

# Management Discussion & Analysis



## Summary Financial Highlights

(HK\$ million)

	2003 (1st half)	2003 (2nd half)	2004 (1st half)	2004 (2nd half)
<b>Turnover</b>	848.2	1,533.7	1,605.1	<b>1,695.8</b>
<b>Gross profit</b>	154.9	238.2	257.6	<b>274.8</b>
<b>EBITA</b>	67.7*	(24.9)	38.0	<b>41.5</b>
<b>Net profit</b>	56.7*	(33.8)	23.3	<b>29.6</b>
<b>Cash flow from operations</b>	6.6	(21.1)	2.9	<b>89.0</b>
<b>Gross margin</b>	18.3%	15.5%	16.0%	<b>16.2%</b>
<b>Net margin</b>	6.7%*	(2.2%)	1.5%	<b>1.7%</b>

\* 2003 first half numbers include an exceptional gain on disposals of associated companies of HK\$21.5 million.

## Business Review and Outlook

Amidst integration challenges, the Group achieved a record revenue of HK\$3.3 billion, 39% higher than the previous year and 151% higher than 2002 before the acquisition of Jardine Logistics. This is due to the full year inclusion of Jardine Logistics revenue and organic growth. The integration of BALtrans and Jardine Logistics businesses onto a common platform have been largely completed during the financial year except for Mainland China, which will be restructured in the near term.

The gross margin of the combined business has continued to improve through emphasis on more profitable businesses, with gross margin bottoming out at 15.5% in the second half of 2003 recovering to 16.0% in the first half and 16.2% in the second half of this financial year. The EBITA of HK\$79.5 million represents a substantial increase of 86% over the prior year. The profit attributable to shareholders was HK\$52.9 million up 131% from the previous year, mainly due to top line growth, continued margin improvement and the turnaround of key operating entities. However, our results have also been held back by provisions and losses of approximately HK\$11.7 million in our US operation, start-up losses of our new offices in Germany of approximately HK\$3 million as well as provision relating to prior year items of approximately HK\$3 million in the UK.

Apart from top line growth and margin improvement, our net cash inflow from operating activities has also recovered to HK\$91.9 million during the financial year due to improved bottom line and better working capital management.

During the financial year, we have set up 6 new offices in Germany, securing our first foothold in the heart of Continental Europe market. We have also acquired Exhibitstrans Logistics Limited (Exhibitstrans), a major exhibitions forwarding company in the PRC market, in order to consolidate our market position, gain access to the attractive automobile and telecommunications equipment market and reduce the cyclical nature of our exhibitions forwarding business.

This financial year is a year of consolidation for the Group during which we have continued to grapple with integration and legacy issues. Whilst such issues continue to weigh on our bottom line performance, we believe that we are putting in place the key building blocks to ensure the longer term success of the Group. Despite the short-term challenges, we will continue to seek to grow the business organically as well as through selective acquisitions outside of Asia to strength our global network.

Looking ahead, we are positive on the rise of Mainland China as the manufacturing powerhouse and we believe our extensive network and our knowledge of the Mainland China market would stand us in good stead and position us as the partner of choice for non-Asian logistics players looking to tap into a reliable and established network in Asia. In conjunction with the opening of the new Baiyun airport in Guangzhou, we have recently obtained Class A License to operate as a full-service freight forwarder in Guangzhou and we are in the process of expanding our business operations rapidly to cope with the growing demand from the Pearl River Delta. We are also positive on the rise of India as a key market and we are in the process of setting up our own offices in India in the coming year.

### Markets

The Group's operation in Hong Kong and Mainland China was the largest contributor to the Group's overall turnover during the period at 47%. This represents an increase of 37% from the previous year due to the inclusion of the full year revenue of Jardine Logistics and the inclusion of 8 month's results of newly acquired BALtrans Logistics (China) Limited. Operating profit increased by 106% over the previous year to HK\$49.5 million.

