

MANAGEMENT DISCUSSION AND ANALYSIS

Performance Highlights

For the six months ended 30 June	2004 HK\$'000	2003 HK\$'000	Percentage change
Turnover	436,658	277,366	+ 57%
Gross profit	237,426	148,077	+ 60%
Operating profit	45,264	13,020	+ 248%
Profit attributable to shareholders	37,211	9,911	+ 275%
Earnings per share	<i>HK cents</i>	<i>HK cent</i>	
– Basic	2.40	0.81	
– Diluted	2.37	0.76	

Property Rental and Management

Income from property rental and management (before inter-segment revenue elimination) for the period amounted to HK\$15,151,000, compared to HK\$17,399,000 a year ago, representing a drop of about 13%. The decrease was mainly attributable to the difficulty in securing tenants to replace expired leases during the immediate post-SARS period in the second half of 2003. As the local economy recovers, leasing activities are expected to become more active. The Group is cautiously optimistic that rental and related income will improve during the balance of the year. As at the end of the period, the overall occupancy rate was 91% versus 88% on 31 December 2003. Management maintains the view that the property investment and management business will continue to provide a steady income to augment the core business of the Group.

Playmates Toys Overview

Income from toy sales was HK\$421,791,000, or an increase of 62% compared to HK\$260,473,000 a year ago. Playmates Toys' disciplined brand building and focused marketing strategies resulted in major increases in sales, gross margin and operating profit. All core brands contributed to this strong performance as the Group continued to build a balanced portfolio of proprietary and licensed entertainment properties and expand worldwide distribution. At the end of the first half of 2004, Playmates Toys is well positioned to achieve its full year objectives.

Of particular note during the first half were the increases in both gross margin and operating profit. Gross margin has consistently improved over the past two years, primarily due to significant efficiency gains in the product development function. The increase in operating profit reflects the Group's ability to more fully leverage the low overhead operating model adopted in 2002.

International sales growth is attributable to the continued success of the **Teenage Mutant Ninja Turtles**[®] (“**Turtles**”) brand, and the strong performance of the other core brands. Both **Speedeez**[®] and **Disney**[®] **Princess** launched in important markets during the first half. International sales increased by 177% over the same period last year and accounted for 27% of Playmates Toys’ turnover during the period. With strong first half results and a healthy order position at mid year, international sales are on track to achieve the planned full year growth target.

Teenage Mutant Ninja Turtles[®]

In the second full year of distribution, and despite vigorous competition in the action figure category, the **Turtles** brand continues to grow and consistently ranks among the top three best selling brands in the male action category in the U.S. and major international markets including Canada, the U.K., France, and Australia. **Turtles** worldwide sales increased by 79% over the same period last year. By the end of the year, **Turtles** distribution will expand to over 45 countries.

U.S. **Turtles** sales growth was propelled by the Group’s comprehensive marketing and promotional support and by the Monday through Friday broadcast of the animated television series on the **Cartoon Network**^{TM&®}. A total of 104 episodes of the series are now completed or in production. This production commitment will deliver a steady stream of new episodes for both the **FOX Box**[®] Saturday morning and **Cartoon Network**^{TM&®} weekday broadcasts throughout 2004 and 2005.

This fall, **Turtles** will be one of the lead boys’ properties to premier on **Majesco**’s new **Game Boy**[®] **Advance Video**TM entertainment system. With a U.S. installed base of over 20 million units, the **Game Boy**[®] **Advance Video**TM platform will expose even more kids to **Turtles** and will enable fans to watch their favorite **Turtles** animation whenever and wherever they wish. Negotiations are continuing to add **Turtles** episodes to the library of television series available for use on other portable entertainment platforms.

Worldwide, the non-toy license program has grown to 113 licensees and continues to expand as **Turtles**’ distribution grows. During the first half and continuing for the balance of the year, the Group, in concert with other non-toy **Turtles**’ licensees, will promote the brand through extensive, multi-layered marketing, including television advertising, retail promotions, on-air and on-line events.

The Group’s **Turtles** toy line has substantially expanded from last year in every key product segment: basic figures, special feature figures, vehicles, playsets, and role play accessories. Strong customer support is reflected in expanded retail presence. Fall retail shelf space for the brand is planned to substantially increase over the same period last year.

With continuous television advertising during the fall season, an expanded product offering, enhanced programming coverage, increased retail presence and targeted marketing efforts from a wide range of promotional and licensing partners, the **Turtles** brand is well positioned for continued growth in the years ahead.

Speedeez®

Sales of the **Speedeez**® brand during the first half increased 169% over the same period last year. The sustained focus by Playmates Toys on design innovation, packaging creativity, distribution expansion and the continued communication of the unique attributes of the patented *Turbo Ball* technology successfully overcame competition and established **Speedeez**® as the leading brand in the highly competitive micro scale vehicle business.

Speedeez® international distribution is expanding to over 25 countries including Spain, Italy, and Latin America. Playmates Toys recently acquired license rights from *BMW* to launch a *Mini Cooper S* playset which will anchor the marketing efforts of distributors in all major international markets this fall. It is expected that this universally recognized vehicle will replicate the success of the *Hummer H2* playset in the U.S. in 2003.

Disney®

Playmates Toys' continued focus on a select few, well defined product lines within the **Disney**® **Princess** brand delivered sales gains in the first half of 56% over the same period last year. In its third year, the *Little Princess* doll assortment remains the best selling large doll in the U.S. The assortment was extended, at a higher retail price, through the introduction of the *Little Princess Color Change* collection. The ability to launch an extension to the *Little Princess* segment at a price premium to the original product offering is testament to the continued strength and long term growth potential of the **Disney**® **Princess** franchise. During 2004 **Disney**® **Princess** dolls will be introduced in all major European markets and a total of over 25 countries worldwide.

