

# MANAGING DIRECTOR'S OPERATIONAL REVIEW



## INTRODUCTION

This year is our seventh straight year to achieve double digit growth in operating profit. This was achieved in spite of the persistent deflationary pressure with record high unemployment in Hong Kong and difficult economic conditions globally.

The unprecedented economic difficulties and continuous corporate downsizing in Hong Kong caused rising unemployment and substantial contraction in the retail and restaurant business. Due to influx of new entrants, the restaurant number actually surged by an astounding 2,233 units during the period of 1998-2001 to 10,899 units in 2001. This has created an extremely competitive environment.

The Group boldly faced these challenges and firmly attached to our proven business philosophy through the implementation of innovative business and operational strategies. Key focused was in balancing the value equation to our customers, driving up productivity and developing new business growth drivers. With this, we successfully sustained our long-term profitability in this extremely challenging time.

## FAST FOOD BUSINESS

**Café de Coral** fast food business continued its strong foothold in Hong Kong. As of 31st March, 2002, there were 117 **Café de Coral** quick service restaurants in operation. During the year, **Café de Coral** opened 8 new restaurants in the prime locations of Tsimshatsui, Kwun Tong and North Point districts for providing convenient food services to our target customers. These new shops generated immediate profit contribution to the Group.



While our competitors concentrated in short term price only competition, **Café de Coral** focused on a strategy that enhances customer value and builds strong brand equity. This included introducing innovative product with high perceived value at an affordable price in the dinner segment, re-packaging popular items into value meals to serve our frequent customers during lunch segment and launching various short-time "special promotion products" to create short-term market noisiness and generate customer visits.

We have successfully re-negotiated favourable purchasing and rental terms with our suppliers and landlords respectively. During the year, we invested HK\$18 million to upgrade and expand the central

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kitchen which resulted substantial improvement in the production lead time and production cost. Saving from these initiatives provided more rooms to adjust our price without hurting bottom line.

In the shop front, we have invested over HK\$32 million to renovate 15 **Café de Coral** shops for enhancing the dining experience to our customers. We also provided new trainings to our front line staff under a “100% customer satisfaction” program.

To further strengthen **Café de Coral** brand, we initiated an enlightening advertising campaign “See You in Café de Coral” with a light-hearted theme to capture the targeted audience attention and proven successful after launching. With all these marketing initiatives and campaigns, **Café de Coral** fast food was able to sustain our profitability and enhance our “most preferred brand” ranking during the year.

**Super Super Congee and Noodles** delivered a promising return within the management expectation during the year. Two new outlets were opened in two major shopping malls in Tuen Mun and Tin Shui Wai which enable this new concept to further penetrate into the mass market. With



this experience gained, the management believe that this brand will capture more patronage and has great potential to develop into a sizable chain in the years to come.

## INSTITUTIONAL CATERING

As of 31st March, 2002, **Asia Pacific Catering** managed 40 operating units in Hong Kong and Southern China, which include, 21 units in the health-care sector, 7 units in the educational sector and 12 units in the commercial manufacturing sector.



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Tong and Tai Wai being in full operation in addition to its 3 existing facilities, management expects **Luncheon Star** to pave a solid new income stream to the Group in future.

### SPECIALTY RESTAURANT

**The Spaghetti House** continued to perform well amid the severely competitive environment. During the year, 2 new outlets were opened at Matheson Centre, Causeway Bay and Metroplaza, Kwai Fong.

During the year, **Asia Pacific Catering** further won two new catering contracts in the education sector to provide catering services to Hong Kong University of Science & Technology and St. Stephen's Girls College. In the health-care segment, a new contract was signed with Ruttonjee Hospital. After the year end, we have signed up three new catering service contracts with Open University of Hong Kong, Queen Elizabeth Hospital and Hong Kong Science Park respectively.

