



Comprehensive Financial Services

Management Discussion and Analysis



OVERVIEW

During the year under review, Hong Kong's economy has reached its lowest level in decades, plagued by unseen high unemployment rates, world wide recession and weak investment sentiment. The situation was further compounded by the SARS outbreak. However, the Group's strategic plan of becoming a comprehensive financial services group in Hong Kong was gradually bearing fruit, although it was hindered by the general weak economy both local and overseas. With stringent cost control measures and the determination of management and staff, the Group managed to record a modest profit even under this challenging business and economic environment.

Japan has been operating its TGE and TOCOM since 1952 and 1984 respectively and is recognised as the second largest commodity futures market in the world. The Group is the largest broker for Japanese commodity futures in Hong Kong in terms of trading volume. Over the years, Tanrich and the Japanese commodity futures market have grown together in expanding the commodity futures market in Hong Kong. Nevertheless, due to the sluggish economy, turnover of TGE futures in Hong Kong for the year ended 30th June 2003 dropped to 237,781 contracts as compared to 369,740 contracts for the corresponding period in 2002. However, Tanrich still maintained its leading position, which preponderated 80% of market share of TGE futures in Hong Kong in terms of trading volume for the year ended 30th June 2003.

OPERATION REVIEW

For the year ended 30th June 2003, the Group recorded a decrease in turnover of 21.5%, from HK\$161.3 million to HK\$126.7 million. Profit from operating activities declined by 66.8% to HK\$12.9 million from HK\$38.9 million while profit attributable to shareholders declined by 66.3% to HK\$10.2 million as compared to the last year's corresponding period of HK\$30.3 million. Despite the decrease in profit, the Group was actually one of the few local financial services companies that managed to achieve a profit in this difficult business environment.

Shareholders' fund declined by 3.4% to HK\$106.4 million as compared to last year's HK\$110.2 million. For the year ended 30th June 2003, basic earnings per share was HK5.1 cents. The underneath is a detailed description of the Group's main business activities in the past year.



FUTURES

For the financial year under review, the Group's futures business contributed to 93.5% of its total turnover. The Group's turnover of TGE futures decreased to 190,898 contracts as compared to 334,556 contracts for the same period in 2002, while turnover of its TOCOM futures increased to 30,470 contracts as compared to 20,406 contracts for the same period in 2002. Despite the challenging operating environment, the Group managed to maintain its unrivaled market leadership position in Japanese commodity futures market in Hong Kong.

During the year under review, the Group has also increased its efforts in expanding business in the US commodity and currency futures market. For the financial year, turnover in the US commodity and currency futures market increased to 75,233 contracts as compared to 7,210 contracts for the same period in 2002, representing a growth of 9.4 times. The turnover from the US commodity and currency futures market is expected to grow gradually in the coming years and bring in encouraging profit for the Group.

The Group strives to maintain its market niche in the futures segment in Hong Kong by recruiting more professionals and experts and holding regular trainings for the Group's account executives with an aim to provide excellent customer services.

SECURITIES BROKING AND MARGIN FINANCING

Cost reduction measures were implemented during the year. An unprofitable branch was closed and staff number of these business was reduced. Overheads were down significantly. Due to the sluggish stock market for most part of the year and the implementation of fully negotiable brokerage commission in April 2003, the securities broking operation performed about the same as compared to last year. Securities broking recorded HK\$3.6 million in turnover as compared to last year's HK\$3.9 million and represented a slight decrease of 7.7%.

Securities margin financing achieved a turnover of HK\$2.1 million as compared to the corresponding period in 2002 of HK\$1.5 million, which represented an increase of 40%. Following last year's strategy, the Group will focus its business on institutional, corporate and high value clients. The Group always maintains a prudent and conservative margin financing policy and a strict control on margin lending in an effort to control the risk level while better protecting its customers. For the year under review, securities broking and margin financing contributed to 4.5 % in aggregate to the Group's total turnover.



