Managing Director's Report

Results Review

2005 is the first year of the Group's Three-Year Plan 2005 – 2007. The Group is pleased to report a strong start to the plan. For the first half of 2005, profit attributable to shareholders reached HK$618 million, an increase of 23% over the same period in 2004.

The Group's turnover increased by 19% to HK$23.5 billion. This increase is above our target annual growth rate in our Three-Year Plan. The strength and resilience of our flexible business model has enabled the Group to continue to flourish amidst a backdrop of uncertainties in the market. During this period, consumer markets were faced with the threat of rising interest and energy costs. There were also big changes to the global trade regulatory environment for textile products in general and the implications for China in particular. Also of concern was the impact of the recently announced de-linking of the renminbi and the US dollar. These changes proved to be positive to the Group's business as more and more customers look to retain flexibility in this environment by using our services.

The strong increase in turnover was also partially attributable to sales contribution from several businesses acquired at the end of 2004 and the beginning of 2005. Excluding these acquisitions, turnover still enjoyed a healthy growth of approximately 16%.

The Total Margin rate increased from 9.4% to 10.0% of turnover during the first half of 2005, a reflection of our move to create more added-value for our customers along the supply chain, as well as the development of the licensed brand business.

Core Operating Profit increased 21% from the year earlier despite additional overhead costs incurred for new sourcing businesses (such as Ecko and Mervyn's) where sales will only start to contribute in the second half of the year in a major way. The Group is also investing in additional people and systems to strengthen our infrastructure to cater for the expected growth in the new Three-Year Plan.

In accordance with the new Hong Kong Financial Reporting Standard 2 "Share-based Payments", the core operating profit above reflected a change to include a share option expense of HK$23 million for the first half of 2005. The core operating profit for the corresponding period last year has also been restated to HK$512 million, reflecting share option expenses of HK$20.7 million.

In terms of major non-operating items, the Group has recognized a profit of HK$27.3 million relating to the sale of office premises in Citicorp Center, Hong Kong. These premises belonged to Colby Group Holdings Limited, which was acquired by the Group in 2000. Since then the business has been fully integrated with the rest of the company on the Kowloon side and hence this office space is no longer necessary for self-use.

Segmental Analysis

The softgoods business accounted for 71% of turnover in the first half of 2005, with turnover and operating profits increasing by 23% and 26% respectively. The removal of textile quotas since January 2005 has caused changes and created uncertainties in sourcing, such as the anti-surge safeguard measures and embargoes imposed on Chinese exports by United States and the EU. These developments were fully anticipated by the Group and we have been well-prepared. Our diversified sourcing and comprehensive global sourcing network proved invaluable to our customers in these situations. Growth in the softgoods business was also boosted by new contribution from acquisitions made at the end of 2004.

Turnover from the hardgoods business grew by 12% for the first half of 2005 and accounted for 29% of the Group's turnover. Operating profit was down slightly by 1% over last year. The rate of growth is lower than that of softgoods mainly because this business is seasonally skewed towards the second half of the year, making the first half comparison less important as a measure of business momentum. Performance on a full year basis is expected to be much better.

Geographically, the United States continued to be the Group's major export market, accounting for 69% of turnover for the first half of 2005. The next largest markets were Europe, Canada and Australasia, accounting for 19%, 5% and 4% of turnover respectively. These proportions saw little changes from the same period last year, indicating that the strong growth of the Group's business was generated across the board.

Of particular strength was business in Central and Latin America, where our penetration with leading retailers there has continued since the acquisition of a trading business there two years ago.

However, the rest of the world, which primarily relates to our business in Japan, dropped from 3% to 2% of turnover. The Group has yet to find a way to develop a meaningful presence in that important market despite our good relationship with several large retailers there.

New Business Ventures

Since the end of 2004, the Group has launched the shipments for two more brands under license: Royal Velvet, and Levi's Red Tab. Despite some initial startup operational challenges, the business saw generally good response with leading retailers. As the sales contribution from this business will be skewed towards the latter half of 2005, this division is still incurring a loss during the period under review but is expected to only incur a small loss, or break even on a full year basis. The recent acquisition of Briefly Stated Holdings, Inc. will serve to strengthen our business in this area.

