

The Directors submit their report together with the audited accounts for the year ended 31 March 2004.

## Principal activities and geographical analysis of operations

The Company continues to be an investment holding company. The principal activities of its subsidiaries are the manufacture and sales of toys and moulds.

An analysis of the Group's turnover, revenue and segment information is set out in Note 2 to the accounts.

## Results and appropriations

The results of the Group for the year are set out in the consolidated profit and loss account on page 29.

The Directors have declared an interim dividend of HK0.75 cents per ordinary share, totalling HK\$3,628,000, which was paid on 15 January 2004. The Directors recommend the payment of a final dividend of HK0.75 cents per ordinary share, totalling HK\$3,628,000.

## Reserves

Movements in the reserves during the year are set out in Note 22 to the accounts.

## Donations

Donations made by the Group during the year amounted to HK\$106,000.

## Fixed assets

Details of the movements in fixed assets are set out in Note 13 to the accounts.

## Information on subsidiaries

Particulars of the subsidiaries are set out in Note 14 to the accounts.

## Share capital

Details of the movements in share capital of the Company are set out in Note 21 to the accounts.

## Five year financial summary

The following is a summary of the consolidated results, assets and liabilities of the Group for each of the last five years ended 31 March 2004, based on the audited accounts of the Group and restated for the adoption of the revised Statement of Standard Accounting Practice No. 12 "Income Taxes" ("revised SSAP 12") which is effective for accounting periods commencing on or after 1 January 2003.

### Five year financial summary (continued)

In accordance with the revised SSAP 12, deferred taxation is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the accounts. This change in accounting policy has been applied retrospectively so that the comparatives presented for each of the four years ended 31 March 2000, 2001, 2002 and 2003 have been restated to conform to the changed policy.

	<b>2004</b> <b>HK\$'000</b>	2003 HK\$'000 Restated	2002 HK\$'000 Restated	2001 HK\$'000 Restated	2000 HK\$'000 Restated
Turnover	<b>743,918</b>	716,714	657,433	646,840	660,015
Profit before taxation	<b>45,506</b>	38,617	31,911	27,222	30,706
Taxation	<b>(8,649)</b>	(7,498)	(1,112)	(4,937)	(4,336)
Profit attributable to shareholders	<b>36,857</b>	31,119	30,799	22,285	26,370
Total assets	<b>851,791</b>	792,573	697,873	613,157	519,184
Total liabilities plus minority interests	<b>(462,094)</b>	(436,621)	(368,469)	(311,951)	(228,286)
Net assets	<b>389,697</b>	355,952	329,404	301,206	290,898

### Distributable reserves

At 31 March 2004, the reserves of the Company available for distribution amounted to HK\$218,374,000 (2003: HK\$189,381,000). These were represented by share premium and retained profits of the Company. Under the Companies Law (Revised) Chapter 22 of the Cayman Islands, share premium of the Company is available for paying distributions and dividends to shareholders subject to the provisions of its Memorandum and Articles of Association and provided that immediately following the distributions or dividend payments, the Company is able to pay its debts as they fall due in the ordinary course of business.

### Purchase, sale or redemption of shares

The Company has not redeemed any of its shares during the year. Neither the Company nor any of its subsidiaries has purchased or sold any of the Company's shares during the year.

## Share option scheme

On 8 September 1997, a share option scheme (the “Old Scheme”) was approved by the shareholders of the Company under which its Directors may, at their discretion, invite employees of the Group including any Executive Directors to take up options (the “Share Options”) to subscribe for ordinary shares of HK\$0.1 each in the Company subject to the terms and conditions stipulated therein.

On 3 September 2002, the shareholders of the Company approved the termination of the Old Scheme and the adoption of a new scheme (“2002 Scheme”) as a result of the amendments of Chapter 17 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the “Listing Rules”). Upon termination of the Old Scheme, no further options can be granted thereunder but in all other respects, the provisions of the Old Scheme shall remain in force and all share options granted prior to such termination shall continue to be valid and exercisable in accordance therewith.

Details of the 2002 Scheme are as follows:

**(1) Purpose**

To recognise the contribution of employees, suppliers, consultants, agents and advisers of the Group.

**(2) Eligible persons**

Full-time employees of the Group (including Directors of the Company and its subsidiaries) and suppliers, consultants, agents and advisers who have contributed or will contribute to the Group.

**(3) Maximum number of shares**

The maximum number of shares available for issue under the 2002 Scheme is 28,940,000, representing approximately 7% of the issued share capital of the Company as at the date of this report.

