RESTAURANT OPERATION

The results of the restaurant operation, including inter-company transactions with the bakery operation, are summarised as follows:

	2003	2002	**Changes**
	HK$'000	*HK$'000*	***%***
Turnover	**465,256**	567,756	(18.1%)
Other revenues	**7,323**	8,705	(15.9%)
Costs of inventories consumed	**(140,193)**	(164,617)	(14.8%)
Staff costs	**(163,389)**	(198,725)	(17.8%)
Operating lease rentals	**(52,026)**	(65,004)	(20.0%)
Depreciation of fixed assets	**(22,288)**	(26,016)	(14.3%)
Other operating expenses	**(96,603)**	(106,395)	(9.2%)
Amortisation of intangible assets	**(195)**	(26)	650.0%
One-off expenses incurred on restaurant closures	**(17,717)**	–	n/a
Impairment and revaluation deficit of properties	**(36,720)**	(2,530)	1,351.4%
Impairment loss of goodwill	**(10,067)**	–	n/a
Operating (loss)/profit	**(66,619)**	13,148	(606.7%)
Share of net losses of associated companies	**(783)**	(290)	170.0%
(Loss)/profit before taxation	**(67,402)**	12,858	(624.2%)
Taxation	**(423)**	(3,589)	(88.2%)
(Loss)/profit after taxation	**(67,825)**	9,269	(831.7%)
Shop area – sq. ft. at year end	**179,000**	246,000	
No. of outlets at year end	**22**	27	

Performance of our restaurant operation deteriorated this year. Compared to last year, we had closed Rainbow Room and Hong Fook Chinese Restaurant ("Hong Fook"), which led to a significant drop in turnover and overall operating expenses. Apart from that, we also incurred a few substantial charges of exceptional nature relating to revaluation of our property portfolio.

In addition to closure of Rainbow Room and Hong Fook, we carried out renovation for seven shops in total of which three were not re-opened until the coming financial year. During the renovation period, which on average last five weeks or so, we closed the shops temporarily and it inevitably dragged our turnover down. Besides, average customer spending also shrank by about 3% from HK$70 to HK$68 per head this year. All these factors jointly contributed to the decline in turnover by 18.1%.

Faced with the price war, we must offer more food variety at lower prices in order to maintain our market share. With the support of our business partners and the creativity of our chefs, we launch year-round promotional campaigns to lure customers with less traditional menu items and greater discounts. The discounts hurt our gross margin which dropped from 71.0% to 69.8%.

RESTAURANT OPERATION *(continued)*

Other revenues comprised of interest income and management fee income dropped by 15.9%. Deposit interest rate stayed at extremely low level throughout the year. We ceased to receive management fee income from our associated company when its four restaurants were closed at various times during the year.

Other than restaurant closures, we managed to reduce our operating expenses through cost saving measures. We renegotiated better lease terms with landlords while further savings were made on staff costs which accounted for 34.4% (2002: 35.4%) of our operating expenses. We reduced our accrual for staff leave by about HK$4.3 million at 31 March 2003 from making flexible leave arrangement with our employees during shop renovation periods. Besides, only the staff of profit-making restaurants were rewarded with the year-end discretionary bonus as opposed to across-the-board payments in the previous year had reduced our total outlay in this area. Offset such savings in staff costs, we had to provide about HK$2.5 million additional provision for long service payments with reference to the valuation performed by a professional actuary. Our net savings in labour costs for the year was about 17.8%.

We incurred one-off expenses from restaurant closures. Other than HK$17.7 million which included compensation paid to landlord, severance and termination wages and write off of fixed assets, we transferred HK$10.1 million to the profit and loss account from our reserve for impairment loss in goodwill as such goodwill was previously written off to reserve at the initial acquisitions of these restaurants.

In view of the significant drop in pedestrian flow in Lam Tin after the commencement of Tseung Kwan O line of the Mass Transit Railway, we wrote down the value of our property portfolio in Sceneway Plaza by HK$36.7 million bringing the cumulative write-down amounts at 31 March 2003 to 37% of the original costs of this property.

