Management Discussion & Analysis

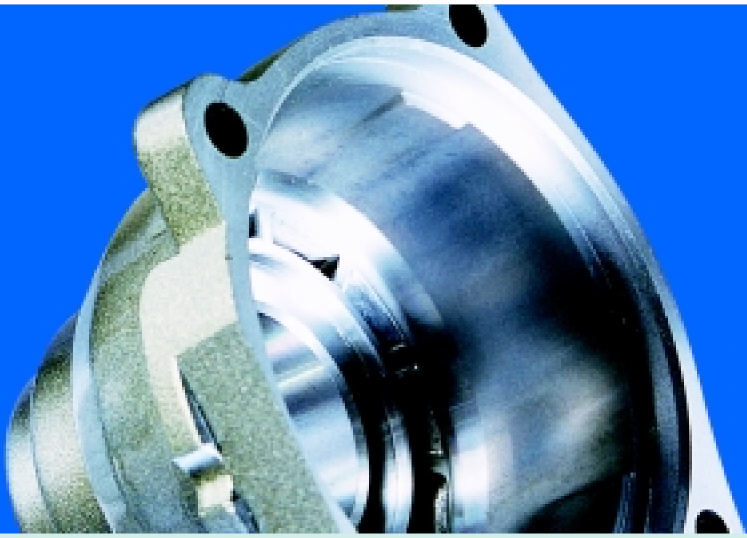
INDUSTRY OUTLOOK

The Gross Domestic Product ("GDP") growth rate of the PRC exceeded 8% in the last three years. The State Information Centre of the PRC has forecasted the national economy to maintain a growth rate of approximately 8.5% in 2005. According to June 2004 issue of Diecasting World, the PRC's total die-casting output in 2002 reached 624,000 tonnes and the projected figures for 2003 and 2004 were 698,000 tonnes and approximately 800,000 tonnes respectively. It is widely expected that the growth of the economy will drive the demand for die casting products.

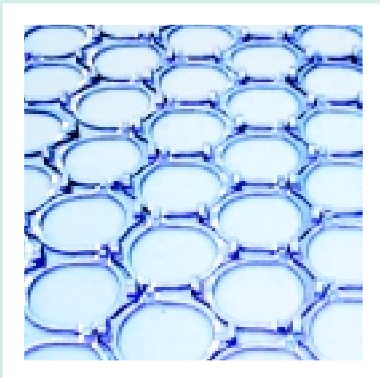
United Metals
is well positioned to capture
the upcoming opportunities

In-depth expertise, a prudent management philosophy and dedication to excellence sustains its leading position

The automotive sector continues to be the most important market for the world die-casting industry, constituting about two-thirds of the total market for die-casting manufacturers in most industrialized countries. Although the expansion rate of the global automotive industry has remained modest, the adoption of aluminium and magnesium parts in automobiles has increased robustly. This coupled with the increased GDP-driven demand for automobiles in the PRC means that the future of the global die-casting market is very bright. In accordance, The North American Die Casting Association reports that, some international automotive industry leaders have expressed their plans to purchase automobile spare parts, components, and whole vehicles from the PRC within the next five years. This shows that there is a continuously enlarging demand for die-castings parts in the automotive industry, which ultimately benefits manufacturers in PRC.



Expansion in technology for product advancement. Dedication to new facilities to expedite full market potential



Along with the increasing living standards in the PRC, an improvement in domestic housing conditions is required. The demand for die-casting parts from the construction industry has also begun to accelerate with high speed. It is forecasted that more development and reconstruction programs in housing will also take place. As a result of the increasing need of construction hardware, family hardware, household equipment and household electric appliances, the die-casting industry is provided with vigorous growth.

Furthermore, many die-casting buyers are now requiring services like machining, heat treatment and surface finishing, and some even demand fully assembled components from die-casting manufacturers. This growing phenomenon will continue to benefit quality die-casting service providers, especially those with fully vertically-integrated production facilities. As such, United Metals, a fully vertically-integrated die-caster for both domestic and overseas customers, is well positioned to capture the opportunities that will arise in the die-casting markets, both locally and internationally.

Management Discussion & Analysis

BUSINESS REVIEW

For the year ended 31st December, 2004, the Group's turnover slightly increased from HK$150,545,000 in 2003 to HK$154,584,000 in 2004, with the Group's aluminium die casting parts continuing to act as its major product category, accounting for 88% of the Group's turnover, followed by zinc parts, accounting for 8% of the Group's turnover. However, due to a number of factors, namely keen market competition, global surges in raw material costs, particularly the prices of petroleum and the alloys required for the production of the Group's various products, and shortages in both electricity and labour, profit attributable to shareholders was affected from HK$25,754,000 in 2003 to HK$8,414,000 in 2004.