**(4) Maximum entitlement of each eligible person**

Unless approved by shareholders, the total number of shares issued and to be issued upon exercise of the share options granted to each eligible person in any 12-months period must not exceed 1% of the shares of the Company in issue.

**(5) Time of exercise of option**

An option may be exercised during the periods to be determined and notified by the Directors of the Company to the grantees at the time of making offers to grant share options to them provided that such periods shall not exceed the period of ten years from the date of grant.

**(6) Acceptance of offers**

Offers for the grant of share options must be accepted within twenty eight days, inclusive of the dates on which the offers are made. Offers for grant of share options have to be accepted together with remittance in favour of the Company of HK\$1.00.

## Share option scheme (continued)

### (7) Basis of determining the option exercise price

The subscription price for the shares under the 2002 Scheme shall be a price determined by the Directors at its discretion, provided that it shall not less than the higher of (i) the closing price of the shares stated in the daily quotation sheets issued by The Stock Exchange of Hong Kong Limited ("Stock Exchange") on the date of grant and (ii) the average closing price of the shares stated in the Stock Exchange's daily quotation sheets for the five business days immediately preceding the date of grant of share options.

### (8) The remaining life of the 2002 Scheme

The 2002 Scheme will be terminated at the close of business of the Company on 3 September 2012, being a date which falls ten years after the date of adoption of the 2002 Scheme.

No options have been granted under the 2002 Scheme.

Details of the share options outstanding as at 31 March 2004 which have been granted under the Share Option Scheme are as follows:

	Options held at 1 April 2003	Options granted during year	Options exercised during year	Options cancelled during year	Options held at 31 March 2004	Exercise price	Grant date	Exercisable from	Exercisable until
Mr. LEUNG Lun	2,000,000	-	-	-	2,000,000	0.675	14 March 2000	1 October 2000	30 September 2005
Mr. LEUNG Chung Ming	2,000,000	-	-	-	2,000,000	0.675	14 March 2000	1 October 2000	30 September 2005
Mr. ZHONG Bing Quan	2,000,000	-	-	-	2,000,000	0.675	14 March 2000	1 October 2000	30 September 2005
Ms. CHENG Yun Tai	2,000,000	-	-	-	2,000,000	0.675	14 March 2000	1 October 2000	30 September 2005
Mr. WONG Tze On, Andy	2,000,000	-	-	-	2,000,000	0.675	14 March 2000	1 October 2000	30 September 2005
Continuous contract employees	1,900,000	-	-	(1,100,000)	800,000	0.675	14 March 2000	1 October 2000	30 September 2005
<b>Total</b>	<b>11,900,000</b>	<b>-</b>	<b>-</b>	<b>(1,100,000)</b>	<b>10,800,000</b>				

#### Note

The above options granted are not recognised in the accounts until they are exercised. Rule 17.08 of the Listing Rules stipulates that the listed issuer is encouraged to disclose in its annual report the value of share options granted to the participants. The Directors consider it inappropriate to value the share options as a number of factors critical for the valuation cannot be determined accurately. Any valuation of the share options based on various speculative assumptions would be meaningless and could be misleading to the shareholders.

## Conversion of preference shares

During the year, 69,333,333 ordinary shares of HK\$0.1 each were issued at HK\$0.45 each as a result of the conversion of all convertible preference shares.

## DIRECTORS

The Directors during the year were:

Mr LEUNG Lun  
 Mr LEUNG Chung Ming  
 Mr ZHONG Bing Quan  
 Ms CHENG Yun Tai  
 Mr WONG Tze On, Andy  
 Mr WONG Lam, O.B.E., J.P.\*  
 Mr YE Tian Liu\*  
 Mr KO Peter, Ping Wah\*

\* Independent Non-executive Directors

**Mr LEUNG Chung Ming**, being the Managing Director of the Company, is not subject to rotation pursuant to Article 116 of the Company's Articles of Association. Mr Leung Lun and Mr Wong Lam, O.B.E., J.P. retire in accordance with Articles 90 and 116 of the Company's Articles of Association but, being eligible, offer themselves for re-election at the forthcoming Annual General Meeting.

