15. Post balance sheet events

Subsequent to 30 June 2004, the following events took place:

1. The Group entered into a non-binding memorandum of understanding ("MOU") for the acquisition of 35% equity interests in World Grand Holdings Limited, which is interested in 90% of the registered capital of Kunming World Grand Colour Printing Co., Ltd. ("Kunming World Grand"). Upon signing of the MOU, a sum of HK$10 million had been paid as deposit and part payment of the consideration for the acquisition, details of which are set out in the announcement of the Company dated 9 July 2004.

2. The Board has declared the payment of an interim dividend of HK$20 million in respect of the six months ended 30 June 2004.

MANAGEMENT DISCUSSION AND ANALYSIS

Results

The Group is pleased to announce its satisfactory results for the first half of 2004 (the "Period"), with turnover and profit attributable to shareholders both having attained historical high and sustained double-digits growth. With the successful listing of the Company's Shares on the Main Board of the Stock Exchange on 26 March 2004, the Group has further enhanced its corporate image and reputation, solidifying its foundation for fast growing developments in the future.

Supported by our proven business operation and established market position successfully built in the past, and through the effective implementation of development plans and operating strategies, the Group's two core businesses – cigarette package printing and laminated paper manufacturing – performed remarkably well during the Period. Significant growth was achieved in the first half of 2004 with turnover and profit both having reached new heights. Turnover increased by about 26.1% to approximately HK$122,666,000 from approximately HK$97,298,000 in the corresponding period of last year. Profit attributable to shareholders grew by about 30.4% to approximately HK$40,044,000 from last year's approximately HK$30,712,000. Basic earnings per share were HK10.7 cents.

To reward shareholders for their support, the Board has declared the payment of interim dividend for the six months ended 30 June 2004 of HK5 cents per Share to shareholders whose names appeared on the register of shareholders of the Company on 7 October 2004.

Business Review

Cigarette Package Printing

For the six months ended 30 June 2004, the cigarette package printing business operated by the Group's subsidiary, Victory Honest Industries (Shenzhen) Co., Ltd. ("Victory Shenzhen") recorded a turnover of approximately HK$44,160,000, representing an increase of about 19.4% over that of approximately HK$36,973,000 in the same period of last year, accounting for approximately 36.0% of the Group's total turnover.

During the Period, the Group's innovative cigarette package designs and patented printing technologies were well received by both our existing and potential customers. Moreover, our advanced and high-quality production capabilities are well recognised by the market which further intensified our competitive advantages. To augment the above success, two main growth drivers pushed up the Group's turnover – steady orders from existing customers and the Group's success in securing several new customers. The new customers included the Guangzhou No. 2 Cigarette Factory and two newly acquired cigarette factories in Liaoning Province by a large cigarette manufacturer – Hongta Cigarette Factory, etc., all of which brought in profitable orders and provided the Group with steady income streams. The increase in orders will provide additional momentum for the Group's future development and expansion of market share in the industry.

Besides having established long term and steady relationships with several customers that are among the 36 key cigarette industrial enterprises in the PRC, Nanjing Sanlong, a 48% interest associated company of the Group, has also maintained a strong strategic relationship with Nanjing Cigarette Factory and Huaiyin Cigarette Factory. The new production plant of Nanjing Sanlong was completed at the end of 2003 and the new additional production line, which doubles the annual production capacity to approximately 600,000 cartoon, had commenced operation in the first quarter of 2004. The increased capacity can further satisfy the increasing demands from Nanjing Cigarette Factory and Huaiyin Cigarette Factory and also significantly boost the income base of Nanjing Sanlong. For the six months ended 30 June 2004, profit contribution from Nanjing Sanlong amounted to approximately HK$15,238,000, representing a growth of about 4.6% over the same period of last year's approximately HK$14,563,000. Upon the completion of handover between the old and new plants together with the smoothness of the teething troubles between the old and new production lines of Nanjing Sanlong during the Period, the management anticipates much better results in terms of production efficiency and profit contribution in the second half of 2004.

The current annual cigarette package production capacity of Victory Shenzhen and the associated company, Nanjing Sanlong reaches approximately 400,000 cartoons and 600,000 cartoons respectively. The average utilisation rate of the production lines for Victory Shenzhen and Nanjing Sanlong also exceeds 70% and 65% respectively.

