

Management Discussion and Analysis

OPERATIONAL AND FINANCIAL REVIEW

The Group is principally engaged in the manufacture and sale of finished woven fabrics targeting at mid to high-end market in the PRC. The Group has vertically integrated its production process, which include research and development, raw fabric weaving, dyeing and setting, cloth finishing such as pattern pressing and calendaring. The Group's products are used for manufacturing men's and women's fashions such as outer garments, eider down wear, trousers, windbreakers and jackets; and household products such as sofa and curtain.

Turnover

For the financial year ended 30 June 2004, the Group recorded a turnover of approximately HK\$420,692,000 (2003: HK\$345,415,000), representing an increase of approximately 21.8% in comparison to the previous financial year. The increase in turnover was attributable to (i) the market demand of ladies' wear increased with the number of customers; (ii) the launching of new type of woven fabrics which are used in eider down wear and windbreaker; (iii) the Group's participation in trade shows in Shanghai, Beijing and Dubai; (iv) the well established distribution network around the major textile markets in the PRC; and (v) the implementation of second production line which increased the production capacity of the Group. During the financial year ended 30 June 2004, the Group has commenced its sales to the overseas customers directly.

Gross profit

The gross profit margin of the Group slightly decreased from about 29.5% in the previous year to about 28.8% in the current year. The slight decrease in gross profit margin was due to the trivial increase of purchase costs of raw materials in this year, of which, the selling prices would be increased if the purchase costs keep increasing in future, in order to maintain a steady gross profit margin and the addition of a new fabric dyeing production line in the second quarter of 2004, of which, the cost of sales was increased by the depreciation charge of this new production line in certain extent.

Net profit

The Group's net profit attributable to shareholders for the financial year ended 30 June 2004 was approximately HK\$75,354,000, (2003: HK\$68,732,000), approximately 9.6% more than that in 2003. Net profit margin for the year ended 30 June 2004 was approximately 17.9% (2003:19.9%). The decrease in net profit margin compared with previous year was due to the increase in depreciation charges of the new fabric dyeing production line and the establishment of sales liaison offices in Shishi and Guangzhou and administration office in Hong Kong during the year. In addition, the increase of the effective tax rate was mainly due to the expiration of tax holidays of a major subsidiary in the PRC.

Expenses

Selling and distribution expenses amounted to approximately HK\$14,136,000, (2003: HK\$13,652,000), representing approximately 3.4% (2003:4.0%) of turnover for the year ended 30 June 2004. The decrease in percentage of turnover was due to the diminishment of the commission rates paid to the major distributors in this year.

Management Discussion and Analysis

Administrative expenses amounted to approximately HK\$10,071,000, (2003: HK\$6,842,000), representing approximately 2.4% (2003:2.0%) of turnover for the year. Administrative expenses increased by approximately 47.2% when compared with that of 2003. It was mainly due to the hiring of additional management professional and related expenses and the establishment of sales liaison offices in Shishi and Guangzhou and administration office in Hong Kong during the year.

Other operating expenses amounted to approximately HK\$1,389,000, (2003: HK\$835,000), representing approximately 0.3% (2003:0.2%) of turnover for the year. Increase in amount was attributable to more research and development costs spent in 2004 in order to develop new products to meet the market needs.

Finance costs of approximately HK\$1,773,000 (2003: HK\$1,677,000) were maintained at the same level with that of 2003.

Dividend

An interim dividend of HK1.0 cent per ordinary share has been paid to shareholders. The directors recommend the payment of a final dividend of HK1.5 cents per ordinary share (each a "Share") in respect of the year, to shareholders whose names appear on the register of members on 24 November 2004. This recommendation has been incorporated in the financial statements as an allocation of retained profits within the capital and reserves section of the balance sheet. The directors also recommend the offer to the shareholders the right to elect as an alternative, to receive such final dividend wholly or partly by allotment of new Shares credited as fully paid in lieu of cash (the "Scrip Dividend Scheme"), subject to the approval of the shareholders on the payment of final dividend at the annual general meeting of the Company and the granting by the Stock Exchange of the listing of, and permission to deal in, the Shares to be issued pursuant thereto.

The Shares to be issued pursuant to the Scrip Dividend Scheme will rank pari passu in all respects with the Shares in issue on the date of allotment and issue of such Shares save that they will not be entitled to the final dividend for the year ended 30 June 2004.

On condition that the payment of the above final dividend is approved by the shareholders at the annual general meeting of the Company, a circular containing details of the Scrip Dividend Scheme will be dispatched to the shareholders of the Company shortly after the annual general meeting of the Company.

FUTURE PLANS AND PROSPECTS

As a result of the improvement of quality of life in the PRC, the demand for fashionable clothing and quality fabrics increases. Moreover, since the PRC's entry into WTO and elimination of textile quotas in the beginning of 2005, the world-wide quota on the PRC-origin imports of textile products will be gradually removed and consequently, more European and American textile companies will commence their sourcing from China where production costs are much lower than other places. The Directors believe that the above creates ample opportunity for the development of the Group's business.

In order to diversify the customer base of the Group and tap the market potential, the Group plans to strengthen its distribution network to the other textile markets in the PRC and overseas textile markets. The Group intends to continue its expansion of its distribution network by, on one hand, establishing sales points or appointing distribution agents in these new distribution locations and, on the other hand, concreting its existing sales and marketing team in order to further promote the Group's product.