The Group managed to minimize the negative impacts brought about by the abovementioned factors and continued to achieve profitable results by leveraging on its sound and flexible business model, as well as its dedication to enhancing production capacity and improving product quality. In accordance with the global die-casting market, the Group was able to expand both its client base and sales orders. In addition, the Group increased its operational efficiency through process automation by deploying more Computerized Numerical Control ("CNC") machinery and thus reducing the negative factors faced by the Group in 2004. The Group has implemented a number of strategies in delivering more sophisticated assembled components to its customers that will allow it to maintain its market-leading position in the coming year.

The Group is extremely confident that with the commencement of new production facilities in Shanghai by the first-half of 2006, further economies of scale will be realized and growth in revenue is expected to resume in future.

OPERATIONAL REVIEW

2004 marked a year of challenges for the Group, the fully vertically-integrated die-caster for domestic and international clients. Despite the challenges, the Group was able to slightly increase its total turnover and solidify its production platform. To counter the factors adversely affecting the present market situation, the Group has been devising and implementing a number of prudent and well-planned strategies, both internally and externally, with the aim to pave the way for United Metals to capture the enormous market potentials ahead.

Machinery advancement

To fulfill the continually increasing global and domestic demand for die-casting services, the Group invested HK$27,026,000 for the advancement of its machinery during the year under review. As part of the investment made for advancement, the Group purchased CNC-related and precision-related machines. The Group also further enhanced its post-production finishing equipment, installing semi-auto surface treatment line, to provide more value-added services to its customers. In addition, to combat electricity shortages faced during the year under review, the Group purchased three additional generators to ensure a stable electricity supply and prevent manufacturing stoppages.

By increasing advanced CNC machineries to 80 sets, at the utilization rate of approximately 55%, the Group benefited from greater economies of scale and was able to accept orders for more higher-margin products.

Product diversification

The Group strived to provide a comprehensive range of product offerings with the aim to offer choices and diversity for leading manufacturers. While aluminium remained the most widely applicable metal alloy and the core income contribution for the Group, representing 88% of the Group's total sales volume in the year under review, zinc and magnesium parts represented 8% and 4% respectively of the Group's total sales volume in 2004 and the demand for these products are continuing to increase. The Group expects that the demand for magnesium die-casting products, in particular, will surge as the need for light-weight products grows.

Stringent cost control

Raw material prices rose by approximately 15% in 2004 and this trend is expected to continue into the coming year. As such, the Group plans to closely monitor price fluctuations to take advantage of lower prices as and when they do occur. In addition, the Group will stringently review product pricing and production planning strategies so as to lower production costs and improve margins.

Diversified clientele with new orders received

During the year under review, the Group further enlarged its client base by gaining new customers from Germany, United States, and within the automotive industry. Turnover generated from the first five customers reduced from 56% to 45%, in keeping with the Group's strategy of lowering risk through diversification. With over 90 clients spanning across the PRC, Japan, Singapore, North America and Europe, the PRC remained the largest shipment delivery country, amounting to 56% of total turnover.

Captured potentials in the automotive market in the PRC

Although market competition was very keen during the year under review and is expected to remain keen in the year to come, the Group is extremely optimistic. This is because the market potential for the die-casting industry is enormous, especially as the demand for automotive die-casting products gains momentum in the PRC. In view of this rising demand, the Group has been constructing new production facilities in the PRC that will commence operation in the first half of 2006 and bring forth great benefits to the Group's overall business.

FUTURE STRATEGIES

Looking forward, the market potentials for the die-casting industry, especially in the PRC market, will continue to be enormous. Capitalizing on its geographical advantage, together with the implementation of a number of sound strategies by the senior management in 2004, the Group has fully positioned itself for future business growth.

In order to cope with the business growth, the Group has been focusing its efforts on the timely completion of its new two-phase production facilities in Shanghai for the provision of automotive parts die-casting services. The facilities will incorporate heavy tonnage machines, suitable for the production of larger die-cast parts. The Group expects that Phase I of the production facilities will be in operation and providing an additional 5,000 tons of productivity during the first half of 2006. United Metal Products (Shanghai) Co., Ltd., the wholly foreign owned enterprise and wholly-owned subsidiary of United Metals, will not only operate the production facilities but also carry out export sales as well as domestic sales in the PRC of the facilities' products. To ensure the high utilization of the manufacturing line and that stringent cost control measures are adhered to in the coming years, the Group is rigorously training an autonomous management team and carefully developing an effective workforce.

To further develop the Group's automotive industry market segment in the coming years, United Metals aims to be certified by the later part of 2005 to fully apply and operate the TS16949 system. The quality system will optimize the Group's production planning for this segment and the resulting reduction in errors and waste will help to increase cost control. The Group will periodically delegate its engineers to ensure that the system maintains optimization.

By the end of September 2005, the Group plans to have Enterprise Resource Planning management software completely installed across all levels. This installation will lead to a host of positive effects, such as improved communication for faster market response, greater work flow efficiency due to more accurate data, better control and competitiveness because of waste reduction, and ultimately higher profit margins and better returns on investments. Furthermore, the management software will allow for more efficient management as it will provide greater operational visibility.