A new *My Baby Princess* line will be launched this fall. This large doll assortment is the first time that the *Classic Princesses* have been interpreted as babies and reflects Playmates Toys' close and collaborative working relationship with *Disney Consumer Products*. Brand expansion will continue in 2005 when the Group will introduce a new scale and positioning strategy for the *Classic Princesses* through the introduction of the "*World of Cinderella*" segment.

Waterbabies®

A 56% increase in sales during the first half over the same period last year set the stage for a promotional renewal for this 15 year brand this fall. This sales growth was led by improved performance of the core *Sweet Cuddlers*® line and the licensed **Waterbabies**® segment, the latter benefiting from the continued popularity of *Care Bears*™&©.

A new *Wiggly Giggly Waterbabies*® assortment will be television advertised this fall. These dolls will be the first **Waterbabies**® to be promoted on television in many years. Previous experience suggests that sales for the entire brand can be expected to benefit from this advertising effort. The *Wiggly Giggly Waterbabies*® campaign will also spearhead the launch of the **Waterbabies**® brand in Latin America.

In spring 2005, Playmates Toys will launch a new product segment – sculpted **Waterbabies**[®] characters. The first character to be brought to life with the **Waterbabies**[®] proprietary design will be *Blue* from *Nickelodeon's Blue's Clues*[™]. *Blue* is the first in a collection of *Nickelodeon* and other licensed characters to be introduced in this new line.

Blinkies[™]

This fall Playmates Toys will introduce **Blinkies**[™] with an extensive promotional and comprehensive marketing campaign. **Blinkies**[™] is an interactive, virtual “best friend” and features a wide variety of themes and play patterns that reflect contemporary interests of young girls. This youth electronic lifestyle product is the first such product to feature a color interactive screen at an affordable price.

Blinkies[™] is broadly supported by all major U.S. customers. Distributors in the U.K. and Canada will launch **Blinkies**[™] to coincide with the U.S. marketing campaign. Localization is underway in preparation for the 2005 launch of **Blinkies**[™] in leading non-English speaking markets.

2005 and Beyond

The Group has recently previewed its 2005 spring product lines to major customers. Both core brand extensions and new brand introductions have been well received by U.S. retailers and international distributors.

Recent entertainment licenses added to Playmates Toys’ brand portfolio include **Atomic Betty**[®] and **Delgo**[®]. Playmates Toys has acquired the master toy license for both properties.

Atomic Betty[®] dolls and playsets, inspired by the *Cartoon Network*^{™&®} animated television series of the same name will be launched in spring 2005. The series will premier in September 2004 and is being heralded as *Cartoon Network's*^{™&®} leading new girls action franchise.

Delgo[®] is a computer animated feature film from *Fathom Studios*, a leading CGI production company in the U.S. The movie’s cutting edge animation, compelling story and wide array of original characters will inspire a range of action figures and related accessories. **Delgo**[®] is expected to premier in the U.S. in late 2005.

The Group continues to selectively invest in new brands and entertainment licenses that offer significant potential for long term growth. The continued development of previously announced properties and the addition of **Delgo**[®] and **Atomic Betty**[®] to Playmates Toys’ portfolio are consistent with this strategy.

The 2004 first half results are further evidence of the effectiveness of the Group’s operating strategies. The brand building fundamentals that have fueled growth during the past two years will continue to guide Playmates Toys’ efforts in the expansion of core brands and the identification of new licenses and product opportunities.

As the fall selling season begins, the Group's distribution continues to expand both in the U.S. and internationally. Core brands continue to perform well, and key gross margin and operating profit indicators remain on target. Additionally, progress is being made in further business expansion through the acquisition of new licenses and the entry into new product categories for 2005 and beyond.

Liquidity and Financial Resources

The toy business is inherently seasonal in nature. Generally speaking, sales in the second half-year are much higher than in the first half. As a result, a disproportionately high balance of trade receivables is generated during the peak selling season in the second half of the year. Consistent with usual trade practices, a significant portion of the trade receivables is collected in the final weeks of the fourth quarter and in the first quarter of the subsequent year, resulting in a seasonal demand for working capital during the peak selling seasons. As at 30 June 2004, trade receivables related to toys operation were HK\$114,611,000 (31 December 2003: HK\$267,182,000) and inventories were HK\$36,355,000 (31 December 2003: HK\$29,108,000).

The property investment and management business generates a relatively steady income stream throughout the period. Approximately 91% of the total gross floor area of the Group's investment properties were leased out as at 30 June 2004. Account receivables were minimal as at the period end.

The Group's gearing ratio, defined as total bank borrowings expressed as a percentage of total tangible assets, at 30 June 2004 was 4.5% compared to 21.9% at 31 December 2003. The current ratio, calculated as the ratio of current assets to current liabilities, was 2.5 at 30 June 2004 compared to 2.1 at 31 December 2003. As at 30 June 2004, the Group's cash and bank balances were HK\$287,664,000 compared to HK\$471,457,000 at 31 December 2003.

Charges on Group Assets

Details of charges on group assets are set out in note 8 to the interim accounts.

Employees

As at 30 June 2004, the Group had a total of 112 employees in Hong Kong, the Mainland China and the United States of America.

There was no material change in remuneration policies compared to those disclosed in the most recently published annual report.