Southeast Asia (including Taiwan) contributes 23% of group revenue and registered an increase of 90% due to the benefits of integration and business growth on the original combined platform. Operating profit reached a historical record of HK\$11.9 million compared to a loss of HK\$6.1 million in 2003. Thailand achieved a turnaround despite operating as two separate entities during the year with the resulting inefficiency and duplication of resources. It commenced its integration process towards the end of the financial year and is expected to improve its performance in the coming year. Malaysia and Singapore achieved record profits during the period whilst Indonesia showed a recovery progress through the year.

US and Canada contributed 20% of group turnover during the period. The turnover increase of 8% is attributed to the extensive restructuring in the US and the loss of certain customers during the first 12 months of the acquisition. After bottoming out in the first half of the year, the revenue base for the US has begun to grow during the second half of the year. The operating loss for North America is approximately HK\$1.9 million, a significant improvement from an operating loss of HK\$11.2 million last year. The US is the only key country that was still suffering from losses during the financial year, but the US operation has been turned around in the new financial year.

The UK market makes up 10% of the group revenue during the period. The revenue increased by 38% to HK\$314 million. The revenue basis has changed this year to exclude tax and duty disbursements. Therefore, on a comparable basis, the revenue has increased by a much higher rate. This is due to organic growth and the inclusion of full year of results from Jardine Logistics in the UK. The operating profit contribution of the UK office is relatively modest at below HK\$1 million compared to a loss of HK\$5 million in the previous year mainly due to the negative impact of a provision relating to prior year items of over HK\$3 million booked in the second half of 2004.

## Services

### Airfreight

#### Sales revenue in HK\$ million

	North America	UK	Hong Kong and Mainland China	Southeast Asia	Total
<b>2004</b>	362	83	978	356	1,779
<b>2003</b>	342	59	780	191	1,372
<b>% growth</b>	6%	41%	25%	86%	30%

Airfreight revenue increased by 30% to approximately HK\$1.78 billion, making up 54% of the Group's total revenue. As the airfreight business of Jardine Logistics was a much smaller addition to the original BALtrans business, the increase is mainly driven by the strong growth in Asia sales to the European market due to the appreciation of the Euro, the opening of our new German offices and the strong volume growth to the US market in the second half of 2004.

North American airfreight revenue increased by 6% due to the negative impact of the newly acquired Jardine Logistics businesses in the US which required substantial management attention in restructuring and addressing legacy issues and led to revenue decline in the second half of 2003 and the first half of 2004. There was a strong recovery in airfreight revenue during the second half of 2004 to achieve a modest growth for the year due to renewed management drive to focus on sales and marketing after stabilisation of the US operations.

The gross margin for airfreight in 2004 has declined slightly compared with 2003 due to unexpectedly tight aircraft capacity during the traditionally slower months in the second half of the year and the adverse impact from airfreight capacity commitments and bad debts on the Supreme Group, one of the Group's key subsidiaries in the first half.

### Seafreight

#### Sales revenue in HK\$ million

	North America	UK	Hong Kong and Mainland China	Southeast Asia	Total
<b>2004</b>	285	231	459	362	1,337
<b>2003</b>	254	168	271	169	862
<b>% growth</b>	12%	38%	69%	114%	55%

Seafreight revenue increased by 55% to approximately HK\$1.34 billion, making up approximately 41% of the Group's total revenue, with the increase mainly attributable to the full year inclusion of Jardine Logistics businesses.

The seafreight revenue as a whole remained fairly stable during the second half of 2003 and the first half of 2004 as we managed to grow our seafreight revenue globally to make up for the loss of certain US customers during the initial 12 months post-acquisition. The overall seafreight revenue resumed its growth path during the second half of 2004. All markets have enjoyed revenue growth since the second half of 2003 (except for the US) due to robust exports to Europe, Canada and Australia. Towards the end of the financial period, the management has taken steps to substantially strengthen our market position in the Asia-Australia trade and we are confident that this traffic will show marked improvement in growth and contribution in the coming year. We are also looking to increase our business revenue to Spain and France through closer cooperation with our overseas agents.