The Group has also formed an important strategic alliance with Daymon Worldwide, the world's largest private label food sales and marketing company. Through their leading position and strong relationship with major grocery and drugstore retail chains, the Group will have access to their more than 100 retail customers. There is strong demand from food retailers to expand their offering of high-quality, value-for-money private label non-food merchandise. While the relationship is just beginning, management believes that this alliance will open up major opportunities in the food and drug retailing sector, bringing significant business in the near term, especially in the hardgoods area.

Acquisitions

A key strategy of the current Three-Year Plan is our two-pronged approach to making acquisitions. Apart from seeking larger acquisitions, which can materially accelerate business growth, the Group has put in place efforts to systematically seek and acquire small-to-medium sized companies as a means to strengthen different areas of business. In a market dominated by smaller players, this will enable us to make acquisitions a regular part of our growth. This strategy is well funded by our net cash balance, as well as our strong cash flow from operations.

For the latter part of 2004, the Group announced four smaller acquisitions including Zee King Trading Company Limited, BMB Apparel Limited, Ralsey Group Ltd. and an unnamed fourth company where formal acquisition procedures were not completed before the announcement. That acquisition has now been completed in the first half of 2005. The company, PromOcean The Netherlands BV, is a corporate premium and promotional products supply company based in Europe.

In addition, in the first half of the year, the Group has acquired the remaining 55% of equity interest of Comet Feuerwerk GmbH. This is a fireworks company in Germany in which the Group already held 45% previously.

The Group has also announced the acquisition of Briefly Stated Holdings, Inc. on 11 August 2005 for a consideration of US$124 million. Briefly Stated is a licensed apparel company based in the United States, focusing on sleepwear, underwear and T-shirts. This acquisition will provide a strong boost for our brand licensing strategy. After becoming part of the Group we anticipate good growth prospects for this business. Further details relating to this acquisition is set out in the Company's announcement dated 11 August 2005.

Financial Position and Liquidity

As indicated above, the Group continues to be in a strong financial position in the period, with more than sufficient cash and cash equivalents amounting to HK$729 million at the end of June 2005. A strong net cash position has been maintained even after the payment of a special dividend of 25 HK cents per share in May.

Normal trading operations are well supported by over HK$17 billion in bank trading facilities. In addition, the Group has available bank loans and overdraft facilities of HK$1.6 billion, out of which only HK$241 million has been utilized.

As of 30 June 2005, the Group has no long-term borrowings, therefore the gearing ratio is not applicable. The current ratio was 1.2, based on current assets of HK$8.8 billion and current liabilities of HK$7.6 billion.

Impact of changes in accounting standards

The Group has adopted certain new or revised Hong Kong Financial Reporting Standards ("HKFRS") and Hong Kong Accounting Standards ("HKAS") (collectively referred to as the "New HKFRSs") in the current period. The impacts of these New HKFRSs are set out as below.

Pursuant to HKAS 17 "Leases", up-front payments made for leasehold land with a carrying value of approximately HK$819 million as at 30 June 2005 (31 December 2004: HK$893 million) are re-classified as prepaid premium for land leases payments instead of fixed assets, which are expensed in the consolidated profit and loss account on a straight-line basis over the period of the leases.

According to HKAS 21 "The Effects of Changes in Foreign Exchange Rates", goodwill arising on acquisition of foreign operations have been treated as assets of the foreign operations and expressed in their respective currencies. At balance sheet date, this goodwill has been translated at closing exchange rates and a difference of HK$13 million so arising have been charged to the exchange reserve.

In accordance with HKAS 39 "Financial Instruments: Recognition and Measurement", investments previously stated at costs of approximately HK$110 million as at 30 June 2005 have been re-classified as available-for-sale financial assets and stated in the balance sheet at fair value of approximately HK$88 million, with the difference of HK$22 million charged to the reserve. In addition, the Group's discounted bills with recourse of approximately HK$822 million, which were previously not recognized but treated as contingent liabilities, have been re-recognized as bills receivable of the Group and the corresponding proceeds received have been accounted for as collateralized bank advances.

