

Business Review

Introduction

2002 remained a year marked with operating difficulties. The tinplating operation was dampened by the trade-war in the international steel market and the State's implementation of provisional protection measures for certain category of imported steel plates. The raw steel market experienced dramatic changes and the market of the imported raw steel plates saw keener competition. Affected by the State's policies on deregulating pond fish quota management and reducing quota for livestock agencies; outbreak of Avian influenza in February and the opening up of the chilled chicken market in December, the turnover of the live and fresh foodstuffs operation dropped significantly. Infectious diseases affected livestock farming and live pigs exported and sold decreased notably. Under such a difficult business environment, the Group promptly adjusted its business strategy and decisively took the initiative to apply to the State for exemption from provisional protection measures and obtained it towards the end of 2002. The Group increased the purchases of imported raw steel plates from countries not involved in anti-dumping, scaled up production and sales of products with higher profit margin and sales of live and fresh foodstuffs under non-policy agency, implemented effective measures on prevention and cure of epidemics of livestock. Thanks to these measures, related operational risks were reduced and satisfactory results were achieved. Most of the economic indicators of the Group in 2002, except for the turnover which was slightly decreased, were remarkably improved as compared to those of the same period of 2001. Cost of sales decreased by HK\$93,059,000 or 5.6%. Gross profit increased by HK\$56,729,000 or 36.5%. Distribution costs decreased by HK\$60,051,000 or 52.4%. Administrative expenses decreased by HK\$10,956,000 or 14.9%. There is a big turnaround in operating profit and share of profits of associates. Operating profit increased by HK\$117,294,000. Share of profits of associates increased by HK\$22,796,000. Profit before tax increased by HK\$114,504,000 or 920.8%. Profit attributable to shareholders increased by HK\$63,991,000 or 124.2%. Basic earnings per share increased by HK0.67 cents or 109.8%. At present, the Group is in a good assets backing condition, with sufficient financial resources, and a healthy operation with comparatively improved profit yield.

Tinplating and Property Leasing

In 2002, amidst dramatic changes in the raw materials market with fierce competition from imported steel plates, and while final arbitration over provisional protection measures is still pending, the Group had, in response to the situation, taken active measures to explore alternative material-importing channels, heightened production and sales of higher profit margin electroplated ferrochrome products. These measures proved effective and the production, sales and profit recorded significant increase. In 2002, the production and sales of tinplating electroplated ferrochrome totalled 111,157 tons, an increase of 18,052 tons or 19.4% over those of 2001. Average product sales gross profit margin improved from 16.7% in 2001 to 21.6% in 2002, an increase of 4.9%. The newly acquired business remained buoyant, and for the year ended 31 December 2002 contributed HK\$565,906,000, or 31.7% of turnover and HK\$85,708,000, or 67.5% of pre-tax profit, and became the Group's core business, a major growth driver and profit contributor.

Property leasing recorded a total revenue of HK\$28,372,000 for 2002, an increase of 6.2% as compared to that of 2001. In order to leverage land resource to develop industrial property leasing, the Group invested HK\$8,740,000 into the construction of the second phase plants of Rugu, Zhongshan with total gross floor area of 1,230 m². The project was completed in July 2002 and the properties were leased out during the year.

Feed Production

Guangnan (Zhan Jiang) Jiafeng Feed Co. Ltd., the Group's wholly owned subsidiary, possesses an annual production capacity of 200,000 tons of poultry feed. In 2002, the Group overhauled the management of the company, restructured its product mix, transformed the shrimp feed production line, discontinued certain loss-making poultry feed products and focused on high value-added types of fish and shrimp feed products, resulting in continued improvement of both the operation quality and economic benefits despite the decrease in production and turnover of 37.8% and 28.1% respectively as compared to those of 2001.

The Group's feed processing operation is situated at Zhanjiang, Guangdong Province. As the aquatic food industry in Zhanjiang and the coastal areas in Hainan and Beihai, Guangxi Province are prospering, growth potential and prospect is expected within the aquatic feed market.