To cope with the expected growth in demand of the Group's product, the Group has completed the establishment of a new production line in May 2004, which is located adjacent to the Group's factory premises for the existing production line for fabric dyeing. This new production line will eventually increase the production capacity by 75%, from 28 million meters each year to 49 million meters.

As a result of the continuous change in the trend of the textile and garment markets, the Group will continue to put effort in research and development of new products to meet the market needs.

Liquidity and Financial Resources

As at 30 June 2004, the Group had net current assets of HK\$152,736,000 (2003: HK\$55,266,000). The Group maintains a strong financial position by financing its operations with the proceeds from the Company's initial public offer and internally generated resources. As at 30 June 2004, the Group had cash and bank deposits of HK\$156,066,000 (2003: HK\$66,422,000). The current ratio of the Group was 303% (2003:174%).

Shareholders' fund of the Group as at 30 June 2004 was HK\$305,145,000 (2003: HK\$160,467,000). The total bank borrowings of the Group as at 30 June 2004, repayable within 12 months from the balance sheet date, were denominated in RMB34,600,000, equivalent to HK\$32,642,000 (2003: HK\$24,151,000), giving a gross debt gearing (i.e. total bank borrowings/net assets) of 10.7% (2003:15.1%).

The financial health of the Group has been strong throughout the year as indicated by the low gearing and high current ratio.

Financing

As at 30 June 2004, the total banking and loan facilities of the Group amounted to about HK\$32,642,000 (2003: HK\$24,151,000), all of which was utilized.

The Board believes that the existing financial resources will be sufficient to meet future expansion plans and, if necessary, the Group will be able to obtain additional financing with favourable term.

The Group also obtained equity financing amounting to approximately HK\$77,100,000 by listing the Company's shares on the Main Board of the Stock Exchange on 10 September 2003. With the support of a shareholder base comprised of predominately long term institutional investors, the Group is in an enviable position to capture the fund market potential in the PRC.

Management Discussion and Analysis

Use of Proceeds from the Company's Initial Public Offering

The proceeds from the Company's issue of new shares at the time of its listing on the Stock Exchange in September 2003, after deduction of related expenses, amounted to approximately HK\$77,100,000. These proceeds were substantially applied up to 30 June 2004 in the following manner and in accordance with the proposed applications set out in the Prospectus:

- as to approximately HK\$47,604,000 for construction of additional production line for fabric dyeing and its ancillary facilities;
- as to approximately HK\$3,197,000 for expansion of distribution network and promotion of the Group's products and trademark;
- as to approximately HK\$5,000,000 for product development (including the establishment of a new research and development centre and acquisition of research and development facilities);
- as to approximately HK\$9,100,000 for general working capital of the Group.

The remaining net proceeds as at 30 June 2004 were placed with banks in the PRC as deposits. The Board is of the opinion that the remaining proceeds will be applied in the future for their intended uses as set out in the Prospectus.

Capital Structure

Since the listing of the Company's shares on the Main Board of the Stock Exchange on 10 September 2003, there has been no change in the capital structure of the Company. The share capital of the Company comprises only ordinary shares.

Foreign Exchange Risk and Interest Rate Risk

For the year ended 30 June 2004, the Group was not subject to any significant exposure to foreign exchange rates risk as the majority of the transactions of the Group were denominated in either Hong Kong dollar or Renminbi. Hence, no financial instrument for hedging was employed.

All bank borrowings of the Group were denominated in Renminbi and at fixed rate basis. The Board is of the opinion that the Group is not subject to any significant interest rate risk.

Charge on Group's assets

As at 30 June 2004, certain leasehold land and buildings, and plant and machinery of the Group with aggregate net book values of approximately HK\$55,859,000 (2003: HK\$24,970,000) and approximately HK\$37,635,000 (2003: HK\$19,379,000) were pledged to banks to secure bank facilities granted.

Capital Expenditure

During the year, the Group invested approximately HK\$61,056,000 (2003: HK\$38,487,000) in fixed assets, of which 42.5% (2003:35.5%) was used for purchase of plant and machinery, 55.5% (2003:64.5%) for construction of new factory premises and the remaining was used for purchase of other fixed assets.

As at 30 June 2004, the Group had capital commitments of approximately HK\$472,000 (2003: HK\$4,732,000) in respect of fixed assets, which are to be funded by the net proceeds from internal resources.

Staff Policy

The Group had 422 employees in the PRC and 4 employees in Hong Kong as at 30 June 2004. The Group offers a comprehensive and competitive remuneration, retirement scheme and benefit package to its employees. Discretionary bonus is offered to the Group's staff depending on their performance. The Group is required to make contribution to a social insurance scheme in the PRC. Also, the Group and its employees in the PRC are each required to make contribution to fund the endowment insurance and unemployment insurance at the rates specified in the relevant PRC laws and regulations. The Group has adopted a provident fund scheme, as required under the Mandatory Provident Fund Schemes Ordinance, for its employees in Hong Kong.

The Group also provides periodic internal training to its staff.

Each of the independent non-executive directors is appointed for a term of 1 year commencing from 1 September each year.

Contingent Liabilities

At the balance sheet date, the Group and the Company did not have any significant contingent liabilities.