Management Discussion and Analysis

Mr FAN Cheuk Hung,
Managing Director

Financial Review of Group Operations

Analysis of Turnover, Gross Profit and Margins

The 2004/2005 financial year was a difficult year for Synergis. Notwithstanding the beginning of a rebound in the Hong Kong economy in 2004, the Group was operating under a tough business environment in the property management industry, faced with irrational price competition from small scale management companies in competing for the Property Services Contracts ("PSC Contracts") tenders and the change of outsourcing model by the HKHA from the existing PSC contracts to Property Services Agents contracts, which removes large scale planned maintenance work from the scope of works to be provided by the management company. The resultant outsourcing model radically reduces the ability of companies to achieve cost savings through efficient and effective process management and training because a significant share of a service provider's costs (60% to 70%) have been fixed through a combination of minimum working hours and wages and staffing numbers – that is, even if a service provider is able to improve productivity through the use of technology and/or process improvement, it is contractually bound to continue to employ such numbers of people.

This is further exacerbated by severe price competition in the public sector market, as evidenced by the significant reduction in contract value from the most recent award of PSC contracts upon contract renewal. The impact is shown in Table 1 below. While none of those estates were previously managed by Synergis, it is important to note that the previous service providers were all large scale management companies while the winning service providers are smaller scale companies which may not have invested similarly in management infrastructure and systems.

Table 1: Recent Pricing Trends in HKHA PSC Contracts

Public Housing Estate	Previous Contract Value (contract period – April 2001 – March 2004)	New Contract Value (contract period – November 2004 – October 2007)	% change	Remarks
Chung On Estate; Pok Hong Estate; Cheung Kwai Estate; Nga Ning Court & Cheung Wang Estate	HK$116.4 million	HK$88.8 million	-23.7%	Note 1
Shek Lei (II) Estate	HK$86.7 million	HK$59.4 million	-31.5%	
Kwai Shing (E) Estate & Kwai Hing Estate	HK$95.1 million	HK$55.3 million	-41.8%	Note 2

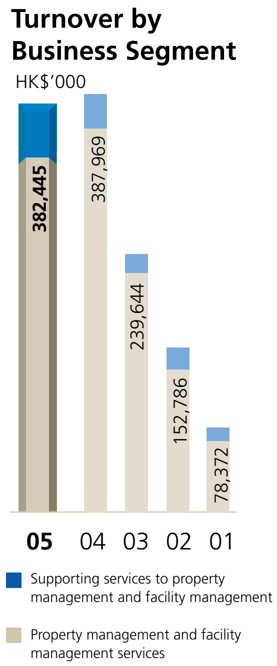
Note 1: The scope of the new contract had been extended by including Cheung Wang Estate.

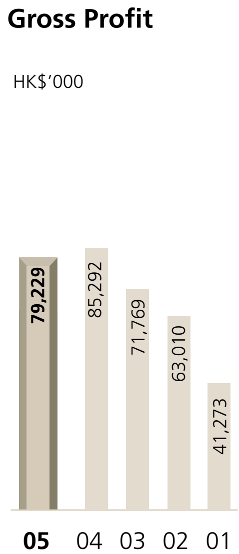
Note 2: The scope for Kwai Hing Estate was relatively reduced.

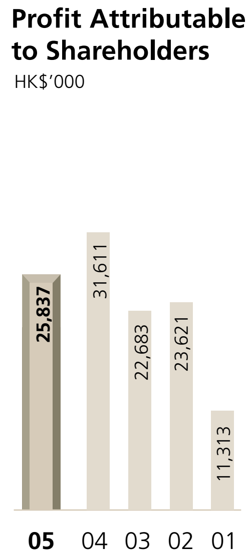
Source: The Government of the HKSAR – Gazette

In recognition of the changing market conditions, Synergis' management team and operational staff promptly adjusted its business development strategy by redoubling its expansion efforts in opportunities outside of the HKHA market. This has been rewarded by further diversification of the Group's portfolio into both the private residential and non-residential markets. These factors coupled with the Group's ability to maintain its existing customer base by achieving a 99% renewal rate, resulted in a turnover for the year of HK$382.4 million, a slight decrease of 1.4% as compared to HK$388.0 million in FY2004. Turnover and gross profit both increased by approximately 4% in the second half of FY2005 compared with the results achieved in the first half of the year.