Laminated Paper Manufacturing

During the Period, the sales volume of laminated paper increased significantly and the business grew rapidly. Turnover increased by about 30.1% from approximately HK$60,325,000 in the corresponding period of last year to approximately HK$78,506,000, accounting for approximately 64.0% of the Group's total turnover.

The fact that most cigarette package printers have not vertically integrated their production processes in producing laminated papers while we enjoy a sound reputation in producing high quality laminated papers, gives us a distinct edge over our competitors. Capitalising on this unique edge, the Group had implemented a unique sales strategy in the second half year of 2003, selling its laminated paper to other large-scaled cigarette package printers in the PRC for their printing and manufacturing needs. This not only broadens the Group's revenue stream and customer base, but also enables the Group to create a win-win situation.

With the successful incorporation of several environment-friendly and cost saving technologies into the production of laminated papers last year, the management expected that the full-scale application of these technologies in mass production this year will stimulate new growth momentum for the Group, further enhance our product attractiveness, and provide substantial savings on production costs.

Prospects

According to a recent announcement issued by the State Tobacco Monopoly Administration of the PRC, the number of cigarette manufacturers has further consolidated from 185 to just over 80. In light of this consolidation, those existing cigarette manufacturers are actively launching new brands and/or renewing the package designs for their existing brands so as to maintain and strengthen their competitiveness and market share. As a result, all cigarette manufacturers at large have become more demanding on the quality of cigarette packages with special focus on the quality of printing, design and outlook for their products which will allow them to enhance product grading and pricing. Such market phenomenal provides an excellent business opportunity for us because it exactly matches our market positioning and business development direction in serving cigarette manufacturers with high quality demand on both design and printing.

Cigarette Package Printing

In view of the huge demand from this potentially lucrative market, the Group will adopt diversified development strategies to speed up its business growth. As for the cigarette package printing business, the Group has been focusing on expanding its sales network to Guangdong Province, Yunnan Province, Hunan Province and Jiangxi Province, with the aim of securing larger and stable cigarette manufacturers as its customers. In July this year, the Group signed a non-binding memorandum of understanding in relation to the acquisition of 31.5% effective interests in Kunming World Grand, a large cigarette package printing company in Yunnan Province, for the purpose of our expansion into the Kunming market which in turn may further strengthen our leading position in the PRC. It is expected that the formal sale and purchase agreement for the acquisition will be entered into on or before 31 December 2004.

Kunming World Grand is a cigarette package printing company with strong foundations and huge market potential. Its excellent management and expertise has enabled it to become one of the leading cigarette package printers in Yunnan Province. Its major customers include Yunnan Cigarette Factory, one of the top three cigarette factories in the PRC.

The management believes that through the acquisition of Kunming World Grand, the Group will benefit from the synergies through the strategic relationship in areas including the sharing of resources such as technological know-how, printing machinery, and consolidation of marketing and sales force, as well as economies of scale. More importantly, the strategic co-operation will provide the Group with the opportunity to explore further potentials of its laminated papers and cigarette packages printing businesses in Yunnan Province, the largest cigarette manufacturing base in the PRC. With Kunming World Grand being a major customer of its laminated papers, the management envisages that the Group can generate a stable inflow of orders in future through its strategic relationship with Kunming World Grand.

Laminated Paper Manufacturing

The Group possesses a high caliber research and development team with ever improving capabilities to ensure the provision of high quality laminated papers to customers. Armed with advanced technology and professional expertise, the Group is prepared to start producing metallised and laser films for the manufacturing of laminated papers and expects to achieve full-scale operation in 2005. This will enable the Group to produce a wide array of innovative and ingenious laminated paper products. The Group expects an increase in revenue from the laminated paper sector as well as substantial savings on production costs of its cigarette package printing business, which will in turn improve the overall profit margin of the Group.

Conclusion

The Group believes the cigarette package printing industry in the PRC has tremendous growth potential and will continue to flourish. We are devoted to relentlessly focusing on the development of our two core businesses. In addition, we are confident to move forward in great strides to realise the benefits from the strategic relationship with Kunming World Grand this year to lead the Group to become the biggest player in the industry.