In the Southern China, institutional catering business progressively established its presence with a total of 4 operating units in Shenzhen and Guangzhou. We continue to explore future business development opportunities in the Southern China and to expand our business presence in this market.

Our student catering business, **Luncheon Star**, has been performing satisfactorily during the year. With the existing production facilities having been upgraded and 2 new reheating centers at Kwun

Continuous efforts have been focused on new shop image and new menu development. Customer feedback on these two areas is encouraging and positive, resulting in increased patronage and enlarged customer base. Apart from this, the brand image of **The Spaghetti House** was further strengthened through launching of a new television advertising campaign which projected a trendy and stylish image.

**The Spaghetti House** was elected as **"The Top 3 Most Popular Dining Venues"** among competitors as per the research undertaken by Hong Kong Polytechnic University in 2001. Being recognized for its service standard, **The Spaghetti House** was awarded the **"Quality Service Award"** by *Hong Kong Tourism Board*.

Management continues exploring the opportunities to franchise **The Spaghetti House** in the South East Asia region and in the PRC. This expedition

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has well been encouraged by the successful experience in opening 5 franchise stores in Indonesia and our recent entry to the China market. The first **The Spaghetti House** franchise restaurant in PRC, will be opened in Beijing, by the end of this year.

**Ah Yee Leng Tong** continued to consolidate and another under-performing store was closed during the year. With the remaining 2 **Ah Yee Leng Tong** restaurants located in the prime tourist districts of Tsimshatsui and Cityplaza, the **Ah Yee Leng Tong** brand still attract customer visit, particularly the tourists, albeit in the competitive environment.

**Bravo le Café** has been gradually solidifying its position as an appealing quick service restaurant concept over the years since we first introduced this house-owned brand in 1997. A large variety of Chinese, Japanese and Western cuisines have been served in our existing 4 **Bravo le Café** restaurants during the year.

The Group continued its expansion of its specialty restaurant business in Hong Kong and launched an upscale new concept restaurant named **Bistro M** in April, 2002. This cosmopolitan styled restaurant, located at Metroplaza, Kwai Fong, is an ideal place for business and social dining. Initial



response is overwhelming as it does fill up a long outstanding market void in the area.

### SCANFOODS

The performance of **Scanfoods** has been steady and healthy during the year. This proven business demonstrated its ability to generate consistent profit contribution to the Group after acquisition in 1997. **Scanfoods** expanded its product line by developing smoked bacon and various kinds of sausage and extended its distribution channels to hyper-market in China.

A new extension has been under construction next to the existing premises in Dongguan to expand the food processing plant catering for in-house consumption and outside customers. The new capacities will replace some of the more labor intensive production processes currently operating in Hong Kong as well as to cope with the increasing demand in China.

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### CAFÉ DE CORAL IN THE PRC AND MACAU

The performance in this market has been most encouraging. As of 31st March, 2002, there were 5 operating units in Southern China and 1 unit in Macau. This year marked the first year of profit making in each and every **Café de Coral** outlets in the PRC. The strategies on marketing, pricing, product and



localization of the management and purchasing team finally pay off. During the year, we have renovated 2 outlets. The improved environment enhanced the dining experience of our customers and brought in extra sales.

After investing and learning for the past 10 years, our existing **Café de Coral** in PRC already operated profitably during the year. We believed that we have successfully developed a viable operating business model in the PRC and with confidence to resume our expansion program by development new outlets in the South China region.

### MANCHU WOK & CHINA INN

Acquisition of **Manchu Wok** has been proven very successful and has delivered the planned cash flow

to the Group immediately after acquisition with earnings before interest, tax, depreciation and amortization amounts to approximately HK\$36 million.

To further widen the business horizon in North America, we have recently acquired a 20 Asian restaurant chain operating under the brand name of **China Inn, Oishii Kitchen** and **Dai Bai Dang**. The acquisition was made through a joint venture entity with the same partnership and shareholding of an about 48% equity interest as the Group's existing joint venture company, Manchu Wok Enterprises Inc. The total consideration of the acquisition amounted to C\$20.7 million, which was partly satisfied by internal funds and largely financed by debts financing. Following the acquisition, **Café de Coral Group** will have a sizable platform of over 200 restaurant units in North America.

