

## MANAGEMENT DISCUSSION AND ANALYSIS

### Financial Performance

The Group's turnover for the six months ended 30th June, 2004 amounted to approximately HK\$108.1 million, represented an increase by 5% from the last corresponding period. Loss from operations amounted to approximately HK\$30.5 million and a loss of approximately HK\$39.5 million attributable to shareholders was recorded.

### Dividend

The directors of the Group do not recommend the payment of an interim dividend for the six months ended 30th June, 2004 (2003: nil).

### Review of Operations

For the six months ended 30th June, 2004, total turnover was approximately HK\$108.1 million, of which approximately HK\$100.6 million were derived from film distribution and the balance from video distribution and other services income. The turnover from film distribution division had slightly increased by 8% when compared with approximately HK\$93.3 million for the six months ended 30th June, 2003.

This period, the Group intended to maintain a stable production volume of high quality films in a conservative and prudent manner. It had released 6 films in the market when compared with 9 films in the last corresponding period. Overall, the results of these films were performed better than the last corresponding period despite the fact that the result of last period had seriously suffered from the impact of Severe Acute Respiratory Syndrome. Same as last period, three of our films' box offices had been ranged as top ten box offices of Chinese films in the first half of the year 2004.

During the period, Hong Kong and Macau ("Hong Kong") remained the Group's largest market. The turnover from Hong Kong increased by approximately 23% to approximately HK\$65.1 million and its segment result improved to approximately HK\$5.7 million (2003: loss of HK\$11.0 million) because the overall box offices of each film had been improved, particularly our Chinese New Year film, *Fantasia* which was ranked as the second highest box office of Chinese films in the first six months of 2004. The turnover from South-east Asia and America & Europe decreased by approximately 23% and 21% respectively, which were in proportion to the decrease in films released during these periods. However, their segment results improved to approximately HK\$3.1 million (2003: loss of HK\$4.3 million) and approximately HK\$6.8 million (2003: profit of HK\$2.4 million) respectively. The turnover from the market in the PRC maintained the same as last period but its segment result recorded loss of approximately HK\$7.3 million when compared to a profit of approximately HK\$8.8 million in last period. Recently, the film industry in the PRC had faced with new challenges and increasing competition. The provision of Closer Economic Partnership Arrangement between Hong Kong and the PRC ("CEPA") had not been fully implemented. The operation modes of distribution were changing rapidly during this development stage. The Group needed to incur substantial expenses in advertising and distribution in order to maintain its sales. Besides, the Group considered that extensive advertising and promotion in different media throughout the PRC can develop its reputation and recognition and can contribute to stabilise its future revenue and built its foundation for future growth.

As a result of the Group's cost control measure in these years, administrative expenses before depreciation and amortisation decreased by approximately 24% to approximately HK\$18.4 million for the six months ended 30th June, 2004. Staff costs and rental expenses further decreased by approximately 24% and 25% to approximately HK\$10.3 million and HK\$1.4 million respectively.

### **Liquidity and Financial Resources**

At 30th June, 2004, the Group had total assets of approximately HK\$898.8 million and a net current assets of approximately HK\$338.3 million, representing a current ratio of 3.8 (30.6.2003: 2.9). The Group had total cash and bank balances of approximately HK\$24.9 million of which a bank deposit of approximately HK\$1.6 million was pledged for bank facility granted. At 30th June, 2004, the Group had total borrowings of approximately HK\$46.9 million comprising mortgage loan of approximately HK\$18.6 million, secured bank loan of HK\$8.3 million and unsecured convertible loan note ("Note") of HK\$20 million. The Group's gearing remained low during the period with total debts of approximately HK\$46.9 million against shareholders' funds of approximately HK\$733.9 million. This represents a gearing ratio, calculated in the basis of the Group's total borrowings over shareholders' fund, of 6% (30.6.2003: 5%). The Group's mortgage loan and bank loan bear interest at commercial rate and are secured by certain of the Group's investment properties and leasehold land and buildings in Hong Kong with carrying value of HK\$31.6 million and net book value of approximately HK\$5.4 million respectively. The mortgage loan and the bank loan are repayable in instalments over a period of ten years and repayable within one year respectively. The Note bears interest at 4% per annum and carry the right to convert into shares of HK\$0.05 each in the share capital of the Company at the conversion price of HK\$5.83 per share at 30th June, 2004. The Note was originally matured on 30th June, 2004. On 14th June, 2004, the Company and the holder of the Note agreed to extend the maturity date of the Note from 30th June, 2004 to 30th June, 2007. Save for the extension of the maturity date, the other terms and conditions of the Note shall remain in full force and effect.

