



LUNG KEE (BERMUDA) HOLDINGS LIMITED

MANAGEMENT DISCUSSION AND ANALYSIS

Business Review

The outbreak of SARS that afflicted the Asian region had slight negative effect on the Group's sales turnover in the second quarter of this year. However, the Group still recorded a satisfactory growth in its overall performance in the first half year.

As the newly expanded plants in China started to operate and with the help of more matured labors, the productivity of both the Heyuan and Dongguan plants in China had been further enhanced, showing great improvements on its products quality and production effectiveness. The Guangzhou factory, located in Guangzhou Free Trade Zone, devotes to produce high precision mould base for overseas clients. Owing to the growing awareness of LKM brand, sales orders from overseas market maintained steady growth.

The second phase development of the Shanghai plant, China had just been completed; and machineries had been well installed. Overall productivity of the plant is continuously strengthened, ready to accommodate further business growth in the Eastern Region in China.

Due to the decline of the mould industry in Singapore, the Group's small-sized factory in Singapore had been restructured into a regional sales office. Its production had been merged with the plant located in Malaysia, for more effective co-ordination and management.

Despite the unfavorable domestic environment in Japan, the Group's business in Japan still achieved constant growth, in terms of its market share and turnover, attributed to its widely accepted LKM brand in the Japan market.

The plant in Taiwan operates smoothly with incessant growth in productivity and sales turnover, further boosting the business development of the Group.

The imported mould steel business faced keen market competition on price. Nevertheless, positive growth in the sales of newly promoted quality steel from China, to a certain extent, compensated the dwindling demand of imported mould steel.



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Prospects

Following China's accession to the WTO, worldwide manufacturers rush into China for direct investment and setting up new production plants. China has further reinforced its position as "The Global Manufacturing Center". Coupled with the economic boom in the domestic market, demand for plastic consumers goods has substantially increased. Looking ahead, the Group is highly optimistic towards its future developments.

The newly expanded plant in Heyuan, China concentrates in the production of large size mould base for the automobile industry, catering for the growing demand of such products in the market. On the other hand, the construction of the new supporting plant in the Zhejiang Province will be completed at the beginning of next year, and will start production in the middle of next year. It aims at providing quality mould bases for privately owned enterprises in that area, further enhancing the Group's business in China.

The Group will put considerably effort in widening its distribution networks with an aim to extend its sales contacts covering all major industrial cities in China. Through closer and direct contacts with customers, the Group can grasp local business opportunities efficiently. For the Eastern region of China, the Group has gradually set up sales offices in the Zhejiang Province and the Jiangsu Province, capturing the vast market opportunity in that region. Turning to the Guangdong Province, sales points and offices have been opened up continuously in those customer-intensive cities in order to offer more direct, intimate and prompt services to privately owned enterprises in that area.

Regarding the mould steel business, the Group commits to launch a wide variety of technical services, to fortify its sales on imported quality steel. Owing to the continued improvement on the quality of steel manufactured by China special steel factories, the Group will, through stringent quality control process, carefully select and market a wide range of quality China mould steel, matching needs of the more price-conscious customers. The parallel development of both imported quality steel and China quality steel products will offer more choices for customers and will sharpen the competitiveness of the Group.

The Group will further develop its value-added services to the customers. In addition to six-sides machining, vacuum heat treatment and mould repairing services, the Group will provide Physical Vapor Deposition (PVD) coating services to customers. Through different types of hard coating, the performance of mould components and machinery parts can be substantially enhanced due



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to the improvement in wear resistance, lubrication and corrosive resistance characteristics. The installation of the PVD system will be completed at the end of this year and service will be available at the beginning of next year, providing a more comprehensive "one-stop services" to customers.

Liquidity and Financial Resources

As at 30th June, 2003, the Group had cash balance of approximately HK\$621 million. Most of the cash balance was placed in HKD and USD short term deposits with major banks in Hong Kong.

Total debts of the Group were approximately HK\$828 million, equal to approximately 103% of shareholders' funds of approximately HK\$803 million.

Employees and Remuneration Policies

As at 30th June, 2003, the Group employed a total of approximately 5,400 employees, including approximately 5,000 employees in its PRC production sites and approximately 400 employees in Hong Kong and other countries. The Group adopts a competitive remuneration package for its employees. Promotion and salary increments are assessed based on a performance related basis. Share options may also be granted to staff with reference to the individual's performance.