

Report of the Directors

The directors submit their report together with the audited accounts for the year ended 31 December 2004.

PRINCIPAL ACTIVITIES AND GEOGRAPHICAL ANALYSIS OF OPERATIONS

The principal activity of the Company is investment holding. The principal activities of the subsidiaries continue to be the creation, design, development, marketing and distribution of toys and family entertainment activity products. The Group is also engaged in property investment and management business.

An analysis of the Group's performance for the year by business and geographical segments is set out in note 2 to the accounts.

RESULTS AND APPROPRIATIONS

The results of the Group for the year are set out in the consolidated profit and loss account on page 41.

The directors have declared an interim dividend of HK\$0.02 per ordinary share, totalling HK\$31,236,000, which was paid on 6 September 2004.

The directors recommend the payment of a final dividend of HK\$0.04 per ordinary share, totalling HK\$62,541,000.

RESERVES

Movements in the reserves of the Group during the year are set out in the consolidated statement of changes in equity on page 45. Movements in the reserves of the Company during the year are set out in note 23 to the accounts.

Distributable reserves of the Company at 31 December 2004, calculated under the Companies Act 1981 of Bermuda, amounted to HK\$417,625,000 (2003: HK\$481,962,000).

FINANCIAL ANALYSIS

Analysis of bank loans, overdrafts and other borrowings

Particulars of the Group's utilised banking facilities are set out in note 19 to the accounts.

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 season. As at 31 December 2004, trade receivables related to toys operation were HK\$336,433,000 (2003: HK\$267,182,000) and inventories were at a seasonal low level of HK\$36,736,000 or 2.9% of turnover (2003: HK\$29,108,000 or 3.1% of turnover).

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FINANCIAL ANALYSIS (Continued)

Liquidity and financial resources (Continued)

The property investment and management business generated a relatively steady income stream throughout the year. Approximately 95% of the total gross floor area of the Group's investment properties were leased out as at 31 December 2004. Accounts receivables were minimal as at the year end.

The Group's gearing ratio, defined as total bank borrowings expressed as a percentage of total tangible assets, at 31 December 2004 was 3.2% compared to 21.9% at 31 December 2003. The current ratio, calculated as the ratio of current assets to current liabilities, was 2.1 at 31 December 2004 compared to 2.1 at 31 December 2003. As at 31 December 2004, the Group's cash and bank balances were HK\$195,839,000 compared to HK\$471,457,000 at 31 December 2003.

EMPLOYEES

As at 31 December 2004, the Group had a total of 121 employees in Hong Kong, the Mainland China and the United States of America. This compares to 108 employees as at 31 December 2003.

The Group remunerates its employees largely based on industry practice, including contributory provident funds, insurance and medical benefits. The Group has also adopted a discretionary bonus programme for all management and staff and share option plans for its employees with awards under both programmes determined annually based upon the performance of the Group and the individual employees.

CONTINGENT LIABILITIES

Details of the Group's contingent liabilities are set out in note 25 to the accounts.

DONATIONS

Charitable and other donations made by the Group during the year amounted to HK\$1,712,000 (2003: HK\$860,000).

FIXED ASSETS

Details of the movements in fixed assets of the Group are set out in note 13 to the accounts.

PRINCIPAL PROPERTIES

Details of the principal properties of the Group held for investment purposes are set out in note 13 to the accounts.

SHARE CAPITAL

Details of the movements in share capital of the Company are set out in note 22 to the accounts.

FIVE YEAR FINANCIAL SUMMARY

A summary of the results and of the assets and liabilities of the Group for the last five financial years is set out on page 84.

PURCHASE, SALE OR REDEMPTION OF SHARES

The Company has not redeemed any of its shares during the year. Neither the Company nor any of its subsidiaries has purchased or sold any of the Company's shares during the year.

