

Climax International Company Limited



2001-2002
Interim Report

INTERIM RESULTS

The Directors of Climax International Company Limited (the "Company") are pleased to announce the unaudited consolidated results of the Company and its subsidiaries (the "Group") for the six months ended 30 September 2001 as follow:

CONDENSED CONSOLIDATED INCOME STATEMENT

		(Unaudited)	
		Six months ended	
		30 September	
	<i>NOTES</i>	2001	2000
		HK\$'000	<i>HK\$'000</i>
Turnover	2	190,932	163,601
Cost of sales		(155,327)	(135,067)
Gross profit		35,605	28,534
Other revenue		7,707	5,470
Distribution costs		(9,528)	(7,872)
Administrative expenses		(24,668)	(26,983)
Other operating income (expenses)		2,693	(2,305)
Profit (loss) from operations	3	11,809	(3,156)
Finance costs	4	(1,718)	(24,384)
Profit (loss) before taxation		10,091	(27,540)
Taxation	5	(6)	(143)
Profit (loss) before minority interests		10,085	(27,683)
Minority interests		(66)	—
Net profit (loss) for the period		10,019	(27,683)
Earnings (loss) per share	6		
— Basic		0.28 cents	(7.38 cents)
— Diluted		0.27 cents	N/A

CONDENSED CONSOLIDATED BALANCE SHEET

		(Unaudited) 30 September 2001 HK\$'000	(Audited) 31 March 2001 HK\$'000
	NOTES		
ASSETS AND LIABILITIES			
Non-current assets			
Property, plant and equipment	7	46,062	52,020
Prepaid rentals		<u>38,625</u>	<u>39,745</u>
		<u>84,687</u>	<u>91,765</u>
Current assets			
Inventories		46,239	71,990
Debtors, deposits and prepayments	8	37,843	32,633
Pledged bank deposits/balances		17,651	16,866
Bank balances and cash		<u>29,109</u>	<u>15,749</u>
		<u>130,842</u>	<u>137,238</u>
Current liabilities			
Creditors and accrued charges	9	40,461	52,236
Taxation payable		3,502	3,694
Bank borrowings			
— amount due within one year		<u>52,028</u>	<u>43,041</u>
		<u>95,991</u>	<u>98,971</u>
Net current assets		<u>34,851</u>	<u>38,267</u>
Total assets less current liabilities		119,538	130,032
Minority interests		66	2,166
Non-current liabilities			
Bank borrowings			
— amount due after one year		<u>25,284</u>	<u>43,623</u>
Net assets		<u>94,188</u>	<u>84,243</u>
CAPITAL AND RESERVES			
Share capital	10	36,197	36,197
Reserves	11	<u>57,991</u>	<u>48,046</u>
Shareholders' funds		<u>94,188</u>	<u>84,243</u>

CONDENSED CONSOLIDATED STATEMENT OF RECOGNISED GAINS AND LOSSES

	(Unaudited)	
	Six months ended	
	30 September	
	2001	2000
	HK\$'000	HK\$'000
Net gains arising from exchange differences on translation of overseas subsidiaries not recognised in the consolidated income statement	—	50
Net profit (loss) for the period	<u>10,019</u>	<u>(27,683)</u>
Total recognised gains (losses)	<u>10,019</u>	<u>(27,633)</u>

CONDENSED CONSOLIDATED CASH FLOW STATEMENT

	(Unaudited)	
	Six months ended	
	30 September	
	2001	2000
	<i>HK\$'000</i>	<i>HK\$'000</i>
NET CASH INFLOW FROM OPERATING ACTIVITIES	25,474	13,159
NET CASH OUTFLOW FROM RETURNS ON INVESTMENTS AND SERVICING OF FINANCE	(1,552)	(23,533)
TAXATION PAID	(198)	—
NET CASH (OUTFLOW) INFLOW FROM INVESTING ACTIVITIES	(1,012)	1,112
NET CASH INFLOW (OUTFLOW) BEFORE FINANCING	22,712	(9,262)
NET CASH OUTFLOW FROM FINANCING	(9,352)	(297)
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	13,360	(9,559)
CASH AND CASH EQUIVALENTS AT BEGINNING OF THE PERIOD	15,749	(66,718)
EFFECT OF FOREIGN EXCHANGE RATE CHANGES	—	(9)
CASH AND CASH EQUIVALENTS AT END OF THE PERIOD	<u>29,109</u>	<u>(76,286)</u>
ANALYSIS OF THE BALANCES OF CASH AND CASH EQUIVALENTS		
Bank balances and cash	29,109	34,340
Bank overdrafts	—	(110,626)
	<u>29,109</u>	<u>(76,286)</u>

Notes:

1. Accounting Policies

The condensed financial statements have been prepared under the historical cost convention.