The overall gross margin for the seafreight business has been negatively impacted by the inclusion of the Jardine Logistics businesses. However, the gross margin has been on an uptrend throughout the financial year, despite the continuous rise of seafreight rates throughout this period. We are confident that such margin improvement will continue with our strengthened market position in the Asia-Australia traffic in recent months.

### Third-party Logistics

The revenue from third-party logistics ("3PL") reached HK\$91.0 million, an increase of 38% over the previous year mainly due to the inclusion of the full year results of Jardine Logistics. Continuing investment in the customer base and facilities with a view to cross-selling other group services to these customers resulted in this division making an operating loss of around HK\$3.4 million.

In the light of strong demand for the 3PL services, we are in the process of reviewing our customer base with a view to bringing in more profitable customers for existing 3PL facilities as well as expanding into new facilities. We believe the 3PL operational performance will improve in the coming year.

### Exhibition Forwarding and Household Removal

The revenue from exhibition forwarding and household removal grew by 15% to HK\$94.1 million mainly due to the inclusion of two months' results for the newly acquired Exhibitstrans. This acquisition has helped to diversify our customer base and reduce the cyclical nature of the contribution from this business.

We believe the market skills of Exhibitstrans combined with our operating and cost control expertise would be highly synergistic going forward.

### Liquidity, Financial Resources and Funding

As at 31st July 2004, the Group possessed cash and cash equivalents of HK\$138.8 million (2003: HK\$110.4 million). The majority of the Group's cash is in either HKD or USD, therefore, exposure to exchange rate fluctuations is minimal. The gearing ratio (total borrowings/total shareholders' funds) for the year was 16.5% (2003: 17.3%). However, the Group was in a net cash position of HK\$71.3 million (2003: HK\$45.5 million).

For the year ended 31st July 2004, total spending on fixed assets was higher than the same period last year. HK\$19.61 million (2003: HK\$6.67 million) was paid for the purchase of fixed assets. HK\$4.02 million (2003: HK\$2.01 million) was received for the disposals of fixed assets.

During the period under review, HK\$4.08 million (2003: HK\$1.01 million) was invested in subsidiaries while HK\$3.61 million (2003: HK\$0.43 million) was invested in joint venture/associated companies.

The Group's funding requirements have been fulfilled mainly by internal resources with some short-term loan/overdraft facilities granted by banks.

The Group's borrowings were mainly in HKD, USD and TWD. Overdraft & short term loan facilities were granted to the Group at normal market interest rates.

As a matter of principle, the Group allows adequate working capital in overseas subsidiaries and transfers excess funds back to the head office. Some of our overseas subsidiaries may use overdraft facilities in foreign currencies. No hedging arrangement is considered necessary since we receive and pay mainly in local currency.

During the period under review there was no significant deviation from the policies above.

### Charges on Group Assets

The whole first floor of Sunshine Kowloon Bay Cargo Centre and the whole 8th floor of New Mandarin Plaza, Tower A were charged to a bank in exchange for general banking facilities for the Group. The Group has placed fixed deposits totaling HK\$1.25 million (2003: HK\$2.45 million) as securities for banking facilities extended to the Group.

### Core Investments and Acquisitions

The BALtrans Logistics agency network, Fondair agency network, Supreme agency network and Jardine Logistics agency network constituted the core investments of the Group during the year.

### Contingent Liabilities

Details of the contingent liabilities of the Group are set out in note 26 to the accounts.

### Staff and Employment

As at 31st July 2004, the Group employed a workforce of 1,478 (2003: 1,330). Total staff remuneration for the year ended 31st July 2004 was HK\$262.4 million including retirement benefit costs of HK\$11.17 million (2003: HK\$192.36 million including retirement benefit costs of HK\$7.97 million).

The Group's remuneration policies, including both salaries and bonuses, are in line with the local practices where the Group and its subsidiaries operate.

The Group follows a policy of encouraging its subsidiaries to send their staff to attend training classes or seminars that are related directly or indirectly to the Group's businesses.