Following the adoption of HKFRS 2 "Share-based Payments", the fair value of share options at grant date of HK$23 million (2004: HK$21 million) is charged to the consolidated profit and loss account in the interim period.

HKAS 36 "Impairment of Assets", HKAS 38 "Intangible Assets" and HKFRS 3 "Business Combinations" have been early adopted by the Group in 2004. Accordingly, the Group ceased to amortize goodwill from 1 January 2004 and amortization of goodwill of HK$21 million made in 2004 interim report was reversed. Goodwill is tested for impairment annually and impairment provision or when there is indication of impairment, if any, will be charged to the consolidated profit and loss account.

Foreign Exchange Risk Management

Most of the Group's cash balances are deposited in HK$ or US$ with major banks in Hong Kong. The Group has a HK$41 million short-term revolving loan denominated in Japanese yen as a currency hedge against shares held in Sojitz Corporation (formerly Nissho-Iwai Nichimen), a strategic investment in Japan made during 2001.

Apart from the above, most of the Group's assets, liabilities, revenues and payments are either in HK$ or US$. Therefore, we consider our risk exposure to foreign exchange rate fluctuations minimal.

Foreign exchange risks arising from sales and purchases transacted in different currencies are managed by the Group treasury with the use of foreign exchange forward contracts.

Capital Commitments and Contingent Liabilities

At the date of this announcement, the Group has long running disputes with the Hong Kong Inland Revenue Department involving additional assessments of tax totaling approximately HK$634 million regarding certain non-Hong Kong sourced income and expenses for the years of assessment from 1992/1993 to 2003/2004. The disputes were only initiated in 1999, and have been disclosed in our annual reports since that year. The Group has been working with its accounting and legal advisors in respect of its dealings with the Hong Kong Inland Revenue Department in relation to these matters.

The structure of the Group's offshore sourcing and marketing activities was established at the time of the Group's re-listing on the Hong Kong Stock Exchange in 1992 at which time the Group had sought advice from its external professional advisors. The directors consider that sufficient tax provision has been made in the accounts in this regard and no additional material tax liabilities are expected to finally crystallize.

To cope with the substantial growth in the business the Group has made commitments in July 2005 to purchase additional office space of approximately 35,000 square feet next to our headquarters in Hong Kong. The total consideration was HK$88.3 million out of which HK$17.7 million has been paid. The balance of the consideration will be paid in the second half of 2005. This purchase will reduce the Group's future rental expenses, and improve overall operational efficiency by consolidating other business locations in Hong Kong. The Group has adhered to our disciplined practice of only investing in assets necessary for our core trading business. Hence, the disposal of Citicorp Centre as mentioned earlier.

Other than the above, there are no material contingent liabilities or off-balance-sheet obligations.

Human Resources

As of the end of June 2005, the Group had a total workforce of 7,162, of whom 2,461 were based in our Hong Kong headquarters and 4,701 were located overseas throughout our sourcing network of over 70 offices in 40 countries and territories. The Group offers its staff competitive remuneration schemes. In addition, discretionary bonuses and share options are also granted to eligible staff based on individual and Group performance. The Group is committed to nurturing a learning culture in the organization. Heavy emphasis is placed on training and development, as the Group's success is dependent on the efforts of a skilled, motivated work force. Total staff costs for the first half of 2005 were HK$1,019 million, compared against HK$822 million in the same period last year.

Prospects and progress on Three-Year Plan 2005-2007

The Group is pleased to see a strong start to the current Three-Year Plan in the first half and anticipates a similar momentum for the remainder of 2005.

Our core sourcing business should continue to do well, especially amidst changes and uncertainties in the trade arena. In particular, many retailers who had traditionally relied on their in-house buying organizations are rethinking their strategy at this juncture, and we are well positioned to gain new customers from this front. Growth will also be aided by our two-pronged acquisition strategy, as well as the development of the licensed brand business. Management remains committed to the Plan Target of reaching a turnover of US$10 billion by 2007.

William FUNG Kwok Lun
Managing Director

Hong Kong, 11 August 2005