

Managing Director's Operational Review



Masanori KOSAKA
Managing Director

INTRODUCTION

On behalf of the Board of Directors (“the Board”), I am pleased to present to you the Annual Report of the Company for the year ended 20th February 2005.

The economy of Hong Kong grew relatively stronger in the past one year. The steady recovery of the property and stock markets, as well as the turn around of the retail, tourism, hotel and catering industries, helped to move the unemployment rate from its high levels to new lows in recent year. Deflation, which has persisted for years, has markedly improved. Various economic indicators all show that the Hong Kong economy has bottomed out.

This was a challenging but successful year for the Company. On the financial side, the Company achieved a growth in the sales volume by 18.0%, an increase in total debtor balance by 17.6% and a surge in net profit by 22.6%. To share this delightful results with our shareholders, the Board decided to increase the full year dividend amount to 16.0 HK cents. On the operating side, in developing new partners for credit card operation, the Company has signed up with JCB and launched a brand new AEON JCB Travel Card in July 2004 to catch up with the increased outbound tourism to Japan. Moreover, the partnership with China UnionPay has further been strengthened in that China UnionPay has granted us a principal member licence and the Company will issue UnionPay credit cards in the second half of 2005/06. The Company can now issue the five popular brands of credit cards in the market. This provides both the merchants and customers with a wider choice and also facilitates us to issue more card types to capture different customer segments.

PERFORMANCE REVIEW

For the financial year ended 20th February 2005, on an audited basis, profit before taxation was HK\$177.8 million, an increase of 22.0% when compared with last year. After deducting income tax of HK\$31.4 million, net profit for the year increased by 22.6%, or HK\$26.9 million, from HK\$119.4 million in 2003/04 to HK\$146.3 million in 2004/05. The Board has recommended the payment of a final dividend of 10.5 HK cents per share and, together with the interim dividend of 5.5 HK cents, total dividend for the year was 16.0 HK cents per share.

At the operating level, the Company recorded an increase in operating profit before charge for bad and doubtful debts by 0.6% from HK\$489.6 million in 2003/04 to HK\$492.7 million in 2004/05. Operating income before interest expense for the year was HK\$840.5 million, as compared with HK\$840.3 million in 2003/04. Interest income increased by 14.6% to HK\$549.7 million, while interest expense dropped by 27.0% to HK\$85.4 million.

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Although the Company had to spend more on advertising and promoters, the Company continued to exercise tight control on the operating expenses and managed to maintain the cost-to-income ratio at 34.7%. With the drop in unemployment rate, the overall charge-off rate also reduced, resulting in the drop in charge for bad and doubtful debts by 8.4% from HK\$343.9 million in the previous year to HK\$314.9 million.

With the stronger demand for consumer loans, total debtor balance recorded an increase of HK\$341.6 million to HK\$2,277.1 million as at 20th February 2005 from HK\$1,935.5 million as at 20th February 2004. As at 20th February 2005, the Company had bank borrowings amounted to HK\$1,875.6 million. Shareholders' funds were strengthened by 7.2% to HK\$1,269.2 million as at 20th February 2005 mainly due to the increase in retained earnings.

OPERATIONAL REVIEW

Marketing

In the second half of the year, the Company collaborated with four new affinity partners and issued four new cards related to travel, health and beauty. J-WORLD credit cards were launched in September 2004 targeting young executive travellers. ISIC Visa Card was launched in October 2004 extending our service to university students. In November 2004, the Company launched HealthPlus Visa Card, endorsing a health conscious lifestyle, and Aster Visa Card, targeting young female working executives. These new cards will be the driving force for us to expand our customer base in the coming one year. In addition, the Company has also extended its loan and hire purchase service to 52 new affinity members. These newly acquired merchants will be the new channels to recruit new members, which in return would increase both personal loan and hire purchase sales.



Launch of new affinity cards related to travel, health and beauty



Marketing programs and products

The Company had also successfully launched different marketing programs and products with its partners to boost up card sales, personal loan sales and recurrent transactions. This includes the 3G promotion, private sale and discount shopping day, as well as the launch of AEON 100 personal loan program.

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Branch Operation

As at 20th February 2005, the Company has a network of fifteen branches. These branches have been operating as individual marketing centers and they are responsible for card and merchant recruitment, as well as telemarketing activities. This not only provides a focal point to serve the customers' needs but also gathers feedback from the customers, which will be passed to the head office to design new marketing programs.

Customer Service

In expanding services to customers, the Company has joined China UnionPay ATM network in the Guangdong Province. Customers can now enjoy cash advance service at over 8,000 ATMs operating in the Guangdong Province. The Company has also launched new ATMs with built-in new functions, which incorporate Octopus reloading function and provide automatic add-value service for anonymous Octopus cards. This has not only generated more recurrent transactions through credit cards but also created a new source for member recruitment. Besides Octopus reloading and add-value functions, the new ATMs also provide instant lucky draw, as well as information search functions to stimulate cash advance and credit purchase transactions. With the launch of card instalment plan in March 2005, which enables customers to enjoy flexible repayment terms, it will increase credit purchase sales in the coming year.