The associated company, Arges Limited ("Arges"), ceased operation during the year after we had resolved with our joint venture partner to dissolve this company. We will proceed with voluntary liquidation of Arges in the next financial year. Our share of the losses of Arges was more than offsetting the profit from another associated company which is operating a Japanese restaurant chain.

BAKERY OPERATION

The results of the bakery operation, including inter-company transactions with the restaurant operation, are summarised as follows:

	2003	2002	**Changes**
	HK$'000	*HK$'000*	***%***
Turnover	**494,492**	476,189	3.8%
Other revenues	**1,639**	2,645	(38.0%)
Costs of inventories consumed	**(143,508)**	(134,497)	6.7%
Staff costs	**(155,765)**	(163,099)	(4.5%)
Operating lease rentals	**(50,091)**	(51,427)	(2.6%)
Depreciation of fixed assets	**(28,623)**	(25,644)	11.6%
Other operating expenses	**(83,532)**	(75,088)	11.2%
Amortisation of intangible assets	**(4,600)**	(4,600)	0.0%
Revaluation deficit of property	**(4,586)**	–	n/a
Profit before taxation	**25,426**	24,479	3.9%
Taxation	**(6,897)**	(4,279)	61.2%
Profit after taxation	**18,529**	20,200	(8.3%)
Shop area – sq. ft. at year end	**69,000**	66,000	
No. of bakeries at year end	**74**	69	
No. of eateries at year end	**2**	2	

The turnover of the core bread and cake business increased by 5.6% due to extensive promotion effort and higher discount offered to customer. Turnover of festive product increased by 2.7% was resulted from the introduction of new products such as "Snowy" mooncakes and the use of celebrities "Twins" to market our products. Turnover of eatery business reduced by 6.3% due to World Cup Soccer and the SARS effect.

Gross margin was reduced by 0.8% due to more discounts offered to customers but was partially offset by cost savings made on sourcing of raw materials.

Staff costs dropped by 4.5% mainly resulted from migration of certain secondary production lines to Shenzhen.

Rental charge slightly decreased by 2.6% despite increase in number of outlets and it was achieved by successful negotiation with landlords for rental reduction.

Depreciation increased by 11.6% mainly due to the additional capital expenditure incurred for migration of production lines to Shenzhen and renovation of outlets to improve brand image.

The increase in other operating expenses was caused by increase in marketing expenses to promote our products, initial setup costs incurred for migrating the production lines to Shenzhen and pre-operating expenses to expand the Guangzhou retail outlets.

LIQUIDITY AND CAPITAL RESOURCES

Despite the reported loss and an annual capital outlay of approximately HK$49.7 million, our operation still returned a small positive cash flow for the year. At 31 March 2003, freely-held cash on hand amounted to HK$203.0 million (2002: HK$200.3 million). The Group's financial position stays healthy with zero gearing. The Group's approved capital commitments in the next financial year is estimated to be about HK$40.6 million, mainly for upgrading the remaining aged shops. These projects will be financed internally and we do not have immediate need for external fund raising.

EMPLOYEES

At 31 March 2003, the Group had a total of 2,849 (2002: 2,843) full time employees. Employees are remunerated based on basic salaries and sales incentives are payable to some operational staff. Bonuses were discretionary in nature and based on the performance of the employees and the Group. The Company and its listed subsidiary, Saint Honore Holdings Limited ("SHHL"), each adopted their own share option schemes, details of which are set out in the section headed "Share Options" in the directors' report.

PLEDGE OF ASSETS

No assets were pledged as at 31 March 2003.

EXPOSURE TO FLUCTUATIONS IN EXCHANGE RATES AND RELATED HEDGES

The Group's activities are primarily denominated in Hong Kong Dollars. There is no significant exposure to foreign exchange fluctuations.

CONTINGENT LIABILITIES

The Group had no significant contingent liabilities as at 31 March 2003.


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