

MANAGEMENT DISCUSSION AND ANALYSIS

Summary of Results

For the six months ended June 30, 2001, the Group's consolidated turnover was approximately HK\$385.78 million (2000: HK\$426.76 million) and the profit attributable to shareholders amounted to approximately HK\$37.55 million (2000: HK\$47.62 million). Basic earnings per share is 6.98 cents (2000: 9.38 cents).

Dyeing and Finishing Machinery Manufacturing

Fong's National Engineering Company, Limited

During the period under review, the turnover for the sales of dyeing and finishing machinery together with machine parts in respect of this core business has decreased by 14.3% as compared with the same period last year. The main reasons attributable to the decrease in turnover are due to more conservative market sentiment and the slowdown in the major textile and garment importing economies. Despite these, with our continuous efforts to improve operational efficiency and the cost control measures implemented, the business is expected to maintain a satisfactory operating profit.

To further sharpen our competitive edge in the market, we will continue to enhance our efforts in technology advancement and to further improve the designs and operational efficiencies of our machines.

Recently, we have collaborated with a local university to conduct a research project on "Development of Wet Oxidation Process for Treating Textile Dyeing Wastewater" under the sponsorship of the Group. The objective of the research is to incorporate such technology into our machines to make them more environmentally friendly as the concerns and costs of treating wastewater continue to increase in the textile dyeing industry.

Lastly, with the impending accession of China into the World Trade Organisation (the "WTO"), the directors are confident that the demand for our machines will remain strong in China. It is expected that this business segment in the forthcoming years will be optimistic and orders will remain steady for the second half of the financial year.

Stainless Steel Trading

Fong's Steels Supplies Company Limited

Despite the decline of stainless steel prices since August 2000 from its high of approximately US\$1,600 per tonne to the current US\$1,300 per tonne, the stainless steel trading business recorded a turnover of approximately HK\$130.22 million, representing a decrease of 9.4% as compared with that of last year and its operating profit down by 64.3% to approximately HK\$4.9 million.

Stock and account receivables levels are closely monitored so as to minimize the bad debt exposure and to shorten the working capital cycle. The price of stainless steel is expected to stabilize at current level which would be beneficial to our Group as a whole as it represents a significant portion of our manufacturing raw materials. Inventory and cost control measures will be closely monitored with an aim to restore the overall profitability in the forthcoming year.

Stainless Steel Casting

Tycon Alloy Industries (Hong Kong) Company Limited

The turnover of stainless steel casting products was approximately HK\$28.51 million, representing an increase of 57.1% and its operating profit increased from HK\$0.22 million to HK\$1.72 million as compared with the same period last year.

The major markets for this business segment are US and Europe. The value-added precision machining service for stainless steel castings business is being well received by our customers with higher profit margins and which we believe will have a strong growth potential.

Also, this business segment will also continue to serve as a complementary arm to our core business, dyeing and finishing machinery manufacturing, and contribute to an overall increase in our Group's operating effectiveness.

Jointly controlled entity

Monforts Fong's Textile Machinery Co. Limited

An encouraging market response has been received from the successful launch of the stenter machines in the China market. Its brand-name "MONFONGS" has already established a recognition in the Mainland China market as the best price to performance machines.

With the joint efforts of both parties, the production efficiency has been greatly improved and the cooperation has been very successful. Furthermore, it is expected that the production capacity will be nearly doubled as compared to the last financial year.

With Fong's broad base of customers together with its manufacturing know-how and the German partner's leading technology, this cooperation will enhance this joint venture business's competitiveness in terms of costs, delivery time, product quality, service level and marketing. The Board is confident that this business will add satisfactory results to the Group in the coming year.

Associate

Foshan East Asia Company Limited

During the period under review, the business of manufacture and sale of color woven fabrics and related products engaged by Foshan East Asia Company Limited remained stable with healthy growth in both turnover and profit.

We are optimistic that this business will continue to post positive results for the second half of the year with anticipated improved consumer sentiment in the Asian region and the re-engineering efforts put in place last year to improve production quality and efficiency.

Prospects

The Board is of the view that 2001 will be a year of challenge for the Group. However, with prudent management and a clear strategy, the Board is confident that the Group is well placed to continue its growth in its operating businesses.

Looking ahead, the Group is expected to benefit from China's subsequent admission to the WTO, despite certain looming external uncertainties. Meanwhile, the Group will continue strengthening its competitive edge to grasp the opportunities brought by the trend of modernization of machinery in the textile industry in China.

Our corporate vision is to build the Group into a market leader in the dyeing and finishing machinery manufacturing industry.

Liquidity and Capital Resources

The Group mainly financed its operations by cash generated from its business activities and banking facilities provided by its bankers. The Group continued to maintain a healthy financial position throughout the period.

In April, 2001, the Company had granted a total of 43,800,000 share options to certain directors and employees of the Company and its subsidiaries to subscribe for shares of the Company at subscription prices ranging from HK\$0.48 to HK\$0.51. During the period under review, 42,750,000 options were exercised raising a capital of approximately HK\$20.52 million. Details of the share option scheme have been disclosed in the Annual Report 2000. In addition, net cash inflow from disposal of the Group's entire interests in Sunshine City Limited during the period amounted to approximately HK\$140 million.

Accordingly, the Group's net borrowings have been reduced from HK\$66.05 million as at December 31, 2000 to approximately HK\$2.86 million as at June 30, 2001. As a result, the gearing ratio, calculated as the total net borrowings of the Group divided by shareholders' funds, decreased from 0.13 to 0.01. The current ratio was 1.78, reflecting a healthy liquidity level.

As at June 30, 2001, bank borrowings amounted to approximately HK\$119.89 million of which approximately 58% were secured by the Group's certain assets. More than 94% of the bank borrowings are repayable within one year and the remaining are repayable between two to five years. Most bank borrowings were sourced from Hong Kong and were in Hong Kong dollars. The bank borrowings of the Group are predominantly subject to floating interest rates.

The cash and bank balance amounted to approximately HK\$122.30 million of which approximately 82% are denominated in Hong Kong dollars, 8% in US dollars, 6% in Renminbi and the remaining are denominated in various foreign currencies.

The Group was not exposed to any material exchange rate fluctuation during the period under review.

Human Resources

The Group's remuneration policies are reviewed on a regular basis and remuneration packages are in line with market practices in the relevant countries where the Group operates. As of June 30, 2001, the Group had approximately 2,100 employees.