Consistent with previous years, over 85% of the total turnover was generated from the Group's core business – property management and facility management services. The Group managed to maintain a stable contract-mix ratio amongst Lump Sum ("LS") contracts versus Management Remuneration ("MR") contracts. The same contract-mix ratio of 93% LS contracts: 7% MR contracts was recorded for both financial years.







Labour is the major cost element associated with LS contracts. On average 80% of the cost of sales are labour costs. Over the preceding 12 month period, the overall annual increment for salaries was less than 1%, which was in line with the market. As indicated in past reports, Synergis' compensation policy is to provide a competitive remuneration package with performance bonuses designed to award employees according to their contribution in a variety of areas and commensurate with their job responsibilities. In line with that policy, and in response to the recommendation of the Employers' Federation of Hong Kong to implement a "Performance-Based Pay" policy, the Group began restructuring employees' salary package by applying part of the fixed salary as an incentive bonus tied to performance.

Revenue generated from supporting services to the Group (before inter-segment elimination) for FY2005 increased to HK$60.6 million (FY2004: HK$55.4 million). Except for security services, which were affected by the expiration of the two PSC contracts, all other supporting services reported steady growth during the year. Total gross profit contributed by the supporting services amounted to HK$10.7 million for the year, a 20.2% increase compared to the HK$8.9 million for FY2004. Gross margins for this business segment remained relatively stable at 17.6% (FY2004: 16.1%). For the total business, FY2005 recorded a gross margin of 20.7% (FY2004: 22.0%), although gross profit dropped HK$6.1 million to HK$79.2 million (FY2004: HK$85.3 million).

Other revenues last year included a one-time gain on disposals of security investment of HK$1.4 million and therefore for FY2005 declined by 30.9% to HK$2.9 million (FY2004: HK$4.2 million).

General and Administrative Expenses and Net Profit

Sales, general and administrative expenses for FY2005 were HK$51.3 million, up 1.1% over last year. As a percentage of turnover, costs increased from 13.1% to 13.4%. The increase was primarily attributable to additional costs for recruiting, training and developing the "right" people; depreciation of new investment in IT infrastructure and financial applications; and the full year effect on expenses in connection with public listing of the Group.

As a result, EBITDA for FY2005 declined by 15.0% from HK$40.8 million to HK$34.7 million. Net profit attributable to shareholders dropped by 18.3% from HK$31.6 million to HK$25.8 million. Nevertheless, it is important to note that the operating profit percentage increased from 7.7% in the first six months of FY2005 to 8.4% in the second half of the year.

Share of Losses of Jointly Controlled Entities

Share of losses of jointly controlled entities reduced by 78.5% to HK$166,000 for the reporting year (FY2004: HK$773,000). Improved results were mainly attributed to the joint venture with Shui On Holdings Limited in Shanghai which contributed HK$205,000 profits to the Group after one year of operation, against a share of loss of HK$164,000 in the previous year.

The results of the joint venture with Beijing Strong Science Park Business Services Co. (北京實創科技園經營服務公司) in Beijing also improved, recording a reduced loss of HK$371,000 (FY2004: HK$609,000 loss).

Taxation

Tax on profits decreased 15.8% to HK$5.1 million, compared to HK$6.0 million in the previous year. The effective tax rate for the year was 16.5% against last year's 16.1%.

Cash Flow

Net cash from operating activities is the main source of liquidity to the Group's operation. Cash generated from operating activities increased substantially to HK$36.0 million compared to HK$15.9 million in FY2004 and HK$6.9 million in the first six months of the year. This dramatic improvement in cash flow was a result of the extensive efforts undertaken by management, working closely with the HKHA, all reported in the FY2004/2005 Interim Report. This demonstrates Synergis' staff's ability to address the concerns of its clients and adapt to operational processes accordingly. The cash generation of Synergis' business showed significant improvement in free cash flow per dollar of operating profit, which for FY2005, increased to 78.3% from 12.8% in the previous year.

Apart from payment of Hong Kong profits tax of HK$5.7 million, cash flow from investing activities recorded a net outflow of HK$4.7 million (FY2004: HK$9.0 million outflow), of which:

- HK$5.9 million was used to fund planned acquisition and development of IT applications and the development of a call center with a customised computerised maintenance management system; and

- HK$0.4 million was used for capital injection into Beijing Financial Street Synergis Property Management Company Limited (北京金融街新昌物業管理有限公司) ("Financial Street Synergis"), a new joint venture established in February 2005 to provide facility management services to Xihuan Plaza (西環廣場) in Beijing, in which the Group has a 30% equity interest.

