

MANAGEMENT DISCUSSION AND ANALYSIS

from left to right:

Mr Kevin Tsang
*Finance Director and
Company Secretary*

Mr Patrick Chau
Chairman

Mr Tommy Leung
Managing Director



FINANCIAL OVERVIEW

Turnover

The turnover of Peace Mark (Holdings) Limited (the "Company") and its subsidiaries (the "Group") is derived primarily from design, manufacture and distribution of timepieces involving OEM, ODM and licence types. For the year ended 31 March, 2002, the Group reported turnover of HK\$931.2 million, increased by HK\$78.8 million, representing 9.2%, from HK\$852.4 million in 2001. This increase was a result of focusing the resources on its core business.

Gross profit

Gross profit remained more or less the same as in 2001 despite an increase of turnover of 9.2%. Gross profit margin dropped slightly from 15.1% in 2001 to 13.9% in 2002. The decrease was mainly due to the pressure on prices because of the global economic downturn.

Other revenue

The increase in other revenue was attributable to the increase in interest income of HK\$1.7 million and increase in exchange gain of HK\$1.6 million as a result of effective treasury policy adopted by the Group.

Administrative expenses and other operating expenses

The total of administrative expenses and other operating expenses increased 3.5% from HK\$73.8 million in 2001 to HK\$76.4 million in 2002 which is in line with the business expansion.



MANAGEMENT DISCUSSION AND ANALYSIS

Finance costs

The finance costs in 2002 decreased by approximately HK\$3.4 million as compared to 2001. This is a result of persistent reduction of interest rate in the market throughout the year and lower cost of borrowings obtained from the banks.

Taxation

The Group's profits tax expenses increased 7.8% from HK\$4.2 million in 2001 to HK\$4.6 million in 2002. The effective tax rate was 11.4% before restatement of profit in 2001 and the effective tax rate was 11.5% in 2002.

Profit attributable to shareholders

Profit attributable to shareholders reported HK\$36.4 million for 2002, compared with a restated profit of HK\$25.8 million in 2001. The increase was partly due to the increase in sales.

Assets

The total assets of the Group increased by 29.2% from HK\$775.3 million in 2001 to HK\$1,001.8 million in 2002. The increase was chiefly attributable to: (i) increase in fixed assets of HK\$52.2 million for the improvement of production facilities; (ii) increase in intangible assets of HK\$35.9 million; (iii) increase in trade and other receivables of HK\$75.7 million due to business growth (iv) increase in inventories of HK\$30.3 million and (v) increase in cash and bank balances of HK\$57.2 million.

Charge on assets

As at 31 March, 2002, there was no pledge of assets.

SEGMENT INFORMATION

The Group's primary business has been customarily divided into three segments, namely, OEM, ODM and licence base.

For the year under review, the turnover of the OEM segment was HK\$338.0 million. Turnover of OEM business represented 41.7% of the Group's turnover.

The turnover of the ODM segment was HK\$497.0 million. The ODM business had contributed a major portion for 2002 since the Group has been transforming from OEM manufacturer to ODM manufacturer. Turnover of ODM business represented 53.4% of the Group's turnover.

Licence business turnover was HK\$46.2 million, representing 4.9% of the Group's turnover. Licence business is growing gradually since the Group has been securing more licensed brands, namely Umbro, Pierre Cardin and Montana blu. During the financial year under review, the sales results of these licensed brands were up to expectation.



MANAGEMENT DISCUSSION AND ANALYSIS

In terms of geographical locations, the United States has been the largest market of the Group. Sales to the United States represented HK\$505.3 million, which is comparable to that of 2001. Sales to the United States represented 54.3% of the Group's turnover in 2002, while the sales to the United States was 59.2% of the Group's turnover in 2001. As the United States is the Group's principal source of the income, management intends to secure its current position and to strengthen the Group's presence and market share by establishing a distribution arm in the United States.