Live and Fresh Foodstuffs Distribution

The live and fresh foodstuffs distribution operation is the Group's traditional business. Following the PRC's accession to the World Trade Organization, the State deregulated quota management in pond fish and reduced quota for livestock agencies in January 2002. Outbreak of Avian influenza in February and the opening up of the chilled chicken market in December exacerbate the business condition further. Faced with the rapid deterioration in the business operating environment, the Group strived to maintain its performance as a policy regulated agency and, simultaneously, increasing its non-policy regulated agency business by expanding direct sales in quality live-chicken. By way of reducing headcounts and effective cost control, we managed to enhance profits and minimize the drop in turnover. Consequently, the live and fresh foodstuffs operation recorded a turnover of HK\$977,642,000 in 2002, a decrease of HK\$283,030,000 or 22.5% over that of the same period of 2001; operating profit of HK\$14,602,000, a decrease of HK\$2,957,000 or 16.8% over that of the same period of 2001.

In order to safeguard the traditional live and fresh foodstuffs distribution operation to meet the ever changing market competition, the Group, by analysing the past, the present and the future trend of the business, formulated a series of measures such as building up an effective incentive mechanism, expanding non-policy regulated agency business, identifying strategic partners, establishing commodity production base, broadening marketing network, and exploring new frozen poultry business and etc. These measures are designed with an aim to lay a strong foundation for the ongoing development of this operation after the State fully deregulated live and fresh foodstuffs quota management.

Foodstuffs Trading

In addition to the original business of trading in foodstuffs like frozen food, rice, starch, egg powder and etc, the Group strived to develop new business such as chilled chicken, feed and the like. In 2002, the trading of foodstuffs recorded a turnover of HK\$69,626,000, an increase of HK\$24,281,000 or 53.5% over that of the same period of 2001.

The Group succeeded in supplying the first consignment of chilled chicken to Hong Kong as Hong Kong opened up its chilled chicken market in December 2002. The turnover of that month was HK\$3,350,000. Currently, the Group has become Hong Kong's major supplier of chilled chickens which are being sold in all major supermarkets and chain stores. Trading of chilled chicken will become the major business of foodstuffs trading operation.

MANAGEMENT DISCUSSION AND ANALYSIS

Livestock Farming

Performance of the Group's livestock farming operation in 2002 had been sluggish due to infectious diseases and reduced selling price of live pigs in the mainland. Turnover of the three pig farms was HK\$50,177,000, a decrease of HK\$12,384,000 or 19.8% as compared to that of the same period last year; operating loss was HK\$5,463,000, an increase in the loss of HK\$3,888,000 or 246.9% as compared to the same period last year.

The Group's livestock farming operates mainly in Dongguan City, Guangdong Province, where the pigs-farming environment deteriorates due to urban planning and development. High-infected rate of pigs associated with the present industry downturn constitutes high operating risks. As a result, the Group will, after examination and demonstration, scaled down this operation, or, even change the operation mechanism to transfer or lease out the pig farms when the time is right.

Financial Position

As at 31 December 2002, the Group's total assets amounted to HK\$963,053,000 and total liabilities stood at HK\$448,066,000, an increase of HK\$4,729,000 and a decrease of HK\$136,889,000 respectively when compared with the position as at the end of 2001. The net current assets of the Group increased from HK\$33,848,000 as at the end of 2001 to HK\$73,049,000 and the current ratio (current assets divided by current liabilities) increased by 10.9%. The Group's financial position has strengthened further since the end of last year, indicating a steady move towards improving results and paving the way for future business expansion.

Liquidity and Financing Resources

As at 31 December 2002, the Group maintained cash balances of HK\$243,010,000, increased by 6.6% from the cash balances as at the end of 2001. The major cash outflow was for the early redemption of HK\$105,000,000 interest-bearing convertible notes.