Given the favourable operating environment of the tobacco industry in the PRC, our effective operating strategies and stringent cost control measures, the management is optimistic to deliver better and more encouraging results in the second half year. We are convinced that with our management's tireless dedication, we will take the Group to new frontiers of growth and to create greater long-term values to our shareholders.

Capital Structure, Financial Resources and Liquidity

Borrowing and banking facilities

As at 30 June 2004, the Group had aggregate banking and loan facilities, including those facilities from banks and finance lease creditors, of approximately HK$219.4 million (31 December 2003: HK$215.3 million) of which approximately HK$115.2 million (31 December 2003: HK$143.2 million) was utilised. The Group generally finances its operation with finance leases and banking facilities provided by its banks and finance lease creditors in Hong Kong and the PRC.

As at 30 June 2004, the short term borrowings of the Group of approximately HK$93.0 million (31 December 2003: HK$117.0 million) were repayable within one year.

As at 30 June 2004, the obligations under finance leases of the Group amounted to approximately HK$22.2 million (31 December 2003: HK$26.2 million), of which approximately HK$8.1 million (31 December 2003: HK$11.3 million) was repayable within one year, approximately HK$8.1 million (31 December 2003: HK$9.0 million) was repayable after one year but within two years, and approximately HK$6.0 million (31 December 2003: HK$5.9 million) was repayable after two years but within five years.

The short term borrowings and obligations under finance leases of the Group are either denominated in Hong Kong dollars or Renminbi.

Net current assets

As at 30 June 2004, the Group had net current assets of approximately HK$184.0 million (31 December 2003: HK$2.0 million). The current assets comprised inventories of approximately HK$58.8 million, trade and other receivables of approximately HK$92.6 million, prepayments and deposits of approximately HK$36.2 million and bank and cash balances of approximately HK$152.6 million. The current liabilities comprised trade and other payables of approximately HK$55.1 million, short term borrowings of approximately HK$93.0 million and current portion of obligations under finance leases of approximately HK$8.1 million. The Group's current ratio, as a ratio of current assets to current liabilities, was maintained at a healthy level of approximately 2.2 times (31 December 2003: 1.0 time).

Capital structure

As at 30 June 2004, the Group had net tangible assets of approximately HK$304.7 million comprising non-current assets of approximately HK$134.8 million (comprising fixed assets of approximately HK$88.7 million and investment in an associated company of approximately HK$46.1 million), net current assets of approximately HK$184.0 million and non-current liabilities of approximately HK$14.1 million (comprising entirely obligations under finance leases).

Capital commitments

As at 30 June 2004, the Group did not have any significant capital commitments.

Working capital
Taking into account the financial resources available to the Group, including internally generated funds, the available banking facilities and the estimated net proceeds from the share offer, the Directors are of the opinion that the Group has sufficient working capital for its present requirements.

Remuneration policies and employee information
As at 30 June 2004, the Group had over 370 full time employees in Hong Kong and the PRC. Total staff costs (including directors' emoluments) amounted to approximately HK$2.1 million (six months ended 30 June 2003: approximately HK$1.9 million) for the period under review. All full time salaried employees, except for factory workers and contract employees, are being paid on a monthly basis, plus a discretionary performance bonus. Factory workers are being remunerated based on a basic wage plus production incentive. The Group ensures that the pay levels of its employees are competitive and employees are rewarded on a performance related basis within the general framework of the Group's salary and bonus system.

In addition to salaries, the Group provides staff benefits including medical insurance and contributions to staff's provident fund. Share options and bonuses are also available to employees of the Group at the discretion of the Directors and depending upon the financial performance of the Group.

Significant investments and material acquisitions
During the period under review, the Group had no new investment or material acquisitions.

Gearing ratio
As at 30 June 2004, the Group's gearing ratio, expressed as a percentage of total borrowings over total assets was 24.2% (31 December 2003: 41.7%). The management believes that the gearing ratio is at an acceptable level for the Group and the Group would be able to create sufficient financial resources to discharge its debts.

Foreign exchange exposure
The Group does not currently have any hedging activities against its foreign exchange exposure nor does it adopt any formal hedging policies. During the period under review, all of the Group's sales and purchases were settled in United States dollars, Hong Kong dollars and/or Renminbi. The Directors consider the Group's risk exposure on foreign exchange as minimal.

Contingent liabilities
The Group did not have any significant contingent liabilities as at 30 June 2004.