Biographical details of Directors and senior management are set out as follows:

### Executive Directors

**Mr LEUNG Lun**, aged 55, is the Chairman of the Company and the founder of the Group. Mr Leung is responsible for the overall corporate policy and development strategy as well as overseeing the Group's overall management. He has 40 years of experience in the toys manufacturing industry. Mr Leung is a member of the committee of the Chinese People's Political Consultative Conference of Jiang Xi Province and vice general director of Guangdong Chamber of International Commerce. He is also a standing member of the committee of the Chinese People's Political Consultative Conference of Dongguan City. He was named an honourable citizen of Dongguan City by the local authority in 1996 for his contribution to the City.

**Mr LEUNG Chung Ming**, aged 44, is the Managing Director of the Group. He is the brother of Mr Leung Lun. He joined the Group in November 1979 and is responsible for strategic planning, OEM sales and marketing functions of the Group. He is also in charge of the Group's ODM products development. He is currently a vice president of The Toys Manufacturer's Association of Hong Kong. Mr Leung is a Hong Kong district special member of the People's Republic of China United Youth Association as well as a director of China Children and Teenagers' Fund. He is also a member of the committee of the Chinese People's Political Consultative Conference of Guizhou Province and 2002 Young Industrialist of Hong Kong.

**Mr ZHONG Bing Quan**, aged 52, is one of the founders of Lung Cheong Toys Limited ("LC Toys") in September 1989. He is responsible for formulation of the sales and marketing strategic planning for the Mainland China market. Mr Zhong is also responsible for liaison with local authorities in Mainland China. He has been general manager of Dongguan City Supply, Marketing and Trading Company since 1979.

### Executive Directors (continued)

**Ms CHENG Yun Tai**, aged 49, is responsible for overseeing the financial control of the Group's operations in Mainland China. She is also responsible for liaising with local authorities in Mainland China. Ms Cheng is also deputy general manager of Dongguan City Supply, Marketing and Trading Company. She has been a director of a subsidiary of the Company since March 1995.

**Mr WONG Tze On, Andy**, aged 37, is responsible for the formulation of the corporate strategy and financial planning of the Group. He is also responsible for new capital ventures and project development of the Group. Mr Wong holds a business degree in accounting from the Curtin University of Technology, Western Australia. He joined the Group in June 1993. He is a member of the Australian Society of Certified Practising Accountants. Mr Wong was appointed as a Director in August 1997.

### Independent Non-executive Directors

**Mr YE Tian Liu**, aged 58, was appointed as an Independent Non-executive Director and Chairman of the Audit Committee of the Company in November 1999. Mr Ye holds a master's degree in business administration. He was formally an executive director of a locally listed company for several years. He has extensive experiences in China trade and investment.

**Mr WONG Lam**, O.B.E., J.P., aged 85, is a former member of Hong Kong Legislative Council and former standing committee member of the Chinese People's Political Consultative Conference of Dongguan City. Mr Wong was appointed as an Independent Non-executive Director and a member of the Audit Committee of the Company in November 1999.

**Mr KO Peter, Ping Wah**, aged 55, was appointed as an Independent Non-executive Director and a member of the Audit Committee of the Company in Jan 2003. Mr Ko holds a master's degree of science in business administration from the University of Bath, England and bachelor's degree in law (Chinese Law) from the University of Beijing, China. He was formally an auditor of ISO900 and QS900 for over 6 years and a management consultant of a local company for over 14 years. He is also appointed a part-time tutor of the Chinese University of Hong Kong and other universities/colleges for over 24 years.

### Company Secretary

**Mr MAK Yee Chuen, Vincent**, aged 47, was appointed as Company Secretary in July 2000. Mr Mak holds a master's degree of laws from The University of Hong Kong in 2001 and master's degree in business administration from The Hong Kong Polytechnic University in 1994. He is a fellow member of the Hong Kong Society of Accountants and The Association of Chartered Certified Accountants. He was the founder and partner of Vincent Mak & Company, Certified Public Accountants in 1987. He became the principal of Vincent Mak & Co., Solicitors in 2002.

### Senior management

**Mr CHAN Tit Yu, Alfred**, aged 57, is the Managing Director of Standard Tooling & Products Co., Ltd., a wholly owned subsidiary of the Group dedicated to fulfill all pre-production functions of toys products including new products research, product design, development & engineering and injection molds manufacturing. Mr. Chan holds a master of science degree in industrial engineering from Georgia Institute of Technology at USA. Apart from his 4 years management consulting experience, he is a 25 years toy industry veteran who has held senior executive positions in number of leading international toys firms prior to joining the Group in February 2004.