The interim report has been prepared in accordance with the Statement of Standard Accounting Practice No. 25 "Interim financial reporting" ("SSAP 25") issued by the Hong Kong Society of Accountants and the applicable disclosure requirements of Appendix 16 to the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited.

The accounting policies adopted are consistent with those followed in the Group's annual financial statements for the year ended 31 March 2001 except as described below.

The Group has adopted a number of new and revised Statements of Standard Accounting Practice ("SSAP"s) issued by the Hong Kong Society of Accountants for the first time in the current period. The adoption of these new or revised SSAPs does not have any effect on the current or previous periods' financial statements.

At 31 March 2001, the Group did not have any goodwill or negative goodwill. Following the adoption of SSAP 30 "Business combinations", goodwill arising on acquisitions after 1 April 2001 is capitalised and amortised on a straight line basis following an assessment of its useful life. Negative goodwill arising on acquisition after 1 April 2001 is presented as a deduction from assets and will be released to income based on an analysis of the circumstances from which the balance resulted. During the current period, the Group recognised a negative goodwill arising on acquisition of additional interest in a subsidiary of HK\$614,000 as income.

2. Turnover and Segment Information

An analysis of the Group's turnover and profit before taxation by principal activity is as follows:

	Turnover		Profit before taxation	
	Six months ended 30 September		Six months ended 30 September	
	2001	2000	2001	2000
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Principal activity:				
OEM paper products manufacturing	177,877	144,020	4,700	(1,609)
House brand and agency products	13,055	19,581	3,350	(2,398)
	<u>190,932</u>	<u>163,601</u>	8,050	(4,007)
Interest expenses - net			(1,266)	(23,533)
Write-back of provision for claims of shares by former employees			1,528	—
Write-back of provision for long service payments			1,165	—
Negative goodwill arising on acquisition of additional interest in a subsidiary recognised as income			614	—
Profit (loss) before taxation			<u>10,091</u>	<u>(27,540)</u>

An analysis of the Group's turnover by geographical market is as follows:

	Six months ended	
	30 September	
	2001	2000
	HK\$'000	HK\$'000
United States of America	101,424	64,025
Europe	46,859	46,939
Asia-Pacific	32,431	35,236
Hong Kong	3,602	7,615
Canada	2,653	3,667
Others	3,963	6,119
	190,932	163,601

Contribution to profit by geographical market has not been presented as the contribution to profit from each market is substantially in line with the overall group ratio of profit to turnover.

3. Profit (Loss) Form Operations

	Six months ended	
	30 September	
	2001	2000
	HK\$'000	HK\$'000
Profit (loss) from operations has been arrived at after charging:		
Amortisation of prepaid rentals	1,120	1,120
Depreciation and amortisation on:		
– owned assets	6,125	9,521
– assets held under finance leases	—	16
Guaranteed payment to a joint venture partner in the People's Republic of China	—	725
Loss on disposal of property, plant and equipment	996	—
Office and factory removal costs	—	2,305
and after crediting:		
Gain on disposal of property, plant and equipment other than Climax Building	—	872
Interest income	452	851
Negative goodwill arising on acquisition of additional interest in a subsidiary recognised as income	614	—
Write-back of provision for claims of shares by former employees	1,528	—
Write-back of provision for long service payments	1,165	—

4. Finance Costs

	Six months ended 30 September	
	2001	2000
	HK\$'000	<i>HK\$'000</i>
Interest on:		
Bank borrowings wholly repayable within five years	1,718	24,383
Obligations under finance leases	<u>—</u>	<u>1</u>
Total borrowing costs	<u>1,718</u>	<u>24,384</u>

5. Taxation

	Six months ended 30 September	
	2001	2000
	HK\$'000	<i>HK\$'000</i>
The charge comprises:		
Hong Kong Profits Tax attributable to the subsidiaries	—	132
Taxation in other jurisdictions	6	55
Deferred taxation	<u>—</u>	<u>(44)</u>
	<u>6</u>	<u>143</u>

No provision for Hong Kong Profits Tax has been made in the financial statements as the estimated assessable profit of the Group for the current period was wholly absorbed by taxation losses brought forward.

Hong Kong Profits Tax was calculated at 16% of the estimated assessable profit for the previous period.

Taxation in other jurisdictions is calculated at the rates prevailing in the respective jurisdictions.

