

Management Discussion and Analysis

FINANCIAL HIGHLIGHTS

For the financial year ended 30 June 2005, the Group recorded turnover of HK\$138.3 million, representing a 27 per cent decrease from the preceding year. The decrease in turnover was mainly the result of increasingly fierce competition in the People's Republic of China (the "PRC") apparel and uniform market. Along with the reduced sales, the Group's profit margin is also reduced to the level of approximate range of 8 to 9 per cent, which was mainly due to heavy pricing pressure and absorption of factory overhead over lesser units of production.

Selling and distribution expenses increased by approximately HK\$3.2 million pursuant to the Group's effort in promulgating an expanded sales network in major cities in the PRC and related promotional campaign, including television advertising. In addition, the substantial increase in other operating expenses of HK\$87.5 million for the year represents mainly non-recurrent impairment of business goodwill in respect of investment in high-tech business of Nano technology and software compression; and also provision for inventories.

During the year, the Group's high-tech nano-technology investment in Zhongke Nanotech Engineering Center Co., Ltd. ("Zhongke Nanotech") has undergone a period of consolidation whereby several major proposed contracts are still in negotiation and have not proceeded to the stage where revenue can be recognized. The Group's share of Zhongke Nanotech's operational loss for the year amounted to HK\$30.8 million.

As a result mainly of the above factors, the Group recorded a net loss of HK\$150.2 million for the year (2004: net profit of HK\$30.3 million), representing a loss per share of HK5.61 cents per share.

BUSINESS AND OPERATIONAL REVIEW

The Group's core business continued to be focused on the design, manufacture and sale of a range of high-end apparel and uniforms. The PRC market remained the most important market segment, accounting for over 80 per cent of the Group's total sales. During the period, the Group's turnover decreased by 27 per cent from the previous period mainly because of the increasingly fierce competition in the PRC apparel market from local competitors and the introduction of more foreign brands into the PRC market. The intensified competition has imparted considerable pricing pressure on the Company. Meanwhile, the retirement of Mr. Ng Leung Tung, the Company's former deputy chairman and executive director, from direct participation in garment operation and management for reason of personal health concern; and the unfavourable emerging factors of group orders in the PRC adopting the form of open bid tender which negatively affected profit margin, all had implications on the Group's operation. On the side of uniform merchandising, during the period the PRC Government initiated the internet bidding of contracts by qualified manufacturers which has increased the pricing exposure and hence competitions in respect of this market segment. In order to maintain its market competitiveness, the Group has adjusted downward the selling prices of its products. The reduction in product pricing and the absorption of factory overhead over fewer units of production have together contributed to the pronounced reduction in the Group's gross profit margin.

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Selling and distribution expenses

In the order of turning around and streamlining the Group's garment business, efforts and resources are deployed in promulgating sales network in major cities in the PRC on a provincial agency basis. The Group's effort in bolstering its sales and marketing initiatives includes the appointment of renowned screen celebrity as spokesperson for the Group's products and rolled out a series of television commercials and exhibitions to enhance its market share in the PRC. These efforts account for the increase in selling and distribution expenses for the year notwithstanding reduced sales.

Share of results of jointly-controlled entities

The Group's share of results of jointly-controlled entities, in the amount of HK\$30.8 million represents share of operational loss from high-tech investment in Zhongke Nanotech. Owing to the nature of the Nanotech business, the business contracts entered are mainly in respect of technology transfer to established conglomerate. The period covered by this annual report witnessed Zhongke Nanotech undergoing a period of consolidation whereby several proposed business contracts are still in negotiation and have not proceeded to the stage where revenue can be recognized. Further, provisions were made of certain business contract receivables of which repayment has been delayed.

Other operating expenses

Significant increase in other operating expenses is attributable to (i) the impairment of the Group's investment in software compression technologies; and related goodwill balance; (ii) the impairment of goodwill in respect of high-tech investment in Nano technologies applications; and (iii) provisions for inventories.

Notwithstanding that the "Smartcompresz" series of information technology compression products launched by the Group's investment vehicle, Global Network Corporation, had been scientifically proven to execute superior electronic data compression exceeding other similar products in the international market, Global Network has experienced severe difficulty in opening up the PRC market and achieve sustainable profitability, due to the very high rate of counterfeit copies and other problematic situations with the PRC software market. There is an increasing appreciation of the difficulty in demonstrating the eventual return with continual investment of the Group's resources. Accordingly, the resources may be more appropriately dedicated to other of the Group's business and new emerging investments. In light of the foregoing considerations, the Board concurred with a full impairment of the investment cost and goodwill involved of HK\$37.1 million.