DIRECTORS

The directors who held office during the year and up to the date of this report were:

Executive Directors

Mr. Thomas CHAN Chun Hoo *Chairman*

Mr. Sidney TO Shu Sing

Independent Non-executive Directors

Mr. Allen LEE Peng Fei

Mr. Anthony LO Kai Yiu

Mr. David YU Hon To

Non-executive Directors

Mr. TSIM Tak Lung *Deputy Chairman*

Mr. Charles IP Shu Wing

Pursuant to Bye-law 87(1) of the Company's Bye-laws, at each annual general meeting one-third of the directors of the Company for the time being (or, if their number is not a multiple of three, the number nearest to but not greater than one-third) shall retire from office by rotation provided that the Chairman of the board and/or the managing director of the Company shall not, whilst holding his office, be subject to retirement by rotation or be taken into account in determining the number of directors to retire each year. However, in the spirit of good corporate governance practices, Mr. Thomas Chan Chun Hoo who is the Chairman and Chief Executive Officer of the Company will voluntarily retire from his office at the forthcoming annual general meeting notwithstanding that he is not required by the Bye-laws to do so. Accordingly, Mr. Thomas Chan Chun Hoo together with Mr. Anthony Lo Kai Yiu and Mr. Tsim Tak Lung, both of whom are subject to retirement by rotation under Bye-law 87(1), will retire at the forthcoming annual general meeting but all of them will be offering themselves for re-election at the same meeting.

The Company has received from each independent non-executive director an annual confirmation of his independence pursuant to Rule 3.13 of Chapter 3 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited ("Listing Rules") and the Company still considers such directors to be independent.

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DIRECTORS' SERVICE CONTRACTS

There is no service contract, which is not determinable by the Company within one year without payment of compensation (other than statutory compensation), in respect of any director proposed for re-election at the forthcoming annual general meeting.

DIRECTORS' INTERESTS IN CONTRACTS

No contracts of significance in relation to the Group's business to which the Company or its subsidiaries was a party and in which any director of the Company had a material interest, whether directly or indirectly, subsisted at the end of the year or at any time during the year.

SHARE OPTIONS

Share options are granted to directors, employees and other eligible participants specified under a Share Option Plan ("Plan") and a Share Option Scheme ("Scheme") approved by shareholders of the Company at the Special General Meetings held on 4 May 1998 and 28 June 2002 respectively. Details of the Plan and the Scheme are as follows:

Purpose	:	Plan To attract, retain and motivate high calibre employees.
		Scheme
		(i) To motivate eligible participants to optimise their performance and efficiency for the benefit of the Group; and
		(ii) To attract and retain or otherwise maintain ongoing business relationship with eligible participants whose contributions are or will be beneficial to the Group.
Participants	:	Plan Employees of the Company or any subsidiary (including any executive director of the Company or any subsidiary).
		Scheme
		(i) Directors, employees, consultants, professionals, customers, suppliers, agents, partners or advisers of or contractors to the Group or a company in which the Group holds an interest or a subsidiary of such company; or
		(ii) The trustees of any trust the beneficiary of which or any discretionary trust the discretionary objects of which include any person/party mentioned in (i) above; or

		(iii) A company beneficially owned by any person/party mentioned in (i) above.
Total number of ordinary shares available for issue under the Plan/Scheme and the percentage of issued share capital that it represents as at 23 February 2005	:	<p>Plan 17,942,400 ordinary shares, representing 1.1% of the issued capital.</p> <p>Scheme 47,479,600 ordinary shares, representing 3.0% of the issued capital.</p>
Maximum entitlement of each participant	:	<p>Plan Shall not exceed 25% of the aggregate number of ordinary shares in respect of options that may be granted under the Plan.</p> <p>Scheme Unless approved by shareholders, the total number of securities issued and to be issued upon exercise of the options granted to each participant (including both exercised and outstanding options) in any 12-month period must not exceed 1% of the issued ordinary shares of the Company.</p>
The period within which the ordinary shares must be taken up under an option	:	The options are exercisable in stages and no option will be exercisable later than 10 years after its date of grant.
The amount payable on acceptance of the option	:	<p>Plan HK\$10.00</p> <p>Scheme HK\$10.00 (or such other nominal sum in any currency as the board may determine).</p>
Period within which payments/calls must/may be made or loans for such purposes must be repaid	:	Not applicable.

