

MANAGEMENT DISCUSSION AND ANALYSIS

FINANCIAL HIGHLIGHT

To facilitate better understanding of the Group's performance, the comparison presented below covered 12-month period ended 31 December 2002 and 2001.

- Total turnover: HK\$1,364.9 million
- Net profit attributable to shareholders: HK\$102.5 million
- Net profit before revaluation deficit: HK\$177.5 million
- Earnings per share: HK6.02 cents
- Earnings per share before revaluation deficit: HK10.42 cents
- EBITDA: HK\$256.7 million
- EBITDA margin: 18.8%

The Group's consolidated operating results for the year ended 31 December 2002 and 2001 were as follows:

(HK\$ million, except per share amounts)	For the year ended 31 December		% change
	2002	(Restated) 2001	
Turnover	1,364.9	1,693.7	(19.4)
Operating cost before depreciation and amortisation	1,108.2	1,306.3	(15.2)
EBITDA	256.7	387.4	(33.7)
Depreciation and amortisation	79.0	88.1	(10.3)
Finance cost	1.1	0.6	83.3
Gain on disposal of long-term investment shares	-	22.8	(100.0)
Gain on disposal of businesses	25.1	-	100.0
Provision for asset impairment	-	72.5	(100.0)
Revaluation deficit	75.0	40.7	84.3
Other revenue	8.8	25.3	(65.2)
Operating profit	135.5	233.6	(42.0)
Net profit attributable to shareholders	102.5	165.7	(38.1)
Earnings per share (HK cents)			
Basic	6.02	9.55	(37.0)
Diluted	N/A	9.55	N/A

For the year ended 31 December 2002, the Group's turnover and profit attributable to shareholders amounted to HK\$1,364.9 million (2001: HK\$1,693.7 million) and HK\$102.5 million (2001: HK\$165.7 million), respectively. Earnings per share was HK6.02 cents (2001: HK9.55 cents), calculated based on the weighted average of 1,704,448,053 shares in issue during the year (2001: 1,734,160,257 shares). The Company bought back (and cancelled) 173,438,400 shares in October 2002, and the number of shares in issue as at 31 December 2002 were 1,560,945,596 shares.

The reported earnings of HK\$102.5 million included a gain of HK\$25.1 million from disposal of certain businesses and a provision of HK\$75 million for deficit in revaluation of the investment properties. Excluding the investment properties revaluation deficit, the Group would report a net profit of HK\$177.5 million, or an earnings per share of HK10.42 cents.

The Group's total revenue in 2002 was down 19.4% from the previous year, primarily due to the downturn in advertising revenue from the newspaper business and disposal of certain businesses. The entertainment, recreation and education businesses were substantially ceased or disposed of in 2001 and early 2002; these operations accounted for HK\$155.5 million of the Group's turnover in 2001, compared with HK\$15.3 million in 2002. Excluding the turnover from the entertainment, recreation and education businesses, the Group's turnover in 2002 was down 12.3% from the previous year.

Operating Costs and Expenses

HK\$ million	For the year ended 31 December		% change
	2002	(Restated) 2001	
Staff costs	417.2	477.7	(12.7)
Cost of production materials and sales	427.6	499.0	(14.3)
Rental and utilities	98.0	143.3	(31.6)
Advertising and promotion	31.4	37.2	(15.6)
Other operating expenses	134.0	149.1	(10.1)
Operating cost before depreciation and amortisation	1,108.2	1,306.3	(15.2)
Depreciation and amortisation	79.0	88.1	(10.3)
Total operating costs and expenses	1,187.2	1,394.4	(14.9)

Total operating costs were down by 14.9%. Staff costs decreased by 12.7% following from headcount reductions undertaken during the year. Total headcount of the Group in December 2002 was 1,293, down from 1,570 in December 2001 due to disposal and suspension of certain businesses and magazine titles, and overall reduction of headcount. Cost of production materials and sales was down 14.3% primarily due to lower newsprint prices and usage. The average cost of newsprint for production decreased by 26.4% to HK\$3,853 (US\$494) per ton. Rental and utilities decreased by 31.6% due to disposal of recreation club and education businesses and the closure of nine *Health Plus* stores, though this was partially offset by net increase of 11 *Daily Stop* outlets. Advertising and promotion and other operating expenses decreased by 15.6% and 10.1%, respectively, due to various cost cutting measures, though offset by an increase in distribution costs related to *Jiu Jik* being distributed in the MTR network from July 2002.

Contribution by Business Segment

The Group's core business of newspapers, magazines and other publications continued to generate the majority of the Group's turnover, EBITDA and operating profit.