During FY2005, net cash used in financing activities included repayment of bank loans of HK$20.0 million and payment of dividends of HK$16.6 million. After repayment of bank loans, the Group had no debt.

Total cash and cash equivalents at March 31, 2005 decreased by HK$11.0 million or 9.4% to HK$106.1 million as compared to HK$117.1 million at March 31, 2004, though it increased by HK$14.4 million or 15.7% as compared to the balance at September 30, 2004. The Group has no bank debt.

Total Assets and Net Working Capital

At March 31, 2005, the Group's total assets were HK$198.8 million, down by HK$7.3 million or 3.6%, mainly due to reduced bank balances after repayment of bank loan of HK$20.0 million. Net current assets remained strong at HK$145.7 million (2004: HK$137.8 million), up 5.8% with a current ratio recorded at 4.6:1 (2004: 3.4:1), of which HK$185.3 million were liquid assets. The Group maintained a strong balance sheet and is well positioned to develop future business opportunities in both Hong Kong and the Mainland.

Trade Receivables

At March 31, 2005, trade receivables increased by 16.3% to HK$59.9 million (March 31, 2004: HK$51.5 million), of which HK$40.9 million was due from PSC Batch 7 contracts (2004: HK$31.1 million). Increase in receivables for PSC Batch 7 contracts was a result of additional revenues generated from in-take of 3 new sites during the year. Management has made significant progress in the collection of such receivables. At June 3, 2005, over 49% of the outstanding receivables (including approximately 73% with an aging over 90 days) relating to the PSC Batch 7 contracts had been received.

Banking, Financial Management and Treasury

The outstanding bank loan of HK$20.0 million at March 31, 2004 was fully repaid on time, and the Group had no borrowing at March 31, 2005. For day-to-day cash management and maintaining flexibility in funding potential business opportunities, the Group has access to uncommitted short term borrowings and bank guarantee facilities, readily provided by its relationship banks. Total uncommitted banking facilities available to the Group amounted to HK$100.0 million of which HK$96.0 million remained unutilise. Most of the Group's assets and liabilities were denominated in Hong Kong dollars whilst a small part of the cash balances were retained in US dollar deposits (approximately US$0.9 million) at balance sheet date. Our Mainland operations are in the early stages of development and exposure to Renminbi currency fluctuation, in term of assets and liabilities, is not considered material. There is, therefore, no significant exposure to foreign exchange fluctuation. The Group has adopted a prudent treasury management policy and not engaged in any leveraged or speculative derivative products. In view of the substantial cash balances with no bank debt, the Group's exposure to interest rate fluctuation is minimal. An investment policy has been established for monitoring the investments of the Group's uncommitted funds to achieve the highest practicable return on the investments consistent with maintaining adequate liquidity and preservation of capital. The Directors will closely monitor the financial risks associated with the Group's assets, liabilities, rights or obligations.

Business and Operations Review

Hong Kong

For the year ended March 31, 2005, Synergis has progressively expanded its business in both Hong Kong and the Mainland. In Hong Kong, a total of 215 sites were under management, representing an increase of 8.0% compared to last year. Of particular note is the growth in the size of the Group's non-residential facilities portfolio – an increase of 31.2% from 1.34 million sq. m. to 1.76 million sq. m. Despite intense market competition, our contract renewal rate was consistently maintained at 99%. Taking into account our portfolio in the Mainland, the Group managed a total portfolio of 230 sites and over 2.42 million sq. m. of non-residential facilities. The increase, not only in the size of our management portfolio but also its diversity, is proof that despite increasingly difficult market conditions, opportunities exist for Synergis to take advantage of its leadership position through a "total solutions" approach – such requires the continuous investment in our people, processes and technologies.