ASSET MANAGEMENT

Wealth management has grown to become a main focus for people from every walk of life. Investors utilise asset management to diversify their investment portfolio as well as to protect and manage their assets. The Group distributes over 1,000 funds, including global equity, fixed income, forex and derivatives, etc., that are managed by over 30 international asset management companies. In addition to providing financial planning services and insurance-linked products, the Group continuously launches new products to cater for customer needs. During the year under review, the Group's asset management business contributed to 3.9% of the total turnover and reached HK\$4.9 million, which represented 2.5 times of last year's HK\$2.0 million.

CORPORATE FINANCE

The Group's corporate finance business commenced its operations in 1999, offering financial services including financial advisory, fund raising, underwriting and sub-underwriting as well as placement activities. In the latter part of the year, a team of competent corporate financial professionals had been recruited with a plan to further expand the business.

Due to the stagnant capital market and weak investment sentiment for most part of the year, the operation generated a turnover of HK\$145,000 for the year as compared to HK\$844,000 of last corresponding period, which represented a decrease of 82.8%. Nonetheless, the capital market should definitely be on an increasing trend in the coming year and turnover in this operation should hence bounce back and improve considerably.

INTERNAL CONTROL AND RISK MANAGEMENT

The Group has stipulated a prudent strategy in internal control and risk management. In today's volatile financial markets, prudent control procedures and stringent internal controls are indispensable key success factors. During the year, the Group has allocated consistent time, efforts and resources in minimising the Group's risk exposure and maximising returns to customers and shareholders.

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RISK CONTROL COMMITTEE

The committee, comprising of members of the Board of Directors, the financial controller of the Group, the manager of legal and compliance department of the Group has been established to develop and implement business risk minimisation policies and procedures so as to confine business risks, formulate credit and risk control policies and procedures of Tanrich Securities Company Limited ("TSCL"), an indirect wholly-owned subsidiary of the Company.

CREDIT CONTROL COMMITTEE

Comprising of members of the Board of Directors, the financial controller of the Group and the sales director of TSCL, the main task of the Credit Control committee is to administer the credit and control policies and procedures formulated by the risk control committee.

LIQUIDITY, FINANCIAL RESOURCES AND GEARING RATIO

In addition to the proceeds from the Company's initial public offering ("IPO") last year, the Group's operations have generated stable and adequate internal cash flow for working capital of the Group. As at 30th June 2003, the Group had cash on hand and bank balances that totalled to HK\$62.8 million (2002: HK\$74.7 million), while net current asset amounted to HK\$76.4 million (2002: HK\$87.2 million). The strong liquidity of the Group is manifested in the current ratio, as a ratio of current assets to current liabilities, of 2.0 times which showed improvement over last year's 1.8 times.

Due to the Group's healthy and strong financial position, the Group minimised its bank borrowings and used internal cash to fund its operations. As at 30th June 2003, the Group had no bank borrowings (2002: HK\$0.2 million, repayable on demand) which resulted in zero gearing ratio (2002: 0.2%). The gearing ratio was calculated by dividing the Group's total borrowings by its total equity.

As at 30th June 2003, the Group had aggregate banking facilities of HK\$101 million, composing of HK\$85 million, the draw down of which is subject to the pledged value of marketable securities, and HK\$16 million general banking facilities, as compared to HK\$86 million in year 2002.



LIQUIDITY, FINANCIAL RESOURCES AND GEARING RATIO *(Continued)*

These banking facilities were secured by clients' pledged securities, certain non-trading investments of the Group, corporate guarantees issued by the Company and its subsidiaries. All the banking facilities were denominated in Hong Kong dollars and based on commercial floating interest rates. There were no seasonal factors in our borrowing requirements.

SIGNIFICANT INVESTMENTS

During the financial year, the Group acquired 1,089,000 listed securities of BOC Hong Kong (Holdings) Limited at HK\$8.5 per share for long-term investment. As at 30th June 2003, together with 1,306,000 listed securities of Hong Kong Exchanges and Clearing Limited on hand, the aggregate fair value of these securities amounted to HK\$23.2 million (2002: HK\$16.8 million), which represented an increase of 38.1% over last year's corresponding period. An unrealised loss of HK\$3.0 million was recorded in the Group's investment revaluation reserve during the financial year ended 30th June 2003 as a result of further decline in the Hong Kong stock market, compared to last year's unrealised loss of HK\$1.4 million.