8. Debtors, Deposits and Prepayments

At 30 September 2001, the balance of debtors, deposits and prepayments included trade debtors of HK\$31,567,000 (HK\$27,793,000 at 31 March 2001). The aging analysis of trade debtors at the reporting date is as follows:

	30 September 2001 HK\$'000	31 March 2001 HK\$'000
0 — 30 days	24,051	19,588
31 — 60 days	2,576	3,684
61 — 90 days	4,359	1,944
91 — 120 days	469	793
> 120 days	112	1,784
	<u>31,567</u>	<u>27,793</u>

The Group allows an average credit period of 30 days (31 March 2001: 33 days) to its trade customers.

9. Creditors and Accrued Charges

At 30 September 2001, the balance of creditors and accrued charges included trade creditors of HK\$22,704,000 (HK\$20,819,000 at 31 March 2001). The aging analysis of trade creditors at the reporting date is as follows:

	30 September 2001 HK\$'000	31 March 2001 HK\$'000
0 — 30 days	8,735	6,109
31 — 60 days	3,556	4,856
61 — 90 days	2,340	2,202
91 — 120 days	2,545	3,889
> 120 days	5,528	3,763
	<u>22,704</u>	<u>20,819</u>

10. Share Capital

There were no movements in the share capital of the Company in either the current or the previous interim reporting period.

11. Reserves

	Share premium HK\$'000	Translation reserve HK\$'000	Capital reserve HK\$'000	Accumulated losses HK\$'000	Total HK\$'000
At 1 April 2000	48,125	(5,397)	18,759	(496,895)	(435,408)
Currency realignment	—	157	—	—	157
Transfer to set off accumulated losses upon capital reduction	(48,125)	—	—	48,125	—
Premium on issue of Subscription Shares	80,000	—	—	—	80,000
Premium on issue of Bank Shares	410,126	—	—	—	410,126
Expenditure incurred for issue of Subscription Shares and Bank Shares	(7,889)	—	—	—	(7,889)
Premium on issue of shares upon exercise of warrants	77	—	—	—	77
Transfer of share capital to set off accumulated losses upon capital reduction	—	—	—	33,749	33,749
Net loss for the year	—	—	—	(32,766)	(32,766)
At 31 March 2001 and 1 April 2001	482,314	(5,240)	18,759	(447,787)	48,046
Realised upon disposal of a subsidiary	—	(74)	—	—	(74)
Net profit for the period	—	—	—	10,019	10,019
At 30 September 2001	<u>482,314</u>	<u>(5,314)</u>	<u>18,759</u>	<u>(437,768)</u>	<u>57,991</u>

12. Capital Commitments

At the balance sheet date, a subsidiary of the Group was committed to contribute approximately HK\$9,070,000 (HK\$9,070,000 at 31 March 2001) in connection with an unpaid investment in a subsidiary.

13. Litigation

The former Chairman of the Company approved a number of employment contracts with certain former employees, under which these former employees were entitled to bonuses in the form of new shares of the Company with an aggregate value equivalent to HK\$7,000,000. These employment contracts were terminated resulting in claims being made by these former employees against the Company.

The Company disputed the claims for shares of the Company equivalent to HK\$7,000,000. However, the Company made a provision of HK\$1,528,000 in the previous years' financial statements in respect of the claims for shares by these former employees. During the period, the directors of the Company considered that the Group is unlikely to make any settlement in respect of the claims and, accordingly, the amount of the provision of HK\$1,528,000 has been written back to the income statement.

INTERIM DIVIDEND

The Directors do not recommend the payment of an interim dividend for the six months ended 30 September 2001 (2000: Nil).

BUSINESS REVIEW, DISCUSSION AND ANALYSIS, AND OTHER INFORMATION

Interim Results

The Group's unaudited net profit attributable to shareholders for the six months ended 30 September 2001 was approximately HK\$10,019,000 (2000: unaudited net loss of approximately HK\$27,683,000) representing an increase of about HK\$37,702,000 over the corresponding period last year.

The competition in the market of paper products is still very severe under the economic downturn of the United States and South East Asia. However, during the period under review, the Group continued to take steps implementing its corporate reengineering and cost saving programme to improve the profitability, competitiveness of the Group's businesses.

The turnover was increased by 17% to HK\$190,932,000 as compare with last period. The gross profit margin for the period was improved by 1.2%. This was mainly attributable to the effect of cost saving in procurement of materials and other manufacturing costs.

Distribution costs, administration expenses and other operating expenses were also reduced by about 15.2% as compare to last period.

