

Management Discussion and Analysis

REVIEW OF RESULTS

The Group's consolidated turnover for year 2004 was HK\$1,135,700,000 (2003: HK\$820,200,000), increased significantly by 38% as compared to that of year 2003. Average gross profit margin was maintained at 34%, at the similar level of last year.

During the period under review, the Group successfully turned around and recorded the profit attributable to shareholders for HK\$6,400,000 (2003: loss of HK\$6,200,000).

In year 2004, the global economy was noticeably recovered. The Group has been benefited from the strong economic situation in the United States and launched a series of new products with successful achievements.

For year 2004, the United States and Europe remained the Group's largest markets.

The Group's sales to the United States increased significantly by 82% to HK\$690,700,000 (2003: HK\$378,800,000), representing 61% (2003: 46%) of the Group's total turnover.

The Group's sales to Europe also increased slightly by 1% to HK\$311,300,000 (2003: HK\$307,500,000), representing 27% (2003: 37%) of the Group's total turnover.



Planter



OVERVIEW OF SALES NETWORK

Silk Road Gifts, Inc. (USA)

During the period under review, the company obtained a large amount of orders for giftware items and successfully turned around. The company will continue to concentrate on the giftware business. The major customers are Target Store, Avon, Office Depot, K-mart, and Wal-mart. The major products are candles, and plastic stationery.

Peaktop Technologies (USA) Hong Kong Limited (Hong Kong)

During the period under review, the company recorded a significant increase of turnover. The turnover exceeded HK\$166,000,000, and consequently contributed a significant amount of turnover to the Group. The company's customers are mainly the garden and water gardening chain stores in the United States, namely Lowes' Store. The management strongly believes the strong performance can be sustained. In addition, the company has obtained sales orders from another huge chain store, Home Depot.

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Heissner AG (Germany)

During the period under review, Heissner recorded a profit with the continuous cost control measures even though the turnover grew steadily. The management believes that the profitability of the company will grow steadily in future years.

Waterwerks Pty. Ltd. (Australia)

During the period under review, the company's business continued to prosper during the year under review and will sustain its primary focus to develop the outdoor gardening business in Australia and New Zealand.

PRODUCT DEVELOPMENT STRATEGY

During the period under review, the Group's two major product types for decorating household and garden lifestyle, outdoor decoration product and indoor decoration product, recorded the turnover of HK\$522,400,000 (2003: HK\$401,300,000) and HK\$523,200,000 (2003: HK\$357,600,000) respectively representing a growth of 30% and 46% respectively.



Outdoor Decoration Product

The Group offers a comprehensive line of outdoor decoration products to the customers in the United States, Europe, and Australia, and is actively involved in the marketing programs of the customers. The Group has set up a series of products that are sold on the specialty shelves in the stores. The outdoor water fountains, planters, and technically modified water pumps that were launched at the early 2004 has recorded remarkable turnover with highly recognition from consumers.

Water Fountain

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Indoor Decoration Product

The products include mainly indoor water fountains, candles, figurines, and photo frames. The major market is the United States. During the period under review, the growth of the business was mainly from the Group's major customers, Homedics, Target Store, and Office Depot. After the newly developed indoor water fountains and candles launched into the market, the information has reflected the success of the business.

FINANCIAL AND MANAGEMENT REVIEW

Cost Control

In year 2004, the Group was taking different challenges. The management has taken effective cost control measures to maintain the gross profit margin at 34%.

While operating conditions remain difficult, with prices of both raw materials and labor cost in PRC kept increasing, the Group actively faces the difficulties and has taken various cost control measures in order to minimize the impacts from the negative determinants. During the period under review, the management continuously observed the price trend of all raw materials and kept negotiating with suppliers in order to obtain the most favorable procurement terms. Besides, to further reduce the loss incurred by the increases in prices of raw materials, the management has shortened the validity period for the quotations when receiving sales orders.



Selling, General and Administrative and Other Operating Expenses

Total selling expenses of the Group in year 2004 was HK\$205,800,000 (2003: HK\$149,600,000), representing 18% (2003: 18%) of the total turnover. The increase in total selling expenses was due to the increase in total turnover, leading to the increase in direct selling costs, e.g. freight costs and commission expenses.

Total general and administrative expenses of the Group for year 2004 was HK\$153,200,000 (2003: HK\$136,700,000), representing 13% (2003: 17%) of the total turnover. The increase in total general and administrative expenses was mainly due to larger operations as a result of a higher sales volume in the United States; in fact, the expenses percentage of total turnover has been reduced from 17% in year 2003 to 13% in year 2004.

Other operating expenses of the Group in year 2004 was HK\$10,800,000 (2003: HK\$11,700,000), mainly consisting of provision for doubtful debts of accounts receivable and other receivables of HK\$5,000,000 (2003: HK\$7,700,000) and loss on disposal of subsidiaries of HK\$2,900,000 (2003: nil). The Group has implemented a series of effective credit control measures to minimize provisions for accounts receivable.

