

## MANAGEMENT DISCUSSION AND ANALYSIS

### RESULTS

The Group continued to maintain operating profit in its first-half results for 2003. For the six months ended 30th June 2003, the Group achieved profit attributable to shareholders of approximately HK\$10.2 million, representing a slightly decrease of 1.9% as compared with the profit attributable to shareholders of approximately HK\$10.4 million in the same period in 2002. The Group's turnover amounted to approximately HK\$174 million as compared with the turnover of HK\$190 million in 2002. The decrease in the turnover was mainly attributable to the drop in turnover contributions from the supply chain management business during the period under review.

### REVIEW OF OPERATIONS

Despite the outbreak of SARS during the period, the Group struggled to sustain the operating profit. As regard to the restructuring of its business operations, the Group adjusted its CD business operation from CD replication to CDR stampers production in view of the high production costs of CD replication in Hong Kong and the declining price of CD. It can reduce the negative impact of this business segment on the Group's operating profit. The restructuring of CD business operation has been completed and the profit margin of CD operation will be ameliorated in the second half of this year. The Group plans to commence the business of CDR mastering by the fourth quarter this year.

With the serious impact of the SARS epidemic, which broke out in the PRC during the period under review, the Group's distribution business was adversely affected. However, by expanding the products range and further developing new distribution channels, the distribution business continued to contribute revenue to the Group during the period. Besides, business in the PRC has gradually rebounded with the ending of the SARS outbreak in the region.

Besides, suppliers of conventional media products such as floppy disks gradually stopped their production lines following market consolidation of these products. As such, the customers of these suppliers shifted to our Group to demand conventional products. This also helps to maintain the Group's profitability.

The sales contribution from the Asian markets (including the PRC) reached to HK\$134 million and increased from 56.5% to 77.3% in the first-half of 2003. The sales contribution from Europe markets dropped by 3.3% to approximately HK\$33 million while the sales contribution from the United States markets further dropped by 14.1% to approximately HK\$7 million.

### **DISTRIBUTION OF MEDIA PRODUCTS**

The distribution business segment continued to generate revenues for the Group during the reporting period. Turnover recorded an approximate 39% growth increasing from approximately HK\$36 million to approximately HK\$50 million due to the increase in variety of its products and the addition of more sub-distributors.

The distribution business was adversely affected by the outbreak of the SARS epidemic during the period under review. However, business in the PRC has gradually rebounded with the ending of the SARS outbreak in the region due to the strong sales base of this business segment.

To increase future sources of revenue for this business segment, the Group will continue to expand the distribution network with minimal operating cost.

## **COMPUTER MEDIA AND ACCESSORIES PRODUCTION AND TOTAL FULFILMENT SERVICES**

Sales of computer media and accessories production and total fulfillment services amounted to approximately HK\$124 million, representing a decrease of 18% as compared with the same period last year.

The drop in sales of this segment was mainly attributable to the discontinuance of the supply chain management business. However, the addition of new customers to increase the demand of the floppy disks from the Group had compensated the shortfall in revenue contribution from supply chain management business.

Revenue from total fulfillment services business operation became minimal due to the slack economy in the United States and the outbreak of SARS in the Asian region. The remaining major issue related to this business segment is the arbitration proceedings against a major customer by the Group's wholly owned subsidiary.

## **PROSPECTS**

The Group continues to diversify its business into service segments such as distribution and retail businesses with minimum capital expenditure. To enhance this profitability, it plans to continue to extend its distribution business including improving the product range. In addition, it will further restructure the organization and trim down operating costs.

The Group will improve the product range by launching a new product called CDR stampers in the fourth quarter of the year. The new products will be manufactured in Hong Kong and distributed through the Group's well-established distribution channels.

In view of a number of uncertainties ahead, such as the possible outbreak of SARS in the coming future, the continuous slack economy in some European countries and the United States, the Group will adopt a very conservative approach to operate the Group's business segments to avoid any potential business risk in the second half of this year.

Meanwhile, in order to pursue growth in operating revenues, the Group continues to strengthen our sales networks in overseas markets, to stay aware of the economic recovery in the US market and tighten operating cost control to achieve profitable returns for shareholders. In consideration of further costs to be incurred for the arbitration against a major customer, the Directors do not recommend the payment of an interim dividend so as to retain sufficient funds to finance the future development of the arbitration.