HK\$ million	Contribution to Turnover For the year ended 31 December		% change
	2002	2001	
Newspapers, magazines and other publications	831.8	1,014.1	(18.0)
Retailing	418.6	414.5	1.0
Investment properties	79.7	77.3	3.1
Video and film post-production	19.5	32.3	(39.6)
Entertainment, recreation and education services	15.3	155.5	(90.2)
Total	1,364.9	1,693.7	(19.4)

HK\$ million	Contribution to EBITDA For the year ended 31 December			Contribution to Operating Profit For the year ended 31 December		
	2002	(Restated) 2001	% change	2002	(Restated) 2001	% change
Newspapers, magazines and other publications	176.1	283.8	(37.9)	109.8	192.6	(43.0)
Retailing	1.3	3.1	(58.1)	(1.6)	(0.4)	300.0
Investment properties	76.4	71.5	6.9	17.2	25.4	(32.3)
Video and film post-production	(0.5)	5.0	(110.0)	(3.8)	2.1	(281.0)
Entertainment, recreation and education services	3.4	24.0	(85.8)	13.9	13.9	-
Total	256.7	387.4	(33.7)	135.5	233.6	(42.0)

Newspapers, magazines and other publications

HK\$ million	For the year ended 31 December		% change
	2002	(Restated) 2001	
Turnover			
Newspapers	742.0	925.4	(19.8)
Magazines and others	89.8	88.7	1.2
Total turnover	831.8	1,014.1	(18.0)
EBITDA	176.1	283.8	(37.9)
Operating profit	109.8	192.6	(43.0)

For the year ended 31 December 2002, this division recorded revenues of HK\$831.8 million, a decrease of 18%. Revenues have come under extreme pressure in these times as companies continue to reduce costs and expenses, especially in marketing and advertising areas, and the volatile and weak stock markets continue to restrict corporate and fund raising activities. Recruitment advertising is still being severely affected by the high unemployment rate in Hong Kong.

Display advertising revenue in the newspapers decreased by 9.7%, average yield also decreased slightly offset by the increase in average volume. Advertising revenue in *Classified Post* declined 35.9%, average volume was down by some 28.6% and average yield also decreased.

The average circulation of *South China Morning Post* and *Sunday Morning Post* recorded a decline in 2002 year-on-year. Circulation for January – June 2002 of the *South China Morning Post* was 104,406 copies (January – June 2001: 110,155), and for the *Sunday Morning Post* was 90,868 copies (January – June 2001: 92,353). Circulation for July – December 2002 for the *South China Morning Post* was 104,484 copies (July – December 2001: 114,028) and for the *Sunday Morning Post* was 81,719 copies (July – December 2001: 89,204). The continuing weak economy has impacted circulation sales. Hotel and airlines subscriptions have recovered since the tragic events of 11 September 2001, but subscription sales from agents and newsstands have declined as Hong Kong is faced with record level of redundancies and closure of small businesses and offices. We are confident, however, that circulation sales will recover when the economy improves, as we have seen similar decline during the Asian financial crisis and subsequent recovery thereafter.

Revenues from magazines and other publications for the year ended 31 December 2002 remained stable. The operating profit was lower due to losses incurred by *CosmoGIRL!*, which was launched in September 2001.

Retailing

HK\$ million	For the year ended 31 December		% change
	2002	2001	
Turnover	418.6	414.5	1.0
EBITDA	1.3	3.1	(58.1)
Operating loss	(1.6)	(0.4)	300.0

This division recorded revenues of HK\$418.6 million, an increase of 1% year-on-year. The operating loss of HK\$1.6 million was due to losses incurred in the *Health Plus* business, the *Daily Stop* operations are profitable. During the year, nine unprofitable *Health Plus* shops were closed and as at the end of 2002, 18 shops were in operation. As at the end of 2002, there were 83 *Daily Stop* outlets compared with 72 in December 2001.

Investment properties

HK\$ million	For the year ended 31 December		% change
	2002	2001	
Turnover	79.7	77.3	3.1
EBITDA	76.4	71.5	6.9
Operating profit	17.2	25.4	(32.3)

Rental income and EBITDA from the Group's investment properties increased due to new leases in 2002, though slightly offset by a lease expiry. Operating profit of HK\$17.2 million was after adjusting for (i) a receipt of HK\$15.9 million from an investment written off in prior years; and (ii) a provision of HK\$75 million for diminution in value of the investment properties. HK\$65 million of the provision relates to the TV City property. This property is currently leased to TVB as film studios at HK\$70.6 million per annum, and the lease will expire in December 2003. The professional property valuers had valued the property on existing use basis as at 31 December 2002.

