

# MANAGEMENT DISCUSSION AND ANALYSIS

## OPERATING ACTIVITIES

### Trading Division

The principal trading activities of the Group and the contribution of each activity to the Group are summarized as below:

	Turnover		Segment Result	
	2004	2003	2004	2003
	HK\$' 000	HK\$' 000	HK\$' 000	HK\$' 000
Electroplating Materials and Chemicals	1,586,352	1,074,180	38,554	28,818
Paint & Coating Chemicals	113,937	90,012	5,725	3,120
Stainless Steel	<u>50,757</u>	<u>39,046</u>	<u>8,146</u>	<u>3,951</u>
Total	<u>1,751,046</u>	<u>1,203,238</u>	<u>52,425</u>	<u>35,889</u>

### Electroplating Materials and Chemicals

Sales performance in 2004 was exceptionally outstanding benefited from high metal prices and strong demand in Asian region. Global imbalance of supply and demand in base metals supported persistent high international prices throughout the year. Nevertheless, overall gross profit margin in most products fell during the year as many factories faced pressure on their margins when they failed to pass on additional costs to end customers.

Sales in precious metal products performed fairly as a result of ample supply in China and keen competition. Offsetting the rises in metal price, total sales in precious metal products slight grew by 3.4% over that of a year earlier. Keen competition from Chinese makers not only led to a reduction in sales quantities but also gross profit margin. On the other hand, satisfactory performance on precious metal products in Singapore was reported during 2004 mainly because of few competitors left in the region due to slim margin and stronger demand from electronics-related industries at the beginning of the year.

Sales of electroplating nickel stayed firm during the year driven by high nickel price and strong demand from industrial use in Asian region. In spite of credits tightening by most Chinese local banks and shortage of power supply in many factories domiciled in China, robust economic growth in China and its neighboring countries like Korea and other South East Asian countries supported the nickel consumption in general. Nevertheless, gross profit margin on nickel was unable to catch up in line with the rise in metal price partly because of

committed premiums charged on long-term customers and partly because of price pressure exerted from reversed pricing strategy initiated by Chinese primary producer causing lower market price selling in China when comparing with international market price. Rising demand in printed circuit board industry also improved their orders to us during the year although price competition remained intensive. Electroplating chemicals performed satisfactory taking advantages of rising metal prices and high demand from Chinese factories especially imitation jewelry industries.

It is expected that tight supply of most metals and chemicals will continue in 2005 but massive volatility in international metal markets prompt us to keep cautious in managing risks associated with purchases and inventory controls. Inventory level as at 31<sup>st</sup> December, 2004 reached to HK\$147.3 million from HK\$89.7 million as at 31<sup>st</sup> December, 2003. The rise in inventory was primarily because most metals' international average prices had advanced ranging from 12% to 84% annually in 2004. Moreover, additional orders to be sold early of year 2005 increased the total inventory level.

### **Paint and Coating Chemicals**

In 2004, demand of most local small-to-medium-sized Chinese factories that manufactured paints and coatings products shrank because of global shortage of raw materials as well as increasing costs in meeting higher standard of production facilities enforced by the Chinese government. However, consumption of foreign-owned and state-owned factories continued to perform well and helped support a rapid growing demand from China's major industries during the year. Amid weak US dollar against major currencies, maintenance stoppage of producers' factories as well as insufficient supply of upstream materials in making paints and coating chemicals, majority of our trading products suffered from insufficient supply during the year, resulting in total sales slightly below our expectation. Average selling prices of major chemicals during 2004 recorded increases from 10% to 47% and total quantities of 2004 sales were advanced by 14.9% over that of 2003.

Profits in 2004 also improved benefited from rally in products prices as well as diversification of products application to different industries. In the coming year, we will continue to solidify our customers' bases to multinational companies of which they are rapidly expanding their production capacity in China. With appreciation of much stricter rules and regulation on environment and health enforced by Chinese government, our products shall gain better competitive edges against other rivals.

### **Stainless Steel**

Stainless steel prices remained robust throughout the year. Average selling price of first-grade stainless steel rose 27.6% in 2004 over that in 2003. The significant rise was mainly driven by the high prices in raw materials like molybdenum, nickel, etc., due to continuous

supply deficits in the world. As many factories hardly charged such large increases in costs to their end customers, these factories either slowed down their purchases or gradually shifted to purchase lower-quality materials. Total sales quantities slightly dropped by 1.8% in 2004 compared with total quantities in 2003. Even so, close to the year end, we were still facing tight supply in stainless steel mills and delayed shipments were not yet solved. Amid high stainless steel prices, 2004 gross profit improved by 48.6% over the previous year and profit margin also enhanced by 14.3%. Nevertheless, inventory level as at 31<sup>st</sup> December, 2004 also climbed to HK\$13.4 million when compared with HK\$8.9 million as at 31<sup>st</sup> December, 2003, representing a rise of 50.6% in yearly basis. It is expected that stainless steel prices will remain firm in 2005 because of solid material costs as well as enduring tight supply.