Sales to Europe was HK\$204.7 million and decreased by 1.6% as compared with 2001. Europe represented 22.0% of the Group's turnover.

Sales to Asia was HK\$221.2 million and increased by 58.2% as compared with 2001. Following the gradual recovery of the economy of the Asian region, the Group recorded encouraging increase in the sales to the Asia.

LIQUIDITY AND FINANCIAL RESOURCES

As at 31 March, 2002, the cash and bank balances of the Group was approximately HK\$154.4 million (2001: HK\$108.8 million) while the total financial indebtedness was approximately HK\$420.6 million (2001: 256.5 million) after a HK\$200 million syndicated loan extended to the Company in November 2001.

The total financial indebtedness of approximately HK\$420.6 million, comprising of term loans and syndicated loan of approximately HK\$263.2 million, trust receipt loans of approximately HK\$156.7 million, bank overdrafts of approximately HK\$0.4 million and obligations under finance leases of approximately HK\$0.3 million.

Among the financial indebtedness, approximately HK\$205.8 million are with maturities within one year, HK\$125.3 million are with maturities after one year but within two years and HK\$89.5 million are with maturities after two years but within five years.

On 7 November, 2001, the Company entered into a HK\$200 million facility agreement with a group of banks to arrange a three-year term loan facility available to the Company for refinancing its existing bank debt, general working capital purpose and the improvement in production facilities and expansion in distribution network of the Group.

The current ratio and liquidity ratio increased from 2.1 and 1.6 in 2001 to 2.8 and 2.1 in 2002 respectively due to the increases in accounts receivables, prepayments and other receivables as well as cash and bank balances. The Group's current assets were in excess of its current liabilities by HK\$417.0 million which was a healthy sign of short-term liquidity.



MANAGEMENT DISCUSSION AND ANALYSIS

The Group's accounts receivable turnover was 50 days as at 31 March, 2002 which is comparable to 49 days as at 31 March, 2001.

The inventory turnover was 54 days as at 31 March, 2001 to 71 days as at 31 March 2002 as a result of increase in inventories level as at year end to meet the orders on hand.

As at 31 March, 2002, the gearing ratio of the Group, measured by reference to the financial indebtedness net of cash and bank balances of HK\$266.3 million to shareholders' equity of HK\$547.3 million was approximately 48.6% as compared to 34.6% in 2001.

In view of the Group's cash generating operations, available banking facilities and the proposed rights issue, the Directors are of the opinion that the Group has adequate cash resources for working capital requirements and capital expenditure commitment.

CAPITAL STRUCTURE

As at 31 March, 2002, the Group's net assets was financed by internal resources through share capital and reserves. Total equity attributable to shareholders was HK\$547.3 million representing an increase of 18.7% over 2001.

In August, 2001, Mr. Leung Yung through United Success acquired 10.00% interests in the share capital of the Company at a consideration of HK\$49.8 million. Immediately after the acquisition, the shareholding of Mr. Chau Cham Wong, Patrick, Mr. Leung Yung and EganaGoldpfeil (Holdings) Limited were 10.18%, 10.00% and 6.50% respectively.

During the year, the Company carried out a capital reorganisation (the "Capital Reorganisation") whereby the paid-up capital and nominal value of all the issued shares were reduced from HK\$0.10 to HK\$0.005 each by cancellation of HK\$0.095 paid up capital on each issued share and every 20 issued shares of HK\$0.005 were consolidated into one share of HK\$0.10 each.

On 6 June, 2002, the Company proposed to raise equity capital by way of rights issue. The net proceeds of the proposed rights issue of HK\$63 million are intended to be used as follows:

- about HK\$24 million for establishing a distribution arm in the United States;
- about HK\$10 million for promoting the Group's licensed products through the distribution arm aforementioned;
- about HK\$20 million for developing its distribution network in the PRC; and
- the remaining balance for the use as the general working capital of the Company.