The Group's interest-bearing borrowings are repayable on demand and carry interest at annual rates ranging from 6.5% to 7.6%. At the end of the year under review, the Group's interest-bearing borrowings together with the convertible notes totalled HK\$139,012,000. Accordingly, the Group's gearing ratio, which was measured on the basis of the Group's total interest bearing borrowings and convertible notes over the shareholders' fund, was 28.1%, representing a sharp decrease of 53.8% from 81.9% as at 31 December 2001.

MANAGEMENT DISCUSSION AND ANALYSIS

One of the Group's subsidiaries in the PRC has secured an additional banking facility for letters of credit of US\$4,000,000 in the second half of the year after securing credit of US\$6,000,000 in the first half of the year, of which US\$6,300,000 was utilized at the end of this year. With its cash holdings, recurring cashflow from its operations and available banking facilities, the Group believes that it will have sufficient funds to meet its present operation requirements and to further develop its business in the foreseeable future.

Charges on Group's Assets

As mentioned in the annual report of the Company for the year ended 31 December 2001, certain land & buildings of a 51%-owned subsidiary in the PRC, namely Dongguan Guangnan Stock Development Co. Ltd. (the "Subsidiary"), with gross carrying amount of HK\$10,369,000, have been pledged to a bank for a loan of HK\$8,476,000 granted to a minority shareholder of the Subsidiary. A provision of HK\$10,369,000 was made in previous years' financial statements.

Convertible Notes

On 3 December 2001, the Company issued convertible notes of HK\$185,000,000 to Richway Resources Limited, a fellow subsidiary of the Company, as part of the consideration for the acquisition of Zhongyue Industry Material Limited. The notes bear interest at a fixed rate of 4.5% per annum and are convertible into ordinary shares of the Company on any business day other than the period in which the register of members of the Company is closed or ten business days prior to the maturity date on 3 December 2006 at an initial conversion price of HK\$0.155 per share. During the year, a total of HK\$105,000,000 convertible notes were redeemed by the Group on 21 June, 14 August and 8 November 2002 respectively, in order to reduce interest expense thereof. As at the date of this report, the outstanding portion was of HK\$80,000,000.

Exchange Rate Exposure

The Group's assets, liabilities and transactions were primarily denominated either in Hong Kong dollars, US dollars or Renminbi. As the exchange rates of Hong Kong dollars, US dollars or Renminbi were relatively stable during the year, the Group was not exposed to significant exchange risk.

Employees and Remuneration Policies

As at 31 December 2002, the Group has a total of 808 employees, reduced by 71 as compared to the same period of 2001, of whom 49 were based in Hong Kong and 759 were based in the PRC. The staff remuneration is determined in accordance with the responsibility for the post, workload, individual performance and prevailing industry practice. In 2002, the Group implemented control on the total salary and effectively reduced the labour cost through re-determining the staffing, headcount and total salaries of each subsidiary. At the same time, the “performance bonus” incentive scheme assessed the performance of the subsidiaries based on the profit before taxation achieved and rewarded the management, key personnel and outstanding staff with bonus of a designated proportion. This incentive scheme activated and mobilized the work enthusiasm of the broad ranks of staff members.

Future Prospect

Looking ahead in 2003, the operation environment is still exceptionally challenging. The live and fresh foodstuffs distribution operation is gradually losing its policy advantages as China enters the World Trade Organisation, the recent relapse of the Avian influenza and the outbreak of Atypical Pneumonia will expect to dampen the business further. Livestock farming is dwindling due to changes in the market situation. However, opportunities exist where there is challenge. The management believes that if we can carry out the objective of “enhancing the quality of the management team and innovative operating systems, integrating business structures to create synergy, developing flagship businesses to increase our competitiveness”, and if we can maintain our strength in existing enterprises and businesses while we continue to nurture and develop our leading business, expedite the improvement of tinplating technology in order to boost productivity and market competitiveness, accelerate business structure reform, aggressively identify investment opportunities and then to acquire projects with potential, we can definitely enhance the Group’s overall economic strength, profitability and competitiveness, and eventually accelerate the growth of the Company.