In order to generate higher return on the Group's assets, it adopts a set of treasury policies to ensure well balance between cash and listed securities. At 30th June, 2004, the revalued amount of listed securities held by the Group amounted to approximately HK\$28.9 million and an unrealized loss of approximately HK\$8.7 million was provided during the period.

In view of the operation of the Group, the exposure to fluctuation in exchange rates was considered limited and no hedge activity were considered necessary. At 30th June, 2004, the Group had no contingent liability.

## Associates

At 30th June, 2004, the Group had 40.61% equity interest in the group headed by Riche Multi-Media Holdings Limited ("Riche Group"), a company incorporated in Bermuda with limited liability and the shares of which are listed in The Stock Exchange of Hong Kong Limited (the "Stock Exchange"). Riche Group is principally engaged in distribution of films rights and sale of advertising rights for advertisements placing on video products and videos. It had net assets of approximately HK\$300.4 million. The turnover of Riche Group amounted to approximately HK\$31.5 million and the Group had shared a loss after goodwill amortisation of approximately HK\$16.9 million for the six months ended 30th June, 2004. Riche Group will continue to act as our distribution partner in the PRC. As it had good distribution network in the PRC, we believed it would have positive contribution to the Group in the long-term.

In March 2004, the Group acquired 15,480 shares of US\$1 each in Together Again Limited ("TAL"), represented 38.7% of the issued share capital of TAL for a total consideration of HK\$38.31 million. TAL is principally engaged in the provision of artist management services. On the same date, the Group sold the entire issued share capital of Imperial International Limited ("Imperial"), a wholly-owned subsidiary of the Group to TAL. The principal assets of Imperial are its 100% shareholding interests in China Star Management Limited and Anglo Market International Limited. The consideration for the sale of the entire issued share capital of Imperial was satisfied by the allotment and issued of 8,080 new shares of US\$1 each in the share capital of TAL, credited as fully paid, by TAL to the Group. Since then, the Group has an aggregate equity interest of 49% in TAL. The acquisition was expected to strengthen ability on provision of artist management services of the Group and in turn stabilised the supply of artists and the production costs of films. During the period, the Group had shared a profit after goodwill amortisation of approximately HK\$2.0 million from the new group headed by TAL.

## Prospect

Looking ahead, the Group will continue to pursue the PRC as one of its prime market for future growth and expansion. Although the contribution from PRC Market was suffered from the lack of distribution mode and lack of cinemas diversity of the film industry in the PRC, the PRC film industry is expected to grow healthy when the effect of implementation of the CEPA become more apparent. With increasing rising standard of living, the demand for entertainment products in the PRC is promising. The Group believes that its huge film library, strong production capability and widely recognised reputation will be able to take full advantage in the development of the film industry in the PRC.

## Employees

At 30th June, 2004, the Group employed 74 staffs of which 5 staffs are based in China. The directors believe that the quality of its employees is the single most important factor in sustaining the Group's reputation and improving its profitability. The staffs are remunerated based on their work performance, professional experience and prevailing industry practices. Apart from the basic salaries, pension fund and medical schemes, discretionary bonuses and options are awarded to certain staffs according to the assessment of individual performance.