## FINANCIAL REVIEW

### *Capital and debt structure*

The Group continued to maintain a healthy financial position. As at 30th June 2003, the Group's total net assets was approximately HK\$242 million (31st December 2002: HK\$232 million), representing an increase of HK\$10 million mainly attributable to operating profit during the period.

As at 30th June 2003, the Group's total bank borrowings and obligations under finance leases notably dropped by HK\$20 million to HK\$136 million (31st December 2002: HK\$156 million). Total short-term bank loans and overdrafts of the Group decreased by HK\$26 million from HK\$134 million as at 31st December 2002 to HK\$108 million as at 30th June 2003 albeit the Group's total long-term bank loans slightly increased by HK\$6 million to HK\$28 million (31st December 2002: HK\$22 million). Most of the bank borrowings are denominated in Hong Kong dollars and subject to floating interest rates. Therefore, the risk of currency exposure was minimal. The Group's total cash and bank balances amounted to HK\$43 million (31st December 2002: HK\$41 million), representing an increase of HK\$2 million.

The Group's net debt to equity ratio, which is expressed as a percentage of total bank borrowings and obligations under finance leases after deducting cash and bank balances over the total net assets, was further ameliorated by 11% to 39% as at 30th June 2003 (31st December 2002: 50%). The considerable decrease in this ratio was primarily attributable to tremendous repayment of bank borrowings and plough-back of operating profit during the period.

The Group had unutilized banking facilities of approximately HK\$221 million as at 30th June 2003 (31st December 2002: HK\$239 million), which is considered sufficient to satisfy the working capital requirement.

#### *Working capital and liquidity*

As at 30th June 2003, the Group continued to have good working capital. Primarily resulted from the re-classification of convertible notes of HK\$39.6 million from non-current liabilities into current liabilities, current ratio slightly deteriorated by 0.09 to 1.08 (31st December 2002: 1.17) whereas quick ratio merely decreased to 0.7 (31st December 2002: 0.8). Receivable turnover improved to 20 days (31st December 2002: 42 days) which was a results of continuous effort on collection of receivables. Inventory turnover increased to 73 days (31st December 2002: 67 days) due to the piling up of inventory for sales orders in the second half of this year and the increase in products range and sales networks for the distribution business. The Group will struggle to reduce the inventory level to sustain a healthy liquidity position in the second half of this year.

#### *Convertible Notes*

On 5th January 2001, the Group issued four interest-free convertible notes for the acquisition of distribution and logistic business.

A convertible note of HK\$32.7 million is convertible in part or in whole into new shares of the Company, at the conversion price of HK\$0.55 per share, at any time during the period commencing 18 months from the date of issue on 5th January 2001 to, but excluding, the third anniversary from the date of issue (the "Maturity Date"). To the extent that this convertible note has not been previously converted, it will be redeemed on the Maturity Date at the then outstanding principal amount provided that the Company has the option to call on the holder to convert this convertible note on the same date wholly into new shares of the Company.

The other three convertible notes, each having a principal amount of HK\$2.3 million, are convertible in part or in whole into the new shares of the Company, at the conversion price of HK\$0.55 per share, at any time during the period commencing 12, 24, and 33 months from the date of issue respectively up to but excluding the Maturity Date. To the extent that the three convertible notes have not been previously converted, the convertible notes will be redeemed on the Maturity Date at the then outstanding principal amounts.

As at 9th September 2003, the holder of two convertible notes, each having a principal amount of HK\$2.3 million, requires the Company to convert the whole of the principal amount outstanding under these convertible notes into share of the Company at HK\$0.55 per share. A total of 8,360,000 shares will be allotted and issued to the holder upon the exercise of the conversion rights under two of the convertible notes by the holder. Given the issue of new shares of the Company to the holder and the increase in the Group's net assets value after the conversion of these convertible notes, the Group's gearing and net debt to equity ratios will likely be improved at the year-end date. Press announcement will be made after the allotment and issue of new shares of the Company to the holder as soon as practicable.

**Ho Yin King, Helena**  
*Chairman*

Hong Kong, 23rd September 2003