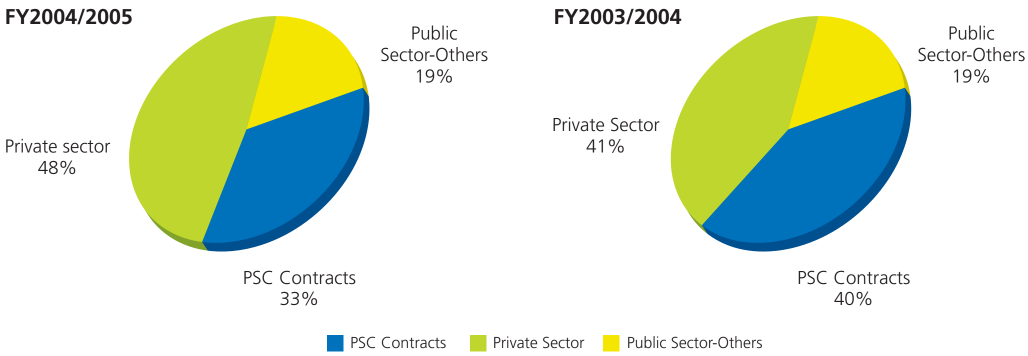
In Hong Kong, the competition in property management market remained fierce in both private and public sectors. As noted, Synergis has strengthened its business development efforts and technological applications in service delivery. Our solutions approach and our people's ability to understand the critical needs of our clients have enabled us to be successful in a number of new private residential projects, including The Paragon (悠然山莊), Billows Villa (浪濤苑), The Hillgrove (漣山), The Aegean (愛琴灣) and Greenview Garden (綠怡花園).

Table 2 below reflects the changing nature of the Group's customer-mix, with a shift towards the private sector, where Synergis has consistently been able to achieve a high renewal rate and where clients understand and appreciate the importance of having a company with a proven track record and the ability to deliver innovative yet practical customised solutions and services to address their needs.

Left:
The Hillgrove

Right:
Hong Kong Heritage Museum

Table 2: Analysis of Turnover of Property Management and Facility Management Services by Customer



The growth in the public residential sector slowed down compared to the previous year. The HKHA has changed the assessment criteria for the new batch of PSC tenders by waiving the requirement on the intake of ex-Housing Department staff and imposing strict requirements on minimum wages and working hours for non-skilled labour. We faced with severe competition from small-scale management companies that have taken a highly aggressive pricing approach in bidding the PSC tenders. As already mentioned in the Interim Report, Synergis has and continues to institute process re-engineering measures to streamline our cost structure and improve competitiveness in this dynamic market environment.

Despite such fierce competition in the public sector, the Group successfully secured three contracts with the Hong Kong Government – the HKHA Headquarters (Blocks 3 and 4), the Hong Kong Heritage Museum and the Hong Kong Heritage Discovery Centre of the Antiquities and Monuments Office. These contracts result in a more diversified portfolio mix for Synergis, enhancing our capability to develop facility management business in different industries.

We are impressed by Synergis' capability in providing comprehensive facility management solutions for AAT's state-of-the-art facilities in a cost-effective way

Mr. Nelson Lee
General Manager, Planning and Services
Asia Airfreight Terminal Co. Ltd.

As further evidence of Synergis' leadership position in the facility management business, which we believe has yet to mature, the Group successfully won contracts from the Hong Kong Jockey Club and the Society of the Prevention of Cruelty to Animals. In addition, the Group's investment in its technological infrastructure, including the Synergis Customer Services Center (Call Center), over the past year has been instrumental in enabling Synergis to continue to differentiate itself and secure business in this market. We successfully extended our service to facility maintenance by securing a facility maintenance contract from Tao Heung Holding Limited (稻香集團有限公司), a large Chinese restaurant group with over 30 business outlets in Hong Kong. Our technological platform has already been deployed in other customer sites; moreover, this contract provides an additional foothold for us to extend our service capabilities to clients operating in multiple dispersed locations.

Mainland of China

While our business in the Zhongguancun (中關村) area of Beijing showed stable growth, we believe that the Group must penetrate Beijing's Central Business District by strategically building a brand presence.

In February 2005, Synergis formed a new joint venture with Beijing Financial Street Property Management Co., Ltd. (北京金融街物業管理有限責任公司). The new joint venture, Beijing Financial Street Synergis Property Management Company Limited (北京金融街新昌物業管理有限公司) will provide professional and quality property and facility management services to Xihuan Plaza (西環廣場) in Xicheng District (西城區) of Beijing. Upon its completion in late 2005, Xihuan Plaza will house a mega shopping mall and modern office buildings with over 180,000 square metres. Financial Street Synergis will manage this new Beijing landmark, which will also serve as a comprehensive transportation hub of railway, underground subway, light rail and public transport.