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SHARE OPTIONS (Continued)

The basis for determining the exercise price	:	Plan Determined by the directors at their discretion, but will not be less than the higher of: <ul style="list-style-type: none">(i) the nominal value of an ordinary share; and(ii) the average (or, in the case of any person who owns ordinary shares possessing more than 10% of the total combined voting power of the ordinary shares of the Company or the shares of its parent or subsidiary corporations, 110% of the average) of the closing prices of the ordinary shares of the Company on The Stock Exchange of Hong Kong Limited ("Stock Exchange") as stated in the Stock Exchange's daily quotation sheets for the 5 trading days immediately preceding the date of grant.
		Scheme Determined by the directors and shall not be less than the highest of: <ul style="list-style-type: none">(i) the closing price of an ordinary share as stated in the Stock Exchange's daily quotations sheet on the date of grant of the relevant option, which must be a business day;(ii) an amount equivalent to the average closing price of an ordinary share as stated in the Stock Exchange's daily quotation sheets for the 5 business days immediately preceding the date of grant of the relevant option; and(iii) the nominal value of an ordinary share on the date of grant.
The remaining life of the Plan/Scheme	:	Plan Remains in force until 3 May 2008. Scheme Remains in force until 27 June 2012.

The following shows the particulars of the share options of the Company granted to directors of the Company and employees of the Group that are required to be disclosed under Rule 17.07 of Chapter 17 and Rule 13(1)(b) of Appendix 16 of the Listing Rules:

Participant	Date of grant	Exercise price HK\$	Balance at 1 January 2004	Number of options			Balance at 31 December 2004
				Granted during the year (Note (1))	Exercised during the year (Notes (2) & (3))	Lapsed during the year	
Plan							
Sidney TO Shu Sing	26 August 1998	0.532	529,000	–	–	–	529,000
<i>Director</i>	27 May 1999	0.506	529,000	–	–	–	529,000
	20 October 1999	0.434	660,000	–	–	–	660,000
	22 July 2000	0.626	551,000	–	–	–	551,000
	21 May 2001	0.297	1,024,000	–	–	–	1,024,000
<i>Continuous Contract</i>	15 May 1998	0.532	2,618,800	–	890,200	–	1,728,600
<i>Employees,</i>	27 May 1999	0.506	962,700	–	450,000	–	512,700
<i>excluding</i>	22 July 2000	0.626	1,579,800	–	157,600	27,000	1,395,200
<i>Directors</i>	21 May 2001	0.297	4,158,200	–	1,185,800	106,000	2,866,400
	28 August 2001	0.294	8,163,000	–	–	–	8,163,000
Scheme							
Sidney TO Shu Sing	9 August 2002	0.199	1,200,000	–	–	–	1,200,000
<i>Director</i>	10 March 2003	0.550	1,200,000	–	–	–	1,200,000
	7 January 2004	1.360	–	1,200,000	–	–	1,200,000
Allen LEE Peng Fei	9 August 2002	0.199	500,000	–	–	–	500,000
<i>Director</i>							
Anthony LO Kai Yiu	9 August 2002	0.199	1,000,000	–	–	–	1,000,000
<i>Director</i>							
TSIM Tak Lung	9 August 2002	0.199	500,000	–	250,000	–	250,000
<i>Director</i>							
David YU Hon To	9 August 2002	0.199	1,000,000	–	500,000	–	500,000
<i>Director</i>							

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SHARE OPTIONS (Continued)

Participant	Date of grant	Exercise price HK\$	Balance at 1 January 2004	Number of options			Balance at 31 December 2004
				Granted during the year (Note (1))	Exercised during the year (Notes (2) & (3))	Lapsed during the year	
Continuous Contract	9 August 2002	0.199	8,977,500	–	1,419,500	134,000	7,424,000
Employees,	10 March 2003	0.550	11,071,000	–	1,079,500	443,000	9,548,500
excluding	7 January 2004	1.360	–	14,382,000	400	302,000	14,079,600
Directors	19 March 2004	1.240	–	11,000,000	–	–	11,000,000

Notes:

- (1) The closing prices of the ordinary shares of the Company on 6 January 2004 and 18 March 2004, being the trading days immediately before the dates on which the share options were granted during the year, were HK\$1.330 and HK\$1.250 respectively.
- (2) The closing prices of the ordinary shares of the Company immediately before the date on which the options were exercised by Mr. David Yu Hon To and Mr. Tsim Tak Lung during the year were HK\$1.240 and HK\$0.990 respectively.
- (3) The weighted average closing price per ordinary share of the Company immediately before the dates on which the options were exercised by continuous contract employees, excluding directors, during the year was HK\$1.194.

