Management Discussion and Analysis

BUSINESS AND OPERATIONAL REVIEW

Operation Overview

The Group recorded significant growth in sales and net profit attributable to shareholders for the year ended 31 March 2005.

Turnover of the Group for the year ended 31 March 2005 amounted to US$212,955,000 (2004: US$183,747,000), showing a growth of 15.9%. The increase in turnover was mainly driven by increase in sales of apparels of 16.5% during the year. The Group had been benefited from improvement in the general economic conditions in some of the markets in which the Group operated. The growth in sales was also attributed to expansion of the Group's retail network, the effectiveness of the Group's structured and rational promotional strategies and the responsiveness of the Group to consumers' demand. During the year, the Group continued to expand its retail network and had 450 retail outlets as at 31 March 2005 (2004: 412 outlets).

The Group continued to adopt a structured and rational promotion strategy to improve sales without forgoing profit margin. Measures were also adopted to control costs through improvement in sourcing and merchandising capabilities. Gross margin for the year ended 31 March 2005 was 54.3%, comparing to 52.8% for the year ended 31 March 2004. As a result of the improvement in sales and gross margin, gross profit increased by 19.2% to US$115,672,000 (2004: US$97,002,000).

Profit from operations for the year ended 31 March 2005 was US$22,186,000 (2004: US$15,167,000). The increase in profit from operations was mainly attributed to increase in gross profit of the Group. Selling expenses amounted to US$79,390,000 (2004: US$70,257,000), representing an increase of US$9,133,000, which was mainly attributed to increase in sales activities. Selling expenses increased by 13.0% which is below the percentage increase in sales of 15.9%. Administrative expenses for the year ended 31 March 2005 amounted to US$14,103,000 (2004: US$11,403,000). The increase in administrative expenses was mainly attributable to pre-operation expenses and set up cost incurred by the United States retail operation of US$1,295,000. Finance costs for the year ended 31 March 2005 amounted to US$1,231,000 (2004: US$1,459,000). The decrease in finance costs was mainly due to reduction in bank loans.

Net profit attributable to shareholders increased by 45.7% to US$16,378,000 (2004: US$11,240,000). Net profit margin also increased to 7.7% (2004: 6.1%).

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Apparels Sales

About 97.9% (2004: 97.5%) of the Group's turnover was attributed to sales of apparels for the year ended 31 March 2005. Sales generated from retail and distribution of apparels amounted to US$208,575,000 for the year ended 31 March 2005 (2004: US$179,092,000). This represents a growth of 16.5% from last year. Most of the sales have been generated from the retail operation in Asia. As at 31 March 2005, the Group had 450 retail outlets (2004: 412 outlets) with total shop floor area of about 427,000 square feet (2004: 385,000 square feet).

Taiwan

Taiwan remained the largest market of the Group. Sales in Taiwan contributed to about 62.1% (2004: 63.2%) of the Group's total turnover. Taiwan experienced an improvement in its economic conditions in the past year which had a positive impact on the retail sector. The Group continued to consolidate its leading position in this market. During the year, the Group added 12 new outlets in Taiwan. It also enhanced and extended its product ranges with particular focus on kids' products. The management also continued to improve profit margin by adopting cost control measures and undertaking structured and rational promotion activities.

Sales in Taiwan increased by 13.8% to US$132,248,000 (2004: US$116,175,000). Out of the total sales in Taiwan, retail sales amounted to US$123,703,000 (2004: US$107,388,000) and sales derived from apparels distribution activity amounted to US$8,545,000 (2004: US$8,787,000). Operating profit derived from the Taiwan market increased by 28.3% to US$17,131,000 (2004: US$13,355,000). The Group had 233 retail outlets (2004: 221 outlets) as at 31 March 2005 with a total retail floor area of approximately 263,000 square feet (2004: 247,000 square feet).

South Korea

South Korea is a significant market of the Group. Sales attributed to this market represented 23.8% (2004: 21.6%) of the turnover of the Group. The Group considered that the South Korean market had a lot of potential for development and continued to expand its retail network. During the year, 27 new outlets were added. Despite that the retail sector in South Korea had not recovered from the clamp down on consumer credit in the previous year and consumer spending in general remained weak, the Group recorded significant growth in sales and profitability in this market. To counter the unfavourable market conditions in South Korea, the Group had restructured its network of franchisees through closing down under-performed franchised outlets and had adopted flexible promotional strategies to increase competitiveness of its operation. In addition, the Group had also enhanced its sourcing and merchandising capabilities to reduce product costs and to maintain its profit margin. The effectiveness of the Group's strategies was reflected in the significant increase in sales and operating profit for the year ended 31 March 2005.

Sales in South Korea amounted to US$50,757,000 (2004: US$39,693,000) for the year ended 31 March 2005, recording a growth of 27.9%. Operating profit for the year ended 31 March 2005 amounted to US$4,322,000 (2004: US$911,000) representing an increase of 374.4%. As at 31 March 2005, the Group had 132 retail outlets (2004: 105 outlets) in South Korea with total retail floor area of approximately 92,000 square feet (2004: 67,000 square feet).