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Liquidity, Financial Resources and Finance Costs

The Group finances its operations with mainly internally generated cash flows and banking facilities. As at 31 December 2004, the Group had aggregate available banking facilities of HK\$486,500,000 (2003: HK\$357,500,000), of which HK\$411,300,000 (2003: HK\$295,900,000) was utilized and subject to floating market rates. The Group's cash and cash equivalents at that date amounted to HK\$69,300,000 (2003: HK\$33,700,000), denominated in United States dollar, Hong Kong dollar, Euro and Renminbi. This together with unutilized banking facilities will enable the Group to fund its operational needs.

As at 31 December 2004, the Group's current ratio and quick ratio were 91% (2003: 91%) and 47% respectively (2003: 48%). At that date, the Group's total borrowing amounted to HK\$375,400,000 (2003: HK\$302,500,000), which included short-term borrowing and long-term borrowing of HK\$291,600,000 (2003: HK\$221,700,000) and HK\$83,800,000 respectively (2003: HK\$80,800,000).

The increase in total borrowing was due to the additional trade financing to deal with the peak production period at the end of year 2004. As at 31 December 2004, the Group's gearing ratio, defined as total borrowing as percentage of total assets, was 42% (2003: 42%).



Total finance costs incurred by the Group in year 2004 was HK\$21,800,000 (2003: HK\$21,600,000), at similar level of that of last year. The Group continues to implement prudent financing policy to reduce short-term borrowing as much as possible in order to ensure that the Group will not be affected by short-term uncertainties.

Capital Expenditure

The Group incurred a total capital expenditure of HK\$95,000,000 in year 2004 (2003: HK\$43,100,000), which included: HK\$41,500,000 (2003: HK\$1,600,000) for expanding the manufacturing plants in the PRC, HK\$14,100,000 (2003: HK\$6,400,000) for acquiring machinery and equipment in the PRC, HK\$7,300,000 (2003: HK\$8,500,000) for acquiring machinery, office and production equipment in Europe, and HK\$32,100,000 (2003: HK\$26,600,000) for acquiring other fixed assets and intangible assets.

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Directors' Loans

On 18 August 2004, the Company entered into three loan agreements with Mr. Lin Chun Kuei, Mr. Ng Kin Nam and Mr. Andree Halim (the "Lenders"), pursuant to which each of the Lenders will advance to the Company a director's loan in the sum of approximately HK\$3,900,000 for general working capital requirement. The lenders are directors and have interests in the share capital of the Company. The directors' loans are unsecured, interest-free and repayable within 1 year. Total outstanding as at 31 December 2004, which was in the amount of HK\$5,900,000, was repaid in early April 2005.

On 29 March 2005, the Group entered into three new loan agreements with each of the Lenders, pursuant to which each of them will advance to the Company a director's loan in the sum of approximately HK\$5,900,000 for general working capital requirement. The directors' loans are unsecured, interest-free and repayable on demand.

Foreign Exchange Exposure

For the year 2004, the Group's major revenue was denominated in the United States dollar and Euro, while banking facilities repayment and purchase were made essentially in the corresponding currencies and Renminbi, thus establishing a natural hedge. During the year under review, the Group was exposed to relatively low risks of exchange fluctuations. To further reduce exchange risks, the Group has utilized foreign exchange hedging tools and will continue to closely monitor exchange rate movements.

Contingent Liability

As at 31 December 2004, the Group had contingent liability of HK\$44,800,000 (2003: HK\$5,400,000) for bills discounted with recourse and standby letters of credit to independent parties.

Charge on Assets

As at 31 December 2004, certain assets of the Group with aggregate carrying value of HK\$344,800,000 (2003: HK\$260,300,000) were pledged to secure loan facilities utilized by the Group.



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Employees

As at 31 December 2004, the Group had a total of 8,000 (2003: 7,100) employees. Total staff costs incurred during the year 2004 amounted to HK\$167,400,000 (2003: HK\$149,300,000). The Group offers comprehensive remuneration policies which are reviewed by the management on a regular basis.

The Company adopts a share option scheme which complies with the requirements of the new rules of Chapter 17 of the Rules Governing the Listing of Securities on the Stock Exchange ("Listing Rules") of the Stock Exchange.



PROSPECTS

Year 2004 was an important year for the Group. After years of efforts, the Group's sales network has gradually matured and gained the confidence and supports from customers enabling to turn around in that year. In the next year, under the influence of the uncertain determinants of the raising interest rate, fluctuating crude oil and raw materials prices, shortage of labor force in PRC, the Group is still optimistic to take up the challenges and continues to adopt prudent operating strategy in order to achieve strict control. While the Group strengthens its core business, it will continue its drive to develop its own brand and explore new business opportunities.

As the Group has successfully launched the major products into the market and obtained a large amount of sales orders, the management confirmed the business growth to be sustained and expected a double-digit percentage growth of turnover in the next year. The management continues to take up the challenges with the consistently prudent approach and achieves the maximum returns for shareholders.