### **Property Investment Division**

Segmental profit climbed by 40.3% to HK\$20.5 million for the year of 2004.

2004's average occupancy rate for Hong Kong office was reported at 88%, same as that in 2003. But average monthly rental per square foot fell 20.9% to HK\$8 per square foot. As at 31<sup>st</sup> December, 2004, about 6% of total area was available for rent. Atmosphere of Hong Kong property market in general has improved a great deal during 2004 but rental market around Tsimshatsui area remained competitive as abundant supply of vacant office is still available in this area.

Rental for Grade A offices in Shanghai slightly dropped by 2.6% in 2004 when compared with the rent received in 2003. The decrease was primarily a result of one-to-two months' interior renovation period before handing over to new tenants after one major tenant delivered the premises to us in the beginning of the year. Therefore, average occupancy rate dropped to 92.4% in 2004 when compared with 96.6% in 2003, although all spaces were fully rented as at 31<sup>st</sup> December, 2004. Most new tenants are either foreign companies or local state-owned enterprises. In the beginning of 2005, we have concluded several renewal tenancy agreements with a rise of 18.6% in average on monthly rental.

Amid credits tightening and governmental measures to cool down the market, property prices of residential properties in Shanghai remained overheated during the year. Average 2004 occupancy rate was reported at 90.8% where that in 2003 was at 85.7%. As at 31<sup>st</sup> December, 2004, total occupancy rate was 78.4% (31/12/2003: 96.0%). Although demand of residential properties stood firm, increasing supply on investment-purposed residential properties put pressures on average rental growth. Average 2004 monthly rental on each flat slightly fell by 1.4%. In view of furious rise in residential property market, close to the year end, the Group decided to steadily selling 50 units of residential flats located in Haihua Garden, Shanghai.

In January, 2005, we have already sold 2 units with average price of HK\$1,130.60 per square foot. Another 2 units were sold with over HK\$1,300.00 per square foot.

As at 31<sup>st</sup> December, 2004, a surplus arising on revaluation of investment properties amounting HK\$17.9 million was recorded, of which a gain of HK\$9.5 million was credited to income statement and the remaining balance of HK\$8.4 million was credited to reserve. Carrying amount of total investment properties as at 31<sup>st</sup> December, 2004 was HK\$208.3 million and that of properties under for sales was HK\$52.0 million.

### Securities Investment Division

An analysis of the portfolio, current and non-current, by type of securities as at 31<sup>st</sup> December 2004 is as below:

	Market Value of Investments	Percentage of Total
Equities	HK\$ 63.8 Million	33.9%
Debt Securities	HK\$ 40.2 Million	21.4%
Mutual Funds	HK\$ 52.1 Million	27.7%
Long Term Bank Deposits	HK\$ 31.1 Million	16.6%
Equity-Linked Deposits	HK\$ 0.8 Million	0.4%

For the Year ended:	31st December 2004	31st December 2003
Purchase: (at cost)	HK\$ 70.4 Million	HK\$ 93.7 Million
Disposal: (at Market Value)	HK\$ 40.0 Million	HK\$ 74.0 Million

As at 31<sup>st</sup> December 2004, the Group used its own fund to finance 91.9% of total securities holdings and the remaining 8.1% was financed by bank borrowings.

An analysis of the portfolio by currency denomination as at 31<sup>st</sup> December 2004 is listed below:

	US		SGP	Aust.		Japanese
HK Dollar	Dollar	Euro	Dollar	Dollar	Renminbi	Yen
19.6%	66.5%	1.2%	1.1%	3.5%	1.4%	6.7%

In 2004, global economy is clouded with the threat of high oil price, geopolitical instability, twin deficits, i.e. Federal deficits and trade deficits, of the United States, weak job growth in U.S. and Europe, as well as inflationary pressure. The most significant issue during the year was the fate of the U.S. dollar. In the past three years, the U.S. dollars have already declined by about 57.2% against Gold and 52.4% against Euro. To combat against inflation pressure, U.S. Federal Reserve policymakers have raised its benchmark interest rate by 1.25% during 2004 to 2.25% at the end of the year. It is widely believed that the Federal Reserve will tighten its policy further in 2005.