The options are exercisable in stages in accordance with the terms of the Plan and the Scheme within ten years after the date of grant. No options were cancelled during the year.

Share options granted are not recognised in the accounts until they are exercised. The weighted average value per option granted during the year estimated at the date of grant using the Black-Scholes option pricing model was HK\$0.812. The calculation of the weighted average value per option granted during the year does not take into account any option granted and forfeited during the year. The weighted average assumptions used are as follows:

Risk-free interest rate	3.94%
Expected life (in years)	10
Volatility	57.3%
Expected dividend yield	1.02%

The Black-Scholes option pricing model was developed for use in estimating the fair value of traded options that have no vesting restrictions and are fully transferable. In addition, such option pricing model requires input of highly subjective assumptions, including the expected stock price volatility. Because of the facts that the Company's share options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, the Black-Scholes option pricing model does not necessarily provide a reliable measure of the fair value of the share options.

Apart from the aforesaid, at no time during the year was the Company or any of its subsidiaries a party to any arrangements to enable the directors and chief executive of the Company to acquire benefits by means of the acquisition of shares in, or debentures of, the Company or any other body corporate.

DIRECTORS' AND CHIEF EXECUTIVE'S INTERESTS AND SHORT POSITIONS IN THE SHARES, UNDERLYING SHARES AND DEBENTURES OF THE COMPANY OR ANY ASSOCIATED CORPORATION

As at 31 December 2004, the interests of each director and chief executive of the Company in the shares, underlying shares of equity derivatives and debentures of the Company and its associated corporations (within the meaning of the Securities and Futures Ordinance ("SFO")) which were required to be notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO, or which were required, pursuant to section 352 of the SFO, to be entered in the register referred to therein, or which were required to be notified to the Company and the Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Companies were as follows:

Long position in shares

Name of director	Name of company	Nature of interest	Number of shares held	Percentage interests held
Thomas CHAN Chun Hoo	Playmates Holdings Limited	Corporate (Note (a))	610,000,000 ordinary shares	39.01%
Sidney TO Shu Sing	Playmates Holdings Limited	Personal	7,300,000 ordinary shares	0.47%
Charles IP Shu Wing	Playmates Holdings Limited	Personal	18,400,000 ordinary shares	1.18%
	Nippon Toys Limited	Personal (Note (b))	1 share	50%
Anthony LO Kai Yiu	Playmates Holdings Limited	Personal	1,400,000 ordinary shares	0.09%
TSIM Tak Lung	Playmates Holdings Limited	Personal	970,000 ordinary shares	0.06%
David YU Hon To	Playmates Holdings Limited	Personal & Corporate (Note (c))	4,000,000 ordinary shares	0.26%

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DIRECTORS' AND CHIEF EXECUTIVE'S INTERESTS AND SHORT POSITIONS IN THE SHARES, UNDERLYING SHARES AND DEBENTURES OF THE COMPANY OR ANY ASSOCIATED CORPORATION (Continued)

Long position in underlying shares of the Company

Name of director	Nature of interest	Number of equity derivatives held	Number of underlying shares (ordinary shares)	Percentage interests held
Thomas CHAN Chun Hoo	Corporate (Note (a))	122,000,000 warrants	122,000,000 shares	7.80%
Sidney TO Shu Sing	Personal	1,460,000 warrants	1,460,000 shares	0.09%
	Personal	6,893,000 share options	6,893,000 shares	0.44%
Allen LEE Peng Fei	Personal	500,000 share options	500,000 shares	0.03%
Anthony LO Kai Yiu	Personal	280,000 warrants	280,000 shares	0.02%
	Personal	1,000,000 share options	1,000,000 shares	0.06%
TSIM Tak Lung	Personal	144,000 warrants	144,000 shares	0.01%
	Personal	250,000 share options	250,000 shares	0.02%
David YU Hon To	Personal	800,000 warrants	800,000 shares	0.05%
	& Corporate (Note (c))			
	Personal	500,000 share options	500,000 shares	0.03%

Notes:

- (a) 610,000,000 ordinary shares and 122,000,000 warrants of the Company were beneficially owned by Angers Investments Limited ("AIL"). All the issued share capital of AIL is beneficially owned by a private company which is in turn wholly-owned by Mr. Thomas Chan Chun Hoo.
- (b) Mr. Charles Ip Shu Wing has a personal interest of one share in Nippon Toys Limited, an associated company of the Group.
- (c) 3,500,000 ordinary shares and 700,000 warrants of the Company were held by a private company which is 50% owned by Mr. David Yu Hon To and 50% owned by a member of his family.