In the coming years, the Group will continue to leverage on its competitive edges by offering one-stop die-casting services and total solutions to its varied clientele. In addition, to increase its orders for higher-margin products, it will improve the tolerance requirements for its products through the use of higher precision machinery.

EMPLOYEES AND REMUNERATION POLICIES

As at 31st December, 2004, the Group had about 2,100 employees (at 31st December, 2003: 2,100) of whom 20 were based in Hong Kong (at 31st December, 2003: 20), 2,080 was based in the Group factories in Dongguan PRC (at 31st December, 2003: 2,080).

Remuneration policies and packages for the Group's employees are based on their performance, working experiences and condition prevailing in the industry. In addition to basic salaries, retirement schemes and medical scheme, discretionary share options and performance bonuses to eligible staff are according to the financial results of the Group and the performance of individual employees. To raise work quality and management abilities of its employees, the Group provides job rotation, in-house training and external training courses to employees.

FINANCIAL REVIEW

Liquidity and financial resources

As at 31st December, 2004, total bank borrowings was HK$9,784,000 (at 31st December, 2003: HK$5,111,000), of which HK$5,084,000 (at 31st December, 2003: HK$2,667,000) would be due within one year and HK$4,700,000 (at 31st December, 2003: HK$2,444,000) would be due after one year. The increase was mainly due to a new bank loan of HK$8,000,000 raised for business expansion purpose during the year under review. The bank borrowings are denominated in Hong Kong dollars and bear interest at rates calculated with reference to Hong Kong Interbank Offered Rate ("HIBOR") plus basis.

In view of the coming capital expenditure requirement of the Shanghai Project, the Group intends to employ additional bank borrowings in the near future. The directors believe that the Group has the capacity to utilize much more bank borrowings while keeping the gearing ratio at a very safe and reasonable level. As at 31st December, 2004, the gearing ratio, in terms of total debts to total assets, stood at 0.18 (at 31st December, 2003: 0.13).

The Group had a net current assets amounting to HK$84,387,000 (at 31st December, 2003: HK$98,423,000) and a current liabilities of HK$29,696,000 as at 31st December, 2004 (at 31st December, 2003: HK$21,565,000). Stock turnover days increased from 48 days at 31st December 2003 to 70 days at 31st December, 2004, resulted from the sharp increase of metal alloys prices and a longer turn-around time due to additional and more complicated value-added jobs. Debtors' turnover days was 80 days as at 31st December, 2004 versus 72 days as at 31st December, 2003.

Capital expenditures on plant and equipment and leasehold improvements totaled HK$30,339,000 (2003: HK$22,234,000) in 2004. Furthermore, about HK$9,978,000 (at 31st December 2003: HK$26,658,000) was committed as at 31st December, 2004 to purchase additional property, plant and equipment.

Net cash generated from operations amounted to HK$5,896,000. The Group's cash on hand and bank balances decreased from HK$62,124,000 as at 31st December 2003 to HK$36,671,000 as at 31st December 2004. The decrease was mainly a result of financing the new plant construction and expansion of production facilities.

Total shareholders' funds increased from HK$161,191,000 as at 31st December, 2003 to HK$165,088,000 as at 31st December, 2004, as a result of HK$8,414,000 of the current year profit being retained.

Exposure to foreign exchange risk

Almost all income and expenditure of the Group were denominated in RMB, HKD and USD in the year under review. With relatively stable HKD/USD and HKD/RMB exchange rates, the Group did not encounter any occasion in which fluctuations in currency had a material effect on its operations or liquidity.

Acquisition and disposal

The Group did not have any material acquisition or disposal of subsidiary and associated company during the year.

Pledge of assets

As at 31st December, 2003, general banking facilities granted by a bank to the Group were secured by the Group's investments in securities amounting to approximately HK$1,225,000. The security was released during the year ended 31st December, 2004.

Contingent liabilities

The Company has given guarantees to a bank in respect of general facilities granted to its subsidiaries. The extent of such facilities utilised by the subsidiaries at 31st December, 2004 amounted to approximately HK$9,784,000 (2003: Nil).

USE OF THE PROCEEDS FROM THE INITIAL PUBLIC OFFERING

Up to 31st December, 2004, the net proceeds of approximately HK$41,600,000 from the Company's issue of new shares at the time of its listing on Main Board of The Stock Exchange of Hong Kong Limited on 6th January, 2003, has been used for the purchase of production facilities, inspection equipments, tooling making facilities as well as expansion of sales and marketing activities in order to increase production capacity, strengthen quality checking and expand sales team.

DIVIDEND

The directors did not declare any interim dividend for the six months ended 30th June, 2004 (2003: HK$0.02 per share).

The directors do not recommend the payment of a final dividend for the year ended 31st December, 2004 (2003: HK$0.02 per share).