Additional impairment is made in respect of the Group's goodwill in respect of investment in Zhongke Nanotech group of companies, in the amount of HK\$31.5 million. In March 2004, the Group acquired additional equity interest in Zhongke Nanotech at a provisional consideration subject to adjustment in the event the Zhongke Nanotech failed to attain a guaranteed profit. Details of the adjustment and guaranteed profit are disclosed in the Company's circular to its shareholders of 13 April 2004. The due course of event subsequent to acquisition confirmed the failure on part of Zhongke Nanotech in meeting the guaranteed profit. The current year set-back in financial performance of Zhongke Nanotech group of companies highlighted the fluctuation in earnings in respect of this high-tech industry segment. Upon prudent consideration by the directors, full provision is made of the related goodwill balance. Further, provision for inventories in the amount of HK\$13.4 million has been made to certain of the Group inventories; for which the sales effort will be mitigated under the Group's directive in re-dedicating its future direction in respect of its garment business.

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LIQUIDITY AND FINANCIAL RESOURCES

The Group maintains a healthy financial position. The Group's net current assets amounted to over HK\$340 million as at the reporting end date; and the current ratio maintained a very high of over 10 times. As at 30 June 2005, the Group's interest-bearing borrowings were exclusively finance lease payables of minimal magnitude.

The Group has obtained available bank credit facilities which are secured by certain of the Group's pledged bank deposits of approximately HK\$14.8 million; short term investments of approximately HK\$7.8 million and corporate guarantees given by the Company. During the year, these available bank credit facilities have been utilized in trade credit financing.

As at 30 June 2005, the Group's cash and bank balances, which were principally Renminbi and Hong Kong dollar denominated, amounted to over HK\$230 million. The Group was not exposed to any substantial risk in foreign exchange fluctuations.

CAPITAL STRUCTURE, GEARING LEVERAGE AND USE OF PROCEEDS

As at 30 June 2005, the capital structure of the Company is constituted exclusively of 2,941,487,600 ordinary shares of HK\$0.10 each. Apart from options to subscribe for shares in the Company, there are no other capital instruments in issue.

The Group generally finances its operation with internally generated resources. The Group's gearing ratio, measured on the basis of total borrowings as a percentage of total assets, remained at a low level over the two years at less than 1 percent.

During the year on 13 January 2005, the Company raised share issue proceeds, net of related expenses, of approximately HK\$95 million from the issue of 489,000,000 new shares in the Company under a top-up placing and subscription arrangement. The resulting net proceeds will be used for general working capital of the Group and/or any future possible acquisition. At the present stage, the share issue proceeds has been retained as general working capital of the Group.

EXPOSURE TO FLUCTUATION IN EXCHANGE RATE

The majority of the Group's transactions and borrowings are denominated in Hong Kong dollars and Renminbi, and therefore the Group's exposure to exchange rate fluctuation is relatively insignificant. In general, the Group mainly utilizes its Renminbi income receipt for operating expenditures in China and does not use any financial instruments for hedging purpose.

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MATERIAL ACQUISITIONS AND SIGNIFICANT INVESTMENTS HELD

There were no material acquisitions and disposal of subsidiaries and associated companies during the year.

The significant investment held by the Group as at 30 June 2005 includes principally a 55% equity interest in Zhongke Nanotech Engineering Center Co., Ltd. ("Zhongke Nanotech"), a PRC limited liability company engaged in the development and sale of nano material and related products. Zhongke Nanotech is a jointly-controlled entity established amongst the Group, the Chinese Academy of Science and certain other joint venture partners. The headquarter of Zhongke Nanotech is based in Beijing, the PRC, and currently contained a strong research team of over 40 scientific researchers, including Mr. Jiang Lei, the chief scientist of China 863 project in nano-technology, and various senior researchers of doctoral and master's degrees. More than 30 patents of the nano-technology research projects had already been filed. In addition, Zhongke Nanotech also operates a second industrialization plant in Suzhou, the PRC, which will be engaged in the production of Nano high elastic plastic and Nano metallic paint; Nano interior and exterior paint; and Nano paste. The Group's interests in Zhongke Nanotech group of companies are accounted for as interests in jointly-controlled entities in the accompanying audited financial statements.

As at 30 June 2005, the Group's aggregate carrying value in respect of its investment in Zhongke Nanotech group of companies, comprising share in net assets, amounted to HK\$19.5 million.

The net sharing in result, after minority interest, in Zhongke Nanotech group of companies for the year ended 30 June 2005 and as reflected in the accompanying audited financial statements amounted to a loss of HK\$30.8 million.

PLEDGE OF ASSETS

The Group's bank borrowing facilities are secured by certain of the Group's pledged bank deposits of HK\$14.8 million; short term investments of approximately HK\$7.8 million and corporate guarantees given by the Company.

CONTINGENT LIABILITIES

The Company and the Group do not have contingent liabilities of material amounts outstanding as at 30 June 2005.

EMPLOYEE

At 30 June 2005, the Group employed approximately 700 employees in our factory premises and approximately 17 staff in Hong Kong. In addition to competitive package offered to the employees, other benefits for eligible candidates include contributions to mandatory provident fund, group medical and accident insurance. On-going training sessions were also conducted to enhance the competitiveness of the Group's human assets. The Company also maintains a share option scheme, pursuant to which share options may be granted to directors, executives and employees of the Company to provide them with incentive interest in the growth of the Group.