Octopus reloading service and instant lucky draw at ATM

PROSPECTS

Improving consumer spending reflected restoration of confidence among Hong Kong people towards the continuous recovery of the economic situation. Local interest rates are expected to catch up with those in the United States and this will narrow the gap between bank overdraft and credit card facilities. With the opening of the Hong Kong Disneyland this September, the tourism industry will flourish, which in turn will create more job opportunities for the Company's target customer segments. Despite the competitive operating environment for consumer finance business, the Company will actively pursue a strategy to increase its receivables under the existing well-established market segments. In order to achieve better results, the Company will reinforce its brand image as innovative and adaptive to the needs of the customers. The mission for Year 2005/06 is to extend services that meet the needs of the public, to expand the service coverage areas to create convenience for customers, to enter into other credit related business to offer added-value service to partners, and to explore new business opportunities in China.

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Credit card business will continue to be the core business of the Company, with the primary target on expanding its customer base and increasing its active ratio. With additional new card benefits and convenient services provided to customers, the Company aims to increase the active ratio of new customers and retain the loyalty of existing cardholders. The Company will also cross-sell personal loan, insurance and investment-related products to this enlarged member base to ensure full service coverage. With the well-established infrastructure, the Company will continue to extend its outsourcing business on hire purchase consultation, collection and credit-related services.

Credit Card Business – Retain Existing Base, Acquire New Base

The average card spending per person on lifestyle items is expected to increase with the recovery of the economic situation. To capture this demand, the Company will sign up with more merchants on card instalment plan and also design tailor-made marketing programs for individual merchants, including issuing member discount passport and organizing festivals. Through data mining on existing customer base, the Company can assist merchants to launch special promotion programs to targeted customers. This not only would increase the average card spending, but also help to recruit new members effectively. Since affinity cards can offer value-added benefits to cardholders and create a unique image for merchants, the Company will issue more affinity cards under the five different brands, with a target of at least five in the coming one year. The Company has just launched AMTD MasterCard targeting young executives that have financial needs on investment and financial products. The Company will issue UnionPay credit cards in the second half of 2005/06. The target segment for UnionPay credit cards will be those frequent travellers to China looking for convenient cash advance and credit purchase networks in China.

Based on our past experience, the cooperation with different partners, such as transport service provider, mobile phone and insurance companies, in promoting recurrent transactions using our credit cards, has successfully boosted up our credit purchase sales. The Company will launch different promotion programs with different service providers to attract new customers. This will increase the card active ratio and also retain the loyalty of existing customers.



Tailor-made marketing programs jointly organised with merchants

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On card benefits, the Company will continue to utilize its marketing forces to source new discount merchants in Hong Kong, Macau and China and build up a network of over 9,300 outlets by the end 2005/06. The Company will also source for attractive products from overseas to be offered to our cardholders as bonus point redemption gifts or as special promotion items.



Joint promotion with convenience stores

Cash advance transactions are expected to increase at a fast pace in the second half of this year, following the increase in interest rates and the return of confidence level in job security. In anticipation of such increase, the Company has extended its cash advance service to the Guangdong Province through the co-operation with China UnionPay. In addition, the Company will open up its ATM network to China UnionPay members in May 2005. In view of the influx of tourists from China, the Company will continue to extend its ATM network inside convenience stores, and in other high traffic and convenient locations to capture new customer sectors. More promotion programs on cash advance transactions will be launched, such as instant lucky draw campaigns through ATMs and the offering of cash coupons to our sleeping and inactive customers.

Personal Loan Business – Drive for Growth

The Company will work closely with its merchants to launch different purpose loan programs to satisfy the demand in the market, such as decoration loans, overseas study loans, car loans, motorcycle loans, education loans and beauty loans. With the expansion of its branch and merchant network, the Company also plans to launch revolving loan products in the second half of 2005/06.

Customer Service – Extend Service Coverage

On the extension of service coverage area, besides the UnionPay cards which will be widely accepted by China UnionPay's merchant network throughout China, China UnionPay will open up their merchant network in the Guangdong Province to the Company's cardholders, who will then be able to use AEON credit cards to enjoy credit purchase at China UnionPay's merchant network.

In view of the booming travel activities in Macau, the Company is in the process of setting up a service counter in Macau to offer travel information to its members and at the same to build up a discount merchant network in Macau. The Company targets to develop 50 discount merchants in Macau within the coming year. The Company is also in the process of applying for a licence to operate in Macau and once it is approved, the Company will extend its consumer finance business to Macau.