Management Discussion and Analysis *(continued)*

Singapore

During the year ended 31 March 2005, the Group continued to adopt a concerted marketing and promotion campaign to improve the sales in Singapore. Unprofitable outlets were closed or relocated to more promising locations to improve operating efficiency and profitability. For the year ended 31 March 2005, the Group recorded growth both in sales and in profitability.

For the year ended 31 March 2005, sales in Singapore amounted to US$17,506,000 (2004: US$14,898,000) and represented 8.2% (2004: 8.1%) of the Group's turnover. Operating profit for the year amounted to US$539,000 (2004: operating loss of US$66,000). The Group had 34 retail outlets (2004: 34 outlets) as at 31 March 2005 with total retail floor area of approximately 25,000 square feet (2004: 29,000 square feet).

Philippines

There had been no significant improvement in the economic environment in the Philippines. The Group's operation in the Philippines remained steady. Sales for the year ended 31 March 2005 decreased by 11.0% to US$5,496,000 (2004: US$6,175,000). This operation recorded an operating profit of US$193,000 (2004: US$331,000). The Philippine market contributed to about 2.6% (2004: 3.4%) of the total turnover of the Group. The Group had 41 retail outlets (2004: 41 outlets) in the Philippines as at 31 March 2005 with total retail floor area of approximately 34,000 square feet (2004: 30,000 square feet).

Management Discussion and Analysis *(continued)*

Malaysia

The Malaysian market contributed to about 1.2% (2004: 1.2%) of the total turnover of the Group for the year ended 31 March 2005. During the year, the Group continued to gradually develop this market and consolidated its position. The Group achieved a growth in sales of 19.4% for the year ended 31 March 2005 in this market. The Malaysian market generated sales amounted to US$2,568,000 (2004: US$2,151,000) and operating profit amounted to US$4,000 (2004: operating loss of US$97,000) for the year ended 31 March 2005. The management believed that the Group had already established a foundation for further development in this market. As at 31 March 2005, the Malaysian operation had 10 (2004: 10 outlets) retail outlets with total retail floor area of approximately 13,000 square feet (2004:12,000 square feet).

Other Markets

The Group had decided to set up retail operation in the United States. A management team with extensive retail experience in the United States was set up during the year ended 31 March 2005 to develop and manage the operation. Significant progress was made in areas such as product design, merchandise sourcing and outlet design. The Group's first store in the United States was opened in the East Coast of the United States subsequent to the year end date in April 2005.

Licensing Operation

The licensing operation provides a steady revenue stream to the Group through licensing of the "Hang Ten" trademark and other trademarks owned by the Group to independent licensees. For the year ended 31 March 2005, revenue generated from the licensing operation amounted to US$4,380,000 (2004: US$4,655,000) and represented about 2.1% (2004: 2.5%) of the Group's total turnover.

Capital Structure

On 12 November 2004, every 100 issued and unissued ordinary shares of HK$0.001 each of the Company were consolidated into one ordinary share of HK$0.10 each. The share consolidation increased the nominal value of the ordinary share of the Company and reduced the total number of ordinary shares in issue, and as such might enhance the overall trading prices of the ordinary shares and increase the liquidity of trading of the ordinary shares. As at 31 March 2005, 780,650,000 ordinary shares and 2,016 convertible preference shares were in issue. Total shareholders' funds amounted to US$57,054,000 (2004: US$41,864,000) as at 31 March 2005.

Liquidity and Financial Resources

The Group generally financed its operation by internally generated cash flow and banking facilities provided by its bankers.

For the year ended 31 March 2005, the Group generated US$30,021,000 (2004: US$26,918,000) of cash from operations. As at 31 March 2005, the Group had cash and bank balances amounted to US$25,345,000 (2004: US$12,406,000) and listed funds, which were readily convertible into cash, amounted to US$9,298,000 (2004: US$6,205,000).

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As at 31 March 2005, the Group had financial facilities provided by banks amounting to approximately US$35,139,000, of which US$592,000 had been utilized. Certain of the banking facilities were secured by the pledge of land and building with a net book value of US$1,093,000. Total indebtedness as at 31 March 2005, comprising bank loans and overdrafts of US$592,000 (2004: US$4,650,000), loans from shareholders of US$16,400,000 (2004: US$16,400,000) and loans from minority shareholders of a subsidiary of US$244,000 (2004: nil) amounted to US$17,236,000 (2004: US$21,050,000) and represented 15.3% (2004: 23.9%) of the total assets of the Group.

The loans from shareholders are unsecured and are due for repayment in the year 2011.

Contingent Liabilities

The Group had certain contingent liabilities with respect to withholding tax and value-added tax in Taiwan. Details are disclosed in note 34 to the financial statements.

Human Resources

As at 31 March 2005, the Group had approximately 1,500 full time employees of which 1,100 were based in Taiwan. About 1,270 employees were engaged in sales and marketing functions. The Group offers its employees competitive remuneration packages based on industry's practices and performance of individual employees. The Company had also adopted a share option scheme to which employees may participate. 12,110,000 options have been granted to certain employees of the Group.