For the year of 2004, huge volatility in the market led us to be more cautious in structuring our portfolio. Having experienced instant changes of market directions and knowing many variables presented in global economies, we have diversified our holdings into alternative investments including traditional equities funds, hedge funds and multi-strategic funds, etc. In 2005, we will remain watchful of the economy and direction of markets.

As at 31<sup>st</sup> December 2004, we recorded an unrealized loss of HK\$0.6 million, which it included an impairment loss of HK\$2.5 million in one of our China's investment. During the year, we disposed of HK\$40.0 million securities, mainly corporate debt, and gained HK\$0.4 million. Dividend and interest income generated from securities portfolio accounted for HK\$1.5 million and HK\$2.6 million respectively in 2004.

## **EMPLOYEES**

The Group employed a staff of 89 at the end of 2004 of whom 63 worked in Hong Kong, 15 worked in Mainland China and 11 worked in overseas offices. Having recognized achievement of good results for 2004, we increased performance rewards to the Group's staff at the year end. Thus, total staff costs for the year 2004 rose by 10.5% to HK\$24.3 million (2003: HK\$22.0 million). In order to retain skilled and experienced staff in the Group, we provide competitive package within the industries and regularly review and monitor the package within the market. The Group also committed to develop staff professional knowledge and encourage them to enroll external and internal training courses. During the year, we have arranged several Putonghua courses aiming at improving communication skills of staff.

## **FINANCIAL RESOURCES AND LIQUIDITY**

The Group's shareholders' fund increased from HK\$ 606.8 million (HK\$1.36 per share) at year-end of 2003 to HK\$ 610.0 million (HK\$1.37 per ordinary share) as at 31<sup>st</sup> December 2004. The small rise of shareholders' fund was primarily because of total dividend distribution of HK\$55.7 million was recognized for the year 2004 when comparing with that of HK\$13.3 million for the year 2003.

The Group held total cash and short-term bank deposits of HK\$ 163.8 million as at 31<sup>st</sup> December 2004, representing a decrease of 20.9% over HK\$207.1 million as at 31<sup>st</sup> December, 2003. The Group also placed HK\$31.1 million cash into long-term bank deposits as of 31<sup>st</sup> December, 2004 (HK\$38.8 million as at 31<sup>st</sup> December, 2003). Including the long term bank deposits, a net borrowing of HK\$107.2 million was reported at the year end of 2004 whereas a net cash of HK\$ 6.0 million was recorded as at 31<sup>st</sup> December, 2003. Net cash outflow from the Group was primarily related to substantial increase in Group's interim

dividend distribution. Increases in inventories of HK\$57.5 million as well as account receivable of HK\$26.0 million also explained the rise in net cash outflow. For the year 2004, the Group raised additional HK\$62.3 million on bank borrowings mainly for financing additional stocks.

An analysis of cash and short term bank deposits by currencies as at 31<sup>st</sup> December 2004 is set out below:

	US		SGP		NT	AUD
HK Dollar	Dollar	Euro	Dollar	Renminbi	Dollar	Dollar
14.7%	75.0%	0.1%	2.3%	5.0%	0.8%	2.1%

### **DEBT STRUCTURE**

Total bank borrowings rose from HK\$240.0 million as at 31<sup>st</sup> December, 2003 to HK\$302.1 million as at 31<sup>st</sup> December, 2004. Gearing ratio, representing total bank borrowing divided by shareholders' fund, was 0.50 as of 31<sup>st</sup> December, 2004. All bank borrowings were in forms of trust receipts and money market loans as at 31<sup>st</sup> December 2004.

All borrowings bear interests on floating rates and matured within one year. Average interest rate charged on borrowings during the year 2003 was 1.52% per annum. Interest expenses in 2004 were HK\$4.1 million, a rise of 6.5% compared to HK\$3.8 million in 2003.

An analysis on bank borrowings by currencies as at 31<sup>st</sup> December 2004 is set out below:

<b>HK Dollar</b>	<b>US Dollar</b>	<b>Japanese Yen</b>
90.2%	4.7%	5.1%

### **FOREIGN CURRENCY RISK**

During the year, the Group's transactions were conducted in Hong Kong Dollars, United States Dollars, Japanese Yen, Euro, British Sterling, Renminbi, Singapore Dollars and New Taiwanese Dollars. The Group used forward exchange contracts to hedge its foreign currency exposure in trading activities when considered appropriate. There were no outstanding forward exchange contracts as at 31<sup>st</sup> December 2004. Short-term borrowings denominated in foreign currencies other than United States Dollars were used to finance assets purchased in the same currencies.