The Company has received an in-principle approval from the Town Planning Board to change the land use of TV City to a "Comprehensive Development Area (2)", thus permitting a development involving principally uses for residential purposes. The Draft Clear Water Bay Peninsula North Development Permission Area Plan (the "Plan"), which indicates the zoning of the land upon which the TV City is situated, was gazetted on 22 March 2002, and was opened to public objections for a period until 22 May 2002; following which the objections have been considered by the Town Planning Board. The Plan, together with the un-withdrawn objections, has been submitted to the Chief Executive in Council for approval. In the meantime, the Company has revised the master layout plan to comply with Government's latest requirements and has submitted it to the Town Planning Board for approval, to be followed by, inter alia, submission of an application and the subsequent execution of a Land Exchange, which includes the assessment and negotiation of land premium. Based on the advice of consultants, the process is likely to take some 18 months.

Video and film post-production

HK\$ million	For the year ended 31 December		% change
	2002	2001	
Turnover	19.5	32.3	(39.6)
EBITDA	(0.5)	5.0	(110.0)
Operating (loss) / profit	(3.8)	2.1	(281.0)

This division recorded revenue of HK\$19.5 million with an operating loss of HK\$3.8 million. The poor performance was mainly due to reduction in documentary tape income.

Entertainment, recreation and education services

HK\$ million	For the year ended 31 December		% change
	2002	2001	
Turnover	15.3	155.5	(90.2)
EBITDA	3.4	24.0	(85.8)
Operating profit	13.9	13.9	-

The operations of this division had substantially ceased with the disposal of the recreation club and education businesses and suspension of the production operation of the entertainment business. The operating profit of the education business included a gain of HK\$11.2 million resulting from the disposal of the business in March 2002.

Capital Expenditure

Total capital expenditure for the year ended 31 December 2002 amounted to HK\$61.7 million, of which HK\$12.1 million was spent on replacement items and HK\$49.6 million on new capital items. Of the new capital items, HK\$23.7 million was spent on partial payment for the editorial and Oracle financial systems and HK\$23.6 million on final payment for the two Geoman colour presses. The remaining new capital expenditures represented investment in new *Daily Stop* outlets and computer hardware and software.

For the coming year, the Group has approved capital expenditure of approximately HK\$79 million, of which HK\$64.1 million is allocated for (i) replacement of the editorial, advertising and circulation systems, (ii) 15 new *Daily Stop* outlets, (iii) video-film production equipment, and (iv) computers and technology related equipment and software. The balance of HK\$14.9 million is allocated for replacement items.

Liquidity and Capital Resources

Net cash provided by operating activities was HK\$255.9 million for the year ended 31 December 2002, compared with net inflow of HK\$587.7 million in the 18-month period ended 31 December 2001. Cash was used primarily for payment of dividends, taxation and capital expenditures.

Net cash outflow from financing activities was HK\$384.8 million for the year ended 31 December 2002, compared with net outflow of HK\$830.7 million in the 18-month period ended 31 December 2001. During the year, the Company repurchased a total of 173,438,400 shares. The total consideration was approximately HK\$629.4 million (including expenses) and was funded by internal cash and HK\$310 million in bank borrowing.

Cash generated from the Group's operations and the funds available from external sources are expected to be adequate to cover all cash requirements, including working capital needs and planned capital expenditure.

As at 31 December 2002, the Group had bank borrowing of HK\$310 million. The bank borrowing is a Hong Kong Dollar unsecured term loan repayable within 3 years and has floating interest rate. The Group has no significant exposure to foreign exchange fluctuations.

The ratio of current assets to current liabilities was 2.07 times as at 31 December 2002 compared to 2.95 times as at 31 December 2001. As at 31 December 2002, the gearing ratio of the Group was 11.1 % (2001: nil) calculated by dividing the total borrowings of HK\$310 million (2001: nil) net of available cash of HK\$139 million by shareholders' funds of HK\$1,537.2 million.

Defined benefit plan's assets

The Group has adopted a new accounting standard, HKSSAP34 "Employee Benefits" in 2002. This standard requires the Group to recognise the surplus on its defined benefit plan as assets in its balance sheet and charge the cost of providing the defined benefit plan benefits to profit and loss accounts systematically. The defined benefit plan's assets recognised as at 31 December 2002 was HK\$37.9 million (2001: HK\$42.4 million) and the cost of providing the defined benefit plan benefits for the year ended 31 December 2002 was HK\$4.5 million (2001: HK\$2.7 million).