MANAGEMENT DISCUSSION AND ANALYSIS

FUNDING AND TREASURY POLICIES

The principle of the Group's treasury policy is to manage the Group's assets and liabilities so as to reduce its exposure to fluctuation in foreign exchange and interest rates.

In the normal course of business, the Company enters into certain derivatives contracts in order to hedge its exposure to fluctuations in interest rates and foreign currencies. These instruments are executed with creditworthy financial institutions. Gains and losses on these contracts are applied to offset fluctuations that would otherwise impact the Company's financial results. Costs associated with entering into such contracts are not material to the Company's financial results.

Over 90% of the Group's borrowings were in Hong Kong Dollars with the balance in Renminbi and US Dollars. It is the Group's treasury policy to manage its foreign currency exposure whenever its financial impact is material to the Group.

As at 31 March, 2002, all of the Group's borrowings were at floating rates with approximately HK\$251 million of borrowings were hedged by the interest rate swaps.

The Company had entered into currency-linked deposit contracts to manage its foreign currency risk. As at 31 March, 2002, the US dollar based currency-linked deposits were amounted to US\$2.2 million in total. The alternative currency of those contracts is Euro currency. The purposes of entering into these contracts are for both currency hedging and yield enhancement.

MATERIAL ACQUISITION

An agreement dated 18 September, 2001 pursuant to which Peace Mark (B.V.I.) Limited, a wholly-owned subsidiary of the Company agreed to acquire 45% of the issued share capital of Capricon Company Limited (which in turn 100% owns Capricon Industrial (Shenzhen) Company Limited) from Goldpfeil Aktiengesellschaft, a subsidiary of EganaGoldpfeil (Holdings) Limited. After the acquisition, the Group has a 100% equity interests in Capricon Company Limited.

SECURITIES INVESTMENT

As a continuation of strategy in focusing the resources in the core business, the remaining portfolio of investment in securities had been disposed of during the year and a realised loss of HK\$10.8 million was included in other operating expenses. There will be no significant impacts on either equity reserve or profit and loss in the following accounting periods as the remaining portfolio investment at the year end date was insignificant.



MANAGEMENT DISCUSSION AND ANALYSIS

CAPITAL EXPENDITURE

Capital expenditure for 2002 amounted to HK\$83.8 million which consist primarily of improvement of production facilities, acquisition of plant and machineries and a trademark. The Group will incur more capital expenditure in developing its global distribution network in coming years.

ORDERS ON HAND

Orders on hand of the Group in the course of the year has been approximately 2-3 months which is in line with industry norm.

NUMBER OF EMPLOYEES AND REMUNERATION POLICY

As at 31 March, 2002, the Group employed a total of approximately 1,300 employees worldwide.

The Group remunerates its employees based on their performance, experience and prevailing industry practice. In addition, the Group has established discretionary bonus and employees share options scheme which are designed to motivate and reward employees to achieve the Company's business performance targets.

CONTINGENT LIABILITIES

As at 31 March, 2002, the Group had contingent liabilities in respect of bills discounted with recourse amounting to approximately HK\$179.7 million.

The Company has given corporate guarantees to banks in respect of general banking facilities granted to subsidiaries amounting to HK\$816.0 million. The extent of such facilities utilised by the subsidiaries at 31 March, 2002 amounted to approximately HK\$195.0 million.

FINANCIAL INSTRUMENTS

The Company had entered into interest rate swaps to manage its interest rate risk. At 31 March, 2002, the total notional amount of such instruments was HK\$201 million. The notional amounts of the outstanding interest rate swaps indicate the contract size outstanding at the balance sheet date and do not represent the amount at risk.

The Company had entered into currency-linked deposit contracts to manage its foreign currency risk. As at 31 March, 2002, the US dollar based currency-linked deposits were amounted to US\$2.2 million in total. The alternative currency of those contracts is Euro currency.