In Shanghai, with the successful implementation of our management and operational systems in Synergis Shui On Property Management (Shanghai) Co., Ltd. ("Synergis Shui On"), we successfully took over the management of four projects from Shui On Land ("Shui On"). With the intake of Rui Hong Xin Cheng (瑞虹新城) Phase 2 in mid 2005 and the expected completion of the first phase of Chuangzhi Tiandi (創智天地) in late 2005, our management portfolio size in Shanghai alone will increase to 974,000 sq. m. from 446,000 sq. m. in FY2004. Chuangzhi Tiandi will be a multi-function community concentrating on education, technology, culture, research and business incubation with a total area of over 1 million sq. m.

Left:
Corporate Avenue, Shanghai

Right:
Rui Hong Xin Cheng, Shanghai

It was particularly heartening to note that our professional management team received a number of customers' appreciation letters during a traditionally difficult time – tenant handover – of Corporate Avenue (企業天地), a Class A commercial building, and Rui Hong Xin Cheng (瑞虹新城), a large scale residential estate. This again is proof of our success in establishing Synergis' quality management system and corporate culture in operations in the Mainland and providing a solid foundation for Synergis to further increase its market share in the Mainland.

Outlook

While Hong Kong has begun an economic recovery which has gathered pace over the past year, there is still substantial pressure, in both public and private organisations, to control costs and to focus resources on core businesses. Moreover, consumers are not only price conscious, but also demand quality services and attention to their specific needs. The Group is confident that the increasing level of market sophistication will help differentiate Synergis from other competitors because of our strong financial position and solid foundation in delivery of customised management solutions, well-maintained customer relationships and sizeable portfolio.

To cope with the increasing customer expectations, the Group will continue to enhance and deliver innovative and quality services through a "total solutions" approach. Given the somewhat irrational competition in the public rental housing market and the lack of incentive to encourage innovation and process improvement in the current outsourcing model for public rental housing, the Group will focus its efforts on opportunities in market segments where the customer understands and appreciates the

Left & Right:
Tin Yiu Estate

relationship between value, on the one hand, and the importance of quality, professionalism and management systems, on the other. Meanwhile, we shall continue with our efforts to contain costs in order to sustain a reasonable level of profitability in the highly competitive market.

The Group is keen to leverage our established platform of management solutions to benefit from the outsourcing strategy of the Hong Kong government. One example will be the emergence of Real Estate Investment Trust ("REIT") in the market. While the re-launch of REIT by The Link Management Limited ("The Link") may take some time, The Link has been progressively assuming control over the management of the HKHA's portfolio of shopping centres and car parks. The Link will focus on deploying innovative information technology and cost-effective management systems to manage its assets. To maintain a commercially attractive asset portfolio, we believe that The Link would strive to improve the asset quality and maximise returns by working in partnership with strong and reputable business associates. Synergis stands ready to capture this business opportunity as it arises since Synergis is the leading total management solutions provider in the industry.

Besides the Link, property developers in the Mainland have indicated a growing interest in raising capital through REIT activity, particularly given the current austerity program. REIT is regarded as a positive move to provide liquidity to Chinese property developers, enabling them to unlock the real value of their assets. In pursuit of launching a REIT in Hong Kong or overseas markets such as Singapore, most Chinese developers will need to identify an experienced and professional management company to assist them in improving and sustaining the quality and value of their portfolio of properties. Synergis believes that it is well positioned to capture this developing market, particularly given our well-established technology infrastructure and track record of professional and innovative service delivery in the industry.

Establishing a strong foundation and business in the Mainland continues to be another area of focus. Our initial success in "transplanting" our systems does not signify an end to the process but rather

Left & Right:
Our teams in Shanghai

provides a stimulus to it. Synergis will continue to review the most effective means of deploying and customising those systems in our operations in the Mainland. One of the most important areas will be the recruitment, training and development of our local employees not only to enable them to achieve operational excellence, but also to inculcate them with Synergis' core values and culture. The Board of Directors is delighted to note the satisfactory progress on these initiatives, as demonstrated by the appreciation and recognition received from our customers and would like to thank our Mainland teams for their dedication and hard work.

We will continue to strengthen the Synergis brand through striving for service excellence, innovation and practical solutions and by instilling a sense of purpose in our people. With a highly motivated team and customised management systems in place, Synergis is confident to further increase its business and reputation in the coming years.

Fan Cheuk Hung
Managing Director