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Credit-Related Business – Potential to Expand

In addition to cross-selling of insurance products, the Company will also cooperate with its partners to introduce investment products to cardholders. By using its vast customer base, the Company has also introduced catalogue sales on discounted products to its customers. This new source of business not only helps to generate additional revenue to the Company, it also helps to retain the loyalty of our customers.

The Company has been providing collection services to five corporate clients in Hong Kong in the fields of telecommunications, insurance and education. The Company aims to expand its client base to ten this year.

China Business – Establish Operation Model

The call center in Shenzhen now provides back-office support on collection, customer service and telemarketing. In the coming year, the Company plans to train the call center staff on judgment operation so as to cater for the future consumer finance operation in China. In October 2004, AEON Information Service (Shenzhen) Co., Ltd. set up its Guangzhou branch to focus on planning and preparation work to form a business alliance to offer hire purchase products. In addition, the Company will make use of its expertise, know-how and experience by setting up credit-related consultancy companies in the Guangdong Province to capture the potential business opportunities upon opening up of the consumer finance market in China.



Insurance programs launched with partners

Future

The customer base and the merchant network that we have built over these years, coupled with the continuous improvement in customer service quality and product development, as well as the investment that we have made on the infrastructure and business model for future growth and expansion into the PRC market, will provide us with a strong driving force to grow in this competitive operating environment.

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SYSTEMS DEVELOPMENT

The Company will continue to enhance its systems to meet the receivable growth, the customers' needs and expectations and to improve on security, risk detection and efficiencies within the Company. Moreover, the Company will revamp the enterprise-wide contingency plan to cater for any unforeseen circumstances and to ensure a continuous operating environment. The measures in the business continuity plan will be tested on a recurrent basis to ensure their efficiencies in time of need.

During the year under review, the Company had completed the operating systems for card instalment plan and the new functions in ATMs, including Octopus reloading, automatic add-value service and lucky draw. On extension of ATM coverage, the linkage with China UnionPay ATM network in the Guangdong Province was completed in the fourth quarter of the year. For new card system, JCB card brand and four new affinity card types were successfully launched.

In the coming year, the Company will put efforts to integrate the database of credit card and hire purchase system to facilitate future enhancement. Moreover, operating systems for the launch of UnionPay credit cards, the open up of the Company's ATM network in Hong Kong to China UnionPay members and the settlement of card usage within the merchant network of China UnionPay in the Guangdong Province will be completed in the coming year. To ensure high security and stable operating environment, the Company will move the information system division to data center with hot standby function.

HUMAN RESOURCES

The total number of staff as at 20th February 2005 and 20th February 2004 was 272 and 260 respectively. Employees are remunerated according to the job nature and market trends, with a built-in merit component incorporated in the annual increment to reward and motivate individual performance. Apart from medical insurance and provident fund, discretionary bonuses are awarded to employees based on individual performance and the financial performance of the Company. The Company also provides in-house training programs and external training sponsorships to strengthen its human resources.

CONTRIBUTION TO THE SOCIETY

Over the years, we emphasize on three key words, "peace", "people" and "community" in our Company's philosophy. Besides striving hard to provide a reasonable return to our shareholders, the Company also aspires to be a responsible corporate citizen placing special attention on local community and environment needs. During the year, the Company received a bronze award from The Community Chest of Hong Kong in recognition of its donation to support the local community. The Company also organised staff



*Best Environmental Trip Reporting
Competition Award Ceremony*

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donation to participate in the tsunami disaster relief program. Besides, the Company made donations through its charity cards to support vital charity causes in the community and also participated in the activities of environmental conservation, education and cultural exchange through the AEON Fund.

The AEON Fund promotes environmental protection through organising projects including the Third Outstanding Home Environmental Ambassadors Selection, the Award Trip to Kyushu of Japan and the Competition for the Best Environmental Trip Reporting. Besides, the Fund has

committed a three years' sponsorship for the Hong Kong Tree Planting Day and also the formation of AEON Eco Kid Club in early 2005. In addition, the Fund continued to support the organic planting competition for schools, the environmental awards for student ambassadors and the publication of the green magazines.



Hong Kong Tree Planting Day 2005

In the PRC, the AEON Fund continued to involve in the green campus, the scholarship and research programs in Tsinghua University, the tree planting at the Great Wall, and the student exchange programs in Tibet, Yunnan and Beijing.

ACKNOWLEDGEMENT

I am most grateful to our customers, business partners, and shareholders whose generous support in the past few years has successfully guided the Company through the adverse operating environment and has put the Company back on the growth track. I also wish to express my gratitude to the members of the Board for their diligent guidance and support, and to thank the management team and staff for their unstinting efforts and dedication.



Masanori KOSAKA
Managing Director

Hong Kong, 26th April 2005