Through the acquisition of **China Inn**, we have successfully expanded our geographical coverage to the major cities in California, including Los Angeles, San Francisco and Sacramento. **China Inn** and **Oishii Kitchen**, which operated under similar mode as in **Manchu Wok**, will be assimilated to the **Manchu Wok** system in due course. **Dai Bai Dang**, on the other hand, presented a new growth opportunity in the fast casual full service sector. Currently there is 1 **Dai Bai Dang** operating in Fresno, California since 1999 and the Group is planning to roll this concept out in year 2003.

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During this year, **Manchu Wok** has initiated a development plan for a stand alone street store concept and the first store will be opened by the end of year 2002 in new market, Ontario. Through acquisition and internal development of new concept restaurant, **Manchu Wok** has developed into a sizable scale, with multiple restaurant concepts and brands for expansion in the future.

### NEW BUSINESS PROCESSES

With a total expected investment of HK\$65 million, the Group's Business Process Re-engineering project reached its final phase and will gradually be integrated into our existing operating system in coming months, for enhancing productivity and information efficiency.

Drawing on the latest broadband IP network technologies and communication infrastructure, together with leading-edge hardware and software products with regard to database server, application servers, and touch-screen POS terminals, all our restaurant outlets have now been seamlessly integrated to interface with the Head Office.

Such a robust, flexible and user-friendly system would mean all critical business information exchange, including sales and marketing, inventory, accounting, human resources, menu changes, ordering and even delivery schedules, can now be instantly, accurately and timely transmitted between branches and Head Office in a private, secure and reliable environment.



### STRATEGIC PROPERTIES HOLDINGS

During the year, the Group completed the purchase of shops at Admiralty Centre, Harcourt Road at the purchase price of HK\$58 million. This acquisition of the property at strategic location with proximity to MTR station, commercial centers and shopping malls

strengthened the real estate portfolio of the Group housing its **Café de Coral** fast food operation. Such investment will bring along decent return to the Group, both on a rental yield and operating yield at a combined return of more than 14%. After this acquisition, the Group currently owns 18 properties for our restaurant use.



### FINANCIAL REVIEW

As of 31st March, 2002, the Group's total borrowings was HK\$230 million and maintained a healthy gearing (being total borrowings over shareholders' funds) of 16%. The loan maturity profile spread over a period of 3 years with HK\$150 million repayable within one year.

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The Group had given guarantees totally approximately HK\$861 million as of 31st March, 2002 to financial institutions in connection with their loans granted to the subsidiaries and jointly-controlled entities.

### HUMAN RESOURCES

As of 31st March, 2002, the Group employed 7,500 employees. Remuneration packages are generally structured by reference to market terms and individual qualifications and experience. With a unique Employee Share Option Scheme together with profit sharing bonus and performance incentive system, employees are allowed to share in the growth of the Group.

During the year, various training activities have been conducted to improve the front-end services quality as well as to ensure the smooth and effective implementation of the Group's Business Process Re-engineering project.



### CONCLUSION

Management anticipates the retail business environment continues to be very challenging in 2002. The Group will strive to sustain its dominant market position by delivering innovative and value-added products with quality service to our customers. We will reiterate our commitment to improve our product range and quality, customer services, rendering differentiated catering services to our customers who always support us in good or bad time. Apart from these, we will continuously leverage on our strong cash flow and balance sheet to continuously grow our new business and to look for new acquisition opportunities in the PRC and North America. With a well defined business strategy to diversify, our business portfolio shall be more balanced, leading us to deliver consistent business growth in future.

**Lo Hoi Kwong, Sunny**

*Managing Director*

Hong Kong, 9th July, 2002