase in turnover from internal growth and a further 21% from acquired companies, the Group grew at a total rate of 53% to reach almost HK$25 billion. Despite the fact that the recent acquisitions generally operated at lower margins than Li & Fung's core business, profits for the year increased commensurately by 51%.

These results were unprecedented for the Group, reflecting the strength of our deep customer base and wide sourcing capabilities. The increase in business was not specific to one area but represented a broad increase in both apparel and hardgoods for the United States as well as Europe. The geographical breakdown of our markets remained unchanged from 1999, with the United States accounting for 69% of our business. The product mix was slightly more skewed towards garment exports, which accounted for 77%, whereas hardgoods accounted for the balance.

The Group, at this level of turnover, is well positioned to take advantage of operating leverage and economies of scale to become the lowest-cost provider of sourcing services compared to our competitors and even when matched against the economics of large customers that operate their own buying offices. This, together with the unrivalled coverage of the world's manufacturing markets by our network of sourcing offices, means we are in a stronger competitive position than ever before.

Financial position

The Group's financial position reflects the strength of its operating results. After raising about US$250 million in March 2000 with the placement of 60 million new shares, the Group ended the year with a current ratio of 1.36 and a gearing (long term liabilities to equity) of less than 5%. Only the properties of newly acquired Colby have a bank charge in order to secure credit facilities of HK$75 million.

The Group now has a net cash balance of HK$2.7 billion from which it can draw for further expansion should opportunities arise. Most of this cash is deposited in the leading banks of Hong Kong in either HK$ or US$.

The Group has no material contingent liabilities other than trade bills discounted in the ordinary course of business.

The Group continues to do most of its business in US$. Payment to factories are also in US$ or HK$. That, together with a policy of keeping the majority of our assets also in these currencies, ensures that our exposure to exchange rate fluctuations is minimal.

The internet

In 1999, the Company set out its objectives and initiatives with respect to the extensive use of internet-based information technology and its impact on our business.

Despite recent changes in the dot.com space, the Group's view remains unchanged. We will continue to aggressively use internet-based communication as an integral part of our organization. Continuous improvements have been made to upgrade our sophisticated intranet that links up our expanding network of offices. Connectivity with large customers via dedicated extranet sites continues to be a key element of our customer relationships.

Li & Fung's position as a global supply chain integrator requires continual investment in and use of information technology.

On the other hand, we will be conservative in our e-commerce activities.

Our e-commerce initiative in the U.S. via a 57% owned subsidiary StudioDirect is making steady headway. The business made a loss attributable to the Group of HK$23 million and is still essentially in its beta stage. We are confident to be able to reach out to our target audience of small and medium sized customers with our private label offering via the internet and will be gradually bringing these customers onto our internet system.

The Group's attitude, with regard to investments in developing e-commerce, remains highly prudent. Out of the US$250 million fund raised in March 2000 for the expansion of the Group's e-commerce business, US$19 million has been used in StudioDirect as at the end of the year. With StudioDirect, we are planning to cover operating losses with the interest income derived from this fund which was about HK$70 million in 2000, more than offsetting the start-up costs of StudioDirect for the year.

Investments

During the year, the Group continued to streamline its business and disposed of a distribution centre in Panyu, China to its majority shareholder Li & Fung (1937) Limited at book value. The remaining investment portfolio of the Group now relates only to venture capital type investments in trading-related companies mainly in the U.S. and Europe.

Acquisitions

The acquisition of the Swire Pacific trading units: Swire & Maclaine and Camberley effective 1 January 2000 contributed very satisfactorily to the Group's business in 2000.

The acquisition of Colby announced in November 2000 contributed only to the Group's results in the one month of December. At formal completion on 23 March 2001, both the guaranteed profit and net assets were met. Hence the balance of the cash consideration of HK$123,750,000 and the consideration shares of 113,188,000 were paid and issued respectively on the same date.

Staff

At the end of year 2000, and consequent to the Colby acquisition, the Group operated 64 offices in 37 countries with a staff of 4,668, of whom 1,704 were in Hong Kong and 2,964 overseas.

Prospects

With such strong results in 2000, the Group is well positioned to achieve the current three-year plan goal of doubling profits over the years 1999-2001.

There is some apprehension about a possible slowdown of the American economy in 2001. Management is monitoring the situation carefully but so far, there seems to be little impact on our order book.

The inclusion of the full year business of the Colby acquisition in 2001 will substantially benefit the Group and cushion any deterioration in our main market of the U.S. However, management notes that Colby's business is heavily skewed towards the second half. This, coupled with the seasonality factor of other newly-acquired accounts, means that going forward the Group's operating results will be more biased towards the second half of the year.

Hence, barring unforeseen circumstances, the Group is well positioned to achieve our three-year plan goal.

William FUNG Kwok Lun
Managing Director

Hong Kong, 26 March 2001