Finance costs incurred for the group was reduced by HK\$22,666,000 as a result of the bank debt restructuring agreement concluded on 11 January 2001.

Market

OEM Paper Product

OEM sales was increased by HK\$33,857,000 to HK\$177,877,000 from HK\$144,020,000 last period. This was mainly due to a substantial increase of 58% of sales to the customers in the United States, although such increase was partly offset by a decrease of 13%, 52% in Asia Pacific and other markets respectively. The sales to one of our biggest customers, Walmart in The States recorded a historical high of HK\$56,000,000 in the period. It is more encouraging that the Group has received orders of more than HK\$80,000,000 for the coming months from Walmart and other major customers. This proves that our quality and prices are well received and recognized by our major customers.

Sales to Europe remained very stable and maintained at the same level compared with last period. The OEM sales team under the guidance of the new management has commenced a sales and marketing redevelopment plan for the coming year to explore potential opportunities in markets in Europe and also to recapture the lost customers during the turbulence period in the past when the Group was under financial difficulty.

House Brand Distribution

Sales to each of the division's major markets, namely China, Hong Kong and South East Asia were decreased by 32%, 28% and 45% respectively.

The paper products markets in Hong Kong and South East Asia were primarily affected by the slowing economy and the sluggish retail market where no visible improvement has been shown. The market share of our house brand products was adversely affected by the abnormal prices cut of our competitors in the regions.

The Group entered a Sales and Purchase Agreement with the management in Climaxpaper (Singapore) Pte Ltd. ("CPS") to sell the division's operating subsidiary CPS on 5 April 2001 "the MBO transaction". The MBO transaction was to be completed on 5 October 2001 after the purchasers paid all installments of the consideration for the transaction. However, owing to the financial difficulties of one of the purchasers, they have requested an extension of the settlement of the outstanding installments amounting to S\$168,000 representing approximately 25% of the total consideration to 15 January 2002.

The Group has also entered into a Distribution Agreement with CPS, pursuant to which CPS is appointed to be the sole and exclusive distributor for re-sales of certain of its products including albums and related collectables in Singapore, Malaysia and Thailand. Nevertheless, the sales to the region were far lag behind the minimum sales quotas stipulated in the Agreement. CPS explained that the markets were generally weak and the sub-agents in Malaysia and Thailand have financial difficulties and their purchases had stopped. In such circumstances, CPS has informed the Group in September 2001 that it has the intention to amend certain clauses of the Agreement by surrendering the distribution exclusivity of the Group's products in Malaysia and Thailand. The exclusivity was therefore limited to the distribution rights only for Easyfil brand in Singapore. The Group is now assessing the situation and will negotiate with CPS to reach an agreement or to take appropriate action to protect its rights in the Agreements.

Given that the Group's financial position has been improving and becoming more stable and stronger, the Group will strengthen its effort and allocate adequate resources particularly in product development and establishment of better distribution channels to capture a higher proportion of the market in Hong Kong and South East Asia.

Sales to China market remained comparatively low in the period. It represented 4.3% of the total turnover of the Group. The Group believes, as many others do, China market provides ample opportunities to investors especially after China has become a member of the WTO. The Group, being an active player in the China market for many years is well aware that there are many uncertainties in the present business environment of China we have to cope with before we can actually gain from it. Therefore, the Group will take extra caution to determine our pace to develop the challenging market.

On 3 September 2001, the Group entered into an patent rights agreement with the Haier Group ("Haier") in Qingdao ("Haier"), pursuant to which the Group was allowed to use the Haier Brothers and other related characters owned by Haier in our products such as photo album, notebook and other paper products. These products have been produced and distributed extensively in the markets. Furthermore, the Group is now exploring a wide range of partnership programme with the Haier Group aiming at capturing other businesses opportunities other than the traditional paper product industry.

Besides, on 10 October 2001, the Group entered into a Distribution Agreement with Globalink Marketing Limited ("Globalink") for one year. Pursuant to the Agreement, Globalink serves as an exclusive distribution agent in the Guangdong, Guangxi and Hainan province in China. It guarantees a minimum sales of HK\$1,200,000 each month starting from March 2002. The engagement of Globalink in the distribution of our products will fasten our pace in the development of our existing distribution channels. The Group and Globalink will work hand in hand in formulating sales and marketing strategies to improve penetration of our brands such as Easyfil, Greenery etc. to markets in such provinces. The appointment of Globalink is only the first move of the Group's marketing programme in China. It will apply similar or other tactics to build up the distribution channels depending on situations in different environment and buying behaviors of customers in cities in China.