**Mr LEUNG Yuk Hung, Paul**, aged 29, is the Associate Director responsible for the management of the Group's information technology infrastructure. He is also responsible for the development of new business ventures. Mr. Leung is the son of the Group's Chairman. He holds a bachelor of engineering (I.T.) degree and a bachelor of commerce (accounting and finance) degree from the University of Western Australia. He is also a Certified Information Systems Auditor (CISA). He joined the Group in March 2003.

**Mr NG Ki Yin, Simon**, aged 50, is the Operations Director of the Group. He holds a bachelor of science degree in business management. He joined the Group in June 1994. Mr. Ng is responsible for the daily operations in term of production, human resources, sourcing, material planning and IT functions of the Group. He has over 20 years of experience in manufacturing resources planning and system management both in overseas corporates and PRC companies.

**Mr NGAI, Vester**, aged 50, the Managing Director of L C Technology Ltd. holds a bachelor degree in electronic engineering. Mr Ngai has 25 years of engineering, production management experienced in the consumer electronic industry. He joined the Group in September 2002, responsible for development non-toy electronic products, and dedicated to raise the Group technical capabilities into high value production.

**Mr SETO Sai Cheong Paul**, aged 42, is the Group's Chief Accountant. He is a member of the Hong Kong Society of Accountants, The Association of Chartered Certified Accountants and The Taxation Institute of Hong Kong and has over 20 years of experience in accounting and taxation. He is responsible for overall finance, accounting and taxation functions of the Group. He joined the Group in December 2000.

### Directors' service contracts

Each of the Executive Directors has entered into a service agreement with the Company for an initial fixed term of three years commencing from 1 September 1997 and shall continue thereafter unless and until terminated by either the Company or the Director giving to the other party not less than six months' notice in writing to determine the same. Under the agreements, the Executive Directors will receive a fixed monthly salary. Certain of the Executive Directors will also receive a year end bonus and a discretionary bonus under the agreements.

Apart from the above, none of the Directors who are proposed for re-election at the forthcoming annual general meeting has a service contract with the Company which is not determinable within one year without payment of compensation, other than statutory compensation.

### Directors' interests in contracts

In fiscal year 2002/03, Fericle Holdings Limited ("Fericle"), a wholly-owned subsidiary of the Group, purchased separate insurance contracts for each of Mr. Leung Lun, Mr. Leung Chung Ming and Mr. Wong Tze On, Andy, all are the Group's Executive Directors, with insured amounts of US\$10,000,000 (HK\$78,000,000), US\$10,000,000 (HK\$78,000,000) and US\$5,000,000 (HK\$39,000,000) respectively. Each of the insurance contracts will mature on the date when the insured reaches the age of 100 or death of the insured, whichever is earlier. Lumps sum payments of US\$2,142,000 (HK\$16,708,000), US\$1,296,000 (HK\$10,112,000) and US\$315,000 (HK\$2,457,000), respectively, totalling US\$3,753,000 (HK\$29,277,000), which were financed by a bank loan, were paid during the year to the insurance company. For each of the insurance contracts, Fericle and the beneficiary of the insured is entitled to 50% of the insured amount but Fericle is wholly entitled to any cash surrender value attached to the relevant insurance contracts during the period of the life insurance.

Save as mentioned above, no contracts of significance in relation to the Company's business to which the Company, its holding companies or its subsidiaries was a party, and in which a Director had a material interest, whether directly or indirectly, subsisted at the end of the year or at any time during the year.

### Directors' interests in equity securities

At 31 March 2004, the Directors, Chief Executives and their Associates had the following interests in the share capital and share options of the Company or any of its associated corporations (within the meaning of the Securities (Disclosure of Interests) Ordinance (the "SDI Ordinance"), as recorded in the register maintained by the Company pursuant to Section 29 of the SDI Ordinance or as notified to the Company:

Name	Type of interest	Number of ordinary shares
Mr Leung Lun	Corporate	279,442,000
Mr Leung Chung Ming	Corporate	279,442,000

Note:

279,442,000 ordinary shares in the Company were owned by Lung Cheong Investment Limited ("LC Investment") which is wholly owned by Rare Diamond Limited. Rare Diamond Limited is beneficially owned as to 70% by Mr Leung Lun and 30% by Mr Leung Chung Ming respectively. Accordingly, Mr Leung Lun and Mr Leung Chung Ming are taken to be interested in those ordinary shares.

Arrangement on share options granted to Directors are set out in the previous part of this report.