MATERIAL INVESTMENTS

As far as practical and up to the date of this analysis, the Group has not planned any major investments or acquisition of capital assets in the foreseeable future.

CHARGE ON GROUP ASSETS

Marketable securities with an aggregate value of HK\$14.6 million (2002: HK\$10.3 million) were pledged as collateral for banking facilities. These marketable securities were beneficially owned by subsidiaries of the Company.

CONTINGENT LIABILITIES

As at 30th June 2003, the Company has undertaken to guarantee the banking facilities of HK\$100.5 million granted to two of its subsidiaries. The banking facilities were applied in their normal courses of business activities.



CONTINGENT LIABILITIES *(Continued)*

A subsidiary of the Company has received a claim for compensation in respect of disputed trades. As the arbitration proceedings are at a preliminary stage, it is not currently possible to estimate the eventual outcome of the claim and based on legal advice to date, the directors consider that no provision needs to be made in the financial statements.

FOREIGN EXCHANGE AND CURRENCY RISKS

The Group has exposure to foreign exchange fluctuation as a result of placing margin deposit in Japanese Yen with two designated futures commission merchants in Japan on behalf of its clients in Hong Kong. According to the Group's hedging policy, the Group hedges at least 80% of its net foreign exchange exposure with USD/JPY foreign exchange deferred trading in order to minimise foreign exchange risk.

During the year, the Group's total margin deposit placed with the two designated futures commission merchants was 696 million Japanese Yen and had a bank deposit of 192 million Japanese Yen, total Japanese Yen being equivalent to HK\$57.7 million. This amount was hedged with USD/JPY foreign exchange deferred trading equivalent to an aggregate amount of US\$6.5 million, which representing 87.8% of the Group's net foreign exchange exposure (2002: 88.6%).

USE OF PROCEEDS FROM IPO

Following the successful listing of the Company's shares on the Main board of the Stock Exchange of Hong Kong Limited (the "SEHK") on 30th January 2002, the net proceeds of the Share Offer, after deduction of related expenses, amounted to HK\$37 million. We have used the listing proceeds as follows:

HK\$15 million was applied in acquisition of new issued shares of TSCL to expand the Group's securities broking and share margin financing business;

**USE OF PROCEEDS FROM IPO** *(Continued)*

HK\$10 million was applied in acquisition of new issued shares of Tanrich Capital Limited ("TCL"), an indirect wholly-owned subsidiary of the Company to expand the Group's corporate finance business;

HK\$5 million was applied in acquisition of new issued shares of Tanrich Asset Management Limited ("TAML"), an indirect wholly-owned subsidiary of the Company to expand the Group's asset management and insurance broking business;

The balance of HK\$7 million was loaned by the Company to TSCL as working capital.

STAFF

As at 30th June 2003, the Group had a total of 200 full time employees. The Group operates different remuneration schemes for account executives and other supporting and general staff. Account executives are remunerated on the basis of on-target-earning packages comprising base pay or draw, commission and/or bonus. Other supporting and general staff are offered basic salary and year-end discretionary bonuses subject to the business results of the Group. Employees' remuneration excluding directors' emoluments amounted to HK\$55.1 million for the year (2002: HK\$71.1 million). The Group ensures that the remuneration paid to its employees is competitive and employees are rewarded within the general framework of the Group's salary and bonus system. The Group also provides training programmes for the staff to enhance their skills and products, regulatory and compliance knowledge.



OUTLOOK

Financial year 2002-2003 was a difficult year for most companies in Hong Kong, but the Group still recorded a modest profit. This clearly demonstrated our strength and competitiveness. In the coming year, Tanrich will not only strive to maintain its leading position in the Japanese commodity futures market but to step up its effort in the US commodity and currency futures market, as well as expand business in corporate finance, securities broking and asset management.

In addition, Tanrich will constantly reinforce the quality of internal control measures to minimise risk exposure and will keep pace with the advancement in information technologies in order to enhance information systems that can improve the overall efficiency and customer service standards.

With a competent and visionary management team and the continuous recruitment of experts and professionals, the Group is well equipped to ascend to higher horizons and consolidate itself as a comprehensive financial services group in Hong Kong.