Enterprise Resources Planning (ERP) System and Company

The first phase of the ERP system, an on line control and integration of flow of cash, materials and information system, has been successfully implemented and the second phase has also been commenced. With the completion of the second phase scheduled in the first quarter of 2002, we expect that the productivity of our production will be greatly enhanced and this will further improve our competitiveness of our company.

Financial Position

As at 30 September 2001, the Group had bank loans amounting to HK\$77,312,000 and cash and bank balance totaling HK\$46,760,000. After deduction of cash and bank balance, the Group's ratio of net bank loans to shareholders' equity was 32%.

The banking facility of HK\$10,000,000 granted to the Group by Standard Chartered Bank subsequent to the restructuring will expire in January 2002.

The group is confident and optimistic to obtain refinancing and financial supports from financial institutions in Hong Kong for its turned-around businesses.

As at 30 September 2001, bank deposits amounting to HK\$17,174,000 was pledged to secured the banking facility granted to the Group and will be repaid to the creditor banks in 11 January 2002.

The Group's capital expenditure during the period under review amounted to HK\$1.5 million. They were incurred mainly for the purchase of computer equipment for the enhancement of the management system.

Exposure to Fluctuations in Exchange Rates and Related Hedges

The Group's bank loans are Hong Kong Dollar borrowings. While US Dollar continues to denominate the Group's major foreign currency receipts, it is the group's view that the current link between HK Dollar and US Dollar will be maintained and the mechanism will continue to function in the foreseeable future.

Contingent Liabilities

The Group has no significant contingent liabilities as at the balance sheet date.

Employees and Remuneration Policies

As at 30 September 2001, the Group employed a total of 2,902 employees in Hong Kong and Mainland China. The Group offers a comprehensive remuneration and benefit package to its employees and remuneration policies are reviewed by the management on a regular basis. The Group adopted a share option scheme for its executive Directors and employees on 19 February 1992.

Management Outlook

Pessimistic sentiment is widely spread in the global market after the incident of September 11. It is of no doubt that market conditions would be more difficult and the competition will be even more severe and sometimes irrational. However, the Group believes, with the dedication of the new management and the full support of its staff, it will find solutions to overcome whatever difficulties it may encounter. The turnaround results and some positive developments in the first half of the financial year provide us additional confidence to drive for success.

DIRECTORS' INTERESTS IN SECURITIES

As at 30 September 2001, none of the Directors or their associates had any interests in the securities of the Company or any of its associated corporations as defined in the Securities (Disclosure of Interests) Ordinance (the "SDI Ordinance").

DIRECTORS' RIGHTS TO ACQUIRE SHARES

As at 30 September 2001, the interests of the Directors in options to subscribe for shares of the Company under the share option scheme adopted by the Company on 19 February 1992 were as follows:

Name of Directors	Number of share options granted during the period and outstanding as at 30.9.2001
Kan Shiu Cheong, Frederick	90,458,000
Chu Hung Lin, Victor	36,182,000
Chan Hoi Lam	36,182,000
Yau Kang Nam	20,000,000

The above options were granted on 31 August 2001, at an exercise price per share of HK\$0.01344. The options are exercisable for a period of three years commencing on 31 August 2001. No options were exercised by the Directors during the six months ended 30 September 2001.

Save as disclosed above, none of the Directors or their spouses and children under the age of 18 had any right to subscribe for securities of the Company, or had exercised any such right during the period.

SUBSTANTIAL SHAREHOLDERS

As at 30 September 2001, the register of substantial shareholders maintained under Section 16(1) of the SDI Ordinance showed that the Company has been notified of the following shareholder with interest representing 10% or more of the Company's issued share capital:

Name of shareholder	Number of shares held
First Century Holdings Limited	2,037,435,889

Save as disclosed above, the Company has not been notified of any other interest representing 10% or more in the issued share capital of the Company as at 30 September 2001.

PURCHASE, SALE OR REDEMPTION OF THE COMPANY'S LISTED SECURITIES

Neither the Company nor any of its subsidiaries purchased, sold or redeemed any of the Company's listed securities during the six months ended 30 September 2001.

REVIEW OF INTERIM RESULTS

The interim financial report of the Group for the six months ended 30 September 2001 has not been audited, but has been reviewed by the Company's Audit Committee and auditors, Deloitte Touche Tohmatsu.

CODE OF BEST PRACTICE

None of the Directors is aware of any information that would reasonably indicate that the Company is not, or was not during the period in compliance with Appendix 14 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited.

By Order of the Board
Kan Shiu Cheong, Frederick
Chairman

Hong Kong, 21 November 2001