

Management Discussion and Analysis

During the year, the Group continued to focus on the distribution of Polyurethane ("PU") materials and the manufacture and sales of PU foam and related products. The Group's audited turnover and net profit attributable to shareholders for the year ended 31 March 2002 (the "Year") were approximately HK\$518 million and HK\$9 million, respectively, representing decrease of approximately 23% and 79%, respectively, over the corresponding period in 2001. Earnings per share for the Year stood at HK4.5 cents (2001: HK28.0 cents).

Distribution business

The deterioration of the global economy which was further aggravated by the September 11 tragedy happened in the United States. Our customers became cautious about replenishing their inventories due to the uncertainties in consumer demand and decided to reduce their orders in the second half of the Year. Although the principal market of the Group remained The People's Republic of China (the "PRC") (excluding Hong Kong) where the demand for PU materials is still growing, the sluggish demand for the PU materials in the United States market has led to the result of oversupply in the global market. Therefore the growth in demand in China has been overwhelmed by this excessive supply of PU materials. Moreover, it gave rise to more intensified market competition that resulted in extra pressure on PU materials prices and sales were achieved at the expense of leaner margins. During the Year, revenue from the distribution of PU materials was approximately HK\$405 million, down from approximately HK\$570 million of last year. The distribution business contributed approximately HK\$10 million to the Group's net profit from operating activities for the Year, representing approximately a 76% decrease in comparison to last year.

Manufacturing business

During the Year, the Group continued to focus on the development of its downstream products, PU foam and related foam products. Revenue from the Group's manufacturing business during the Year still showed a steady growth from approximately HK\$100 million in 2001 to approximately HK\$114 million in this Year. Unfortunately, under the tough business environment in Hong Kong and the world market, the Group has experienced an increase in the level of provision for doubtful debts. In addition, inventories worth approximately HK\$3 million was written off mainly due to the sudden cancellation of orders by certain customers. The manufacturing business recorded a disappointing operating profit of approximately HK\$5 million, representing a decrease of approximately 60%. However, the Group will be cautious about credit control and will continue to adopt an effective cost control policy in order to boost both sales and operating profit.

LIQUIDITY AND FINANCIAL RESOURCES

The Group generally finances its operations with internally generated cash flow and facilities provided by its principal bankers in Hong Kong. During the Year, the cash generating ability of the Group remained strong, with approximately HK\$7 million being generated from operating activities. The Group recorded a net cash inflow of approximately HK\$40 million, which raised the total cash and cash equivalents to approximately HK\$43 million as at the balance sheet date. The Group's cash and cash equivalents are mostly held in Hong Kong dollars. Approximately HK\$8 million of the Group's time deposits was pledged to secure the general banking facilities.

LIQUIDITY AND FINANCIAL RESOURCES *(continued)*

The Group's bank borrowings are made in Hong Kong dollars, such borrowings bear interest at floating lending rate. As at 31 March 2002, the Group had no bank borrowings (2001: approximately HK\$39 million). As at 31 March 2002, the net book value of the Group's fixed assets held under finance leases amounted to approximately HK\$524,000. Finance lease payables of approximately HK\$224,000 were repayable within one year. The remaining finance lease payables of approximately HK\$313,000 were repayable within five years. All of the Group's borrowings are denominated in Hong Kong dollars and US dollars.

As at 31 March 2002, the Group had a gearing ratio of zero (defined as long term bank borrowings over shareholders' equity). Net current assets at 31 March 2002 was approximately HK\$94 million and current ratio was maintained at a healthy level of approximately 188%. As the Group's transactions are mostly settled by Hong Kong dollars or Hong Kong dollars pegged currencies, no use of financial instruments for hedging purposes is considered necessary.

With the available resources and the proceeds from the new issue and placing of shares of the Company, the Group has adequate working capital to finance its business operations.

CONTINGENT LIABILITIES

The Company had executed several guarantees, with unlimited amount, in favor of banks in respect of general banking facilities granted to certain subsidiaries. As at 31 March 2002, the subsidiaries had utilised approximately HK\$41 million of the facilities.

EMPLOYEES

As at 31 March 2002, the Group's total number of staff in Hong Kong and the PRC was 41. Salaries of employees are maintained at a competitive level. The Group has not encountered any problem with the recruitment of its employees. None of the companies in the Group has experienced any labor disputes during the Year and the Directors of the Company consider that the Group has maintained an excellent employment relationship.

USE OF PROCEEDS

The shares of the Company were listed on The Stock Exchange of Hong Kong Limited on 19 April 2001. After deduction of necessary expenses payable by the Company, the net proceeds amounted to approximately HK\$37.5 million. The Directors at present applied the net proceeds as follows:—

- approximately HK\$6.0 million was used for the purchase of new machinery and equipment for the new production facility;
- approximately HK\$2.5 million was used for marketing activities of PU materials and PU foam products produced by the Group; and
- approximately HK\$5.5 million was used as additional working capital of the Group.

The Group has placed the unused balance of the net proceeds of approximately HK\$23.5 million with licensed banks in Hong Kong, which will be applied for according to the intended uses as set out in the Company's prospectus dated 30 March 2001.