Apart from the Share Option Scheme, at no time during the year was the Company, its holding companies or its subsidiaries a party to any arrangements to enable the Directors, Chief Executives and their Associates to acquire benefits by means of the acquisition of shares in, or debentures of, the Company or any other body corporate.



### Directors' interests in equity securities (continued)

Save as disclosed above, at no time during the year, the Directors, Chief Executives (including their spouse and children under 18 years of age) had any beneficial or non-beneficial interests in, or had been granted, or exercised, any rights to subscribe for shares of the Company and its associated corporations.

On 26 June 2001 the Company entered into a transferable term loan agreement (the "First Syndication Loan Agreement") which imposes an obligation for the controlling shareholders of the Company, Mr Leung Lun and Mr Leung Chung Ming and their respective family members/associates (as defined under the Listing Rules) to maintain in aggregate at least 51% of the total issued voting share capital of the Company as at the date of the First Syndication Loan Agreement and from time to time when the loan remains outstanding.

Pursuant to another loan facility agreement ("Second Syndication Loan") entered into by the company and a group of financial institutions on 3 December 2002, Mr Leung Lun and Mr Leung Chung Ming are required to jointly hold at least 45% of the issued share capital of the Company.

### Substantial shareholders

At 31 March 2004 the register of substantial shareholders maintained under Section 16(1) of the SDI Ordinance shows that the Company had not been notified of any substantial shareholders' interests, being 10% or more of the Company's issued share capital, other than those of the Directors, Chief Executives and their Associates as disclosed above.

### Management contracts

Other than the contracts of service with the Directors or any persons engaged in the full-time employment of the Group, no contracts concerning the management and administration of the whole or any substantial part of the business of the Group were entered into or existed during the year.

### Connected transactions

At 31 March 2004, a wholly-owned subsidiary of the Company, Lung Cheong Toys Limited ("LC Toys"), had long-term loans and deferred trading balances amounted in aggregate to HK\$60,648,000, plus accrued interest, due by PT. Lung Cheong Brothers Industrial ("PTLC"), a 60% owned subsidiary of LC Toys. The balance of the 40% interest in PTLC is owned by independent third parties who are not connected with the Directors, Chief Executives or substantial shareholders of the Company and its subsidiaries, other than PTLC, or any of their respective associates. The long-term loans were advanced to finance the set up of the production facilities of PTLC. The amounts are unsecured, bearing interest at the rate of 10% per annum and have no fixed repayment terms. LC Toys does not intend to demand repayment of the advances in the foreseeable future.

The Directors, including the Non-executive Directors, are of the opinion that the above transaction was entered into on normal commercial terms which are fair and reasonable.

## Major customers and suppliers

The percentage of sales and purchases attributable to the Group's largest customers and suppliers are as follows:

	<b>2004</b> %	2003 %
Sales		
– the largest customer	<b>25</b>	21
– five largest customers combined	<b>74</b>	76
Purchases		
– the largest supplier	<b>7</b>	12
– five largest suppliers combined	<b>21</b>	25

No Directors or their Associates and no shareholders (which to the knowledge of the Directors own more than 5% of the Company's share capital) had an interest in the major suppliers or customers noted above.

## Audit Committee

Pursuant to the Listing Rules, an audit committee was established on 14 March 2000. The Committee comprises three Independent Non-executive Directors, namely Mr YE Tian Liu, Mr KO Peter, Ping Wah and Mr WONG Lam, O.B.E., J.P..

By reference to "A Guide for the Formation of An Audit Committee" published by the Hong Kong Society of Accountants, written terms of reference which describe the authority and duties of the audit committee were prepared and adopted by the Board of the Company on the same date. The principal activities of the Audit Committee include the review and supervision of the Group's financial reporting process and internal controls.

## Compliance with the Code of Best Practice of the Listing Rules

The Code of Best Practice has been complied with by the Company during the year ended 31 March 2004 except that Non-executive Directors are not appointed for a specific term as recommended under paragraph 7 of Appendix 14 of the Listing Rules. They are subject to retirement by rotation and re-election at the Annual General Meeting in accordance with the Articles of Association of the Company. In the opinion of the Directors this meets the same objective as the Code of Best Practice.

## Auditors

The accounts have been audited by PricewaterhouseCoopers who retire and, being eligible, offer themselves for re-appointment.

On behalf of the Board

A handwritten signature in blue ink, appearing to be 'L. Lun', written over a horizontal line.

**Leung Lun**  
*Chairman*

Hong Kong, 22 July 2004