All the aforesaid shares and equity derivatives were beneficially owned by the directors concerned. The percentage shown was the number of shares or underlying shares the relevant director was interested expressed as a percentage of the number of issued shares as at 31 December 2004.

The warrants are exercisable at any time from 24 May 2004 to 23 May 2005, both dates inclusive, at an initial subscription price of HK\$1.42 per share (subject to adjustment) and subject to the terms and conditions under the Warrant Instrument dated 20 May 2004.

Details of the share options held by the directors and chief executive of the Company are disclosed in the above section headed "Share Options".

As at 31 December 2004, none of the directors and chief executive of the Company were interested or deemed to be interested in short positions in the shares, underlying shares of equity derivatives and debentures of the Company or any associated corporation.

SHAREHOLDERS' INTERESTS AND SHORT POSITIONS IN THE SHARES AND UNDERLYING SHARES OF THE COMPANY REQUIRED TO BE RECORDED UNDER SECTION 336 OF THE SFO

Apart from the interests disclosed above in respect of directors and chief executive of the Company, as at 31 December 2004, no other party had an interest or a short position in the shares and underlying shares of the Company, being 5% or more of the Company's issued share capital, as recorded in the register required to be kept under section 336 of the SFO.

MANAGEMENT CONTRACTS

No contracts concerning the management and administration of the whole or any substantial part of the business of the Company were entered into or existed during the year.

MAJOR CUSTOMERS AND SUPPLIERS

The percentages of purchases and sales for the year attributable to the Group's major suppliers and customers were as follows:

Purchases	
– the largest supplier	40%
– five largest suppliers combined	94%
Sales	
– the largest customer	34%
– five largest customers combined	75%

None of the directors, their associates or any shareholder (which to the knowledge of the directors owns more than 5% of the Company's share capital) had an interest in the major suppliers or customers noted above.

Report of the Directors

COMPLIANCE WITH THE CODE OF BEST PRACTICE OF THE LISTING RULES

In the opinion of the directors, the Company has complied with the Code of Best Practice as set out in the Listing Rules Appendix 14 Guidelines throughout the year ended 31 December 2004, with the exception that all non-executive directors of the Company were not appointed for a specific term. Pursuant to Bye-law 87(1) of the Bye-laws of the Company, non-executive directors are subject to retirement by rotation and re-election (if they offer themselves for re-election) at the Company's annual general meetings.

PRE-EMPTIVE RIGHTS

There are no pre-emptive rights provisions in the Bye-laws of the Company nor are there any pre-emptive rights provisions generally applicable under Bermuda law.

AUDIT COMMITTEE

The written terms of reference which describe the authority and duties of the Audit Committee were prepared and adopted with reference to "A Guide for the Formation of an Audit Committee" published by the Hong Kong Institute of Certified Public Accountants.

The Audit Committee provides an important link between the board and the Company's auditors in matters coming within the scope of the Group audit. It also reviews the effectiveness of the external audit and of internal controls and risk evaluation. The Committee comprises four non-executive directors, namely Mr. Anthony Lo Kai Yiu as chairman, Mr. Allen Lee Peng Fei, Mr. Tsim Tak Lung and Mr. David Yu Hon To as members.

SUFFICIENCY OF PUBLIC FLOAT

Based on information that is publicly available to the Company and within the knowledge of its directors as at the latest practicable date prior to the issue of this report, the Company has maintained sufficient public float as required under the Listing Rules during the year.

AUDITORS

The accounts have been audited by PricewaterhouseCoopers who retire and, being eligible, offer themselves for re-appointment at the forthcoming annual general meeting.

On behalf of the Board

Thomas CHAN Chun Hoo

Chairman

Hong Kong, 23 February 2005