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Management Discussion & Analysis



SNP Yau Yue Paper Products Limited

BUSINESS AND FINANCIAL REVIEW

2005 was a remarkable year for SNP Leefung. In May 2005, the Company completed the acquisition of a 60% stake in SNP Yau Yue Paper Products Limited (“SNP Yau Yue”, formerly known as Yau Yue Paper Products Limited) from the founders of SNP Yau Yue for an aggregate cash consideration of HK\$68.4 million. In July 2005, the Company raised HK\$120 million, before expenses, by way of a Rights Issue of 100,681,729 Rights Shares at a price of HK\$1.2 per Rights Share on the basis of one Rights Share for every four existing Shares held.

During the year under review, we were able to attain sound operating and financial results under a very competitive market environment. The Group posted a record turnover of HK\$1,700 million, up from HK\$974 million, representing an increase of HK\$726 million, approximately 75% over last year. The increase was attributed to the inclusion of the full-year turnover from the pop-up business which amounted to approximately HK\$547 million and the turnover

contributed by the newly-acquired SNP Yau Yue of approximately HK\$215 million. Our core printing businesses continue to provide positive contributions in terms of operating profits and cashflows, the EBITDA has improved significantly from HK\$116.7 million for the year 2004 to HK\$177.5 million for 2005.

Despite the pressure from the increase in operating costs such as fuel and oil charges, labour costs, etc, we were able to maintain our gross profit margin at 20%, which was slightly down from 23% in last year. Cost savings were achieved through effective reduction in overhead expenses. We continue to strive for stringent cost control, low bad debt levels and the enhancement of cost efficiency across the Group.

Finance costs have increased from HK\$4.1 million to HK\$26.6 million as a result of the additional interest costs incurred for the additional loans drawn for the acquisition of subsidiaries and the continual increase in the interest rates.

Management Discussion & Analysis



China Division

China Division

Being a well-known printing group in Mainland China, we are focusing on producing high-quality magazines and hardcover books. In early 2005, we acquired new machineries to increase our production capacity to cope with the expansion in demands from the market. Even with the increased capacity, our sales orders almost utilised our full production capacity bringing in a turnover of approximately HK\$385 million for the year. With our continuous proactive marketing efforts and our prestige in the market, we expect that our PRC sales will grow next year.

Export Division

The turnover has increased by 39% over the year. This is primarily due to the continual efforts by our overseas sales team which has become fully functional in 2005. Further, we benefited from the integration with the SNP Excel (Hong Kong) Company Limited ("Excel (HK)") by having better opportunities in cross selling to existing customers.



Export Division

Packaging Division

With the acquisition of SNP Yau Yue, the Packaging Division made a turnaround in 2005, as compared to losses incurred in 2004 as a result of the incorporation of the eight-month results from SNP Yau Yue. This was mainly attributed to the effectiveness of the new management team in increasing the sales volume, obtaining bulk purchase discounts and implementing cost control measures.

Pop-up Division

Since the acquisition of Excel (HK) and SNP Excel (Thailand) Co., Ltd ("Excel (Thai)") in September 2004, the Pop-up Division started to have a full year contribution of HK\$547 million for year 2005 versus a partial inclusion of four-month results in the previous year. Other than benefiting from the synergistic opportunities in the areas of marketing and production, the profitability of the Group is expected to improve upon the diversification of its product offerings into pop-up books business.

Management Discussion & Analysis



Packaging Division

Capital Investments

During the year, we have invested approximately HK\$67 million in upgrading our existing facilities and increasing our production capacities. This indicates our determination in reinforcing our production capability and commitment to offer high-quality services. It is contemplated that further investments in advanced printing machines will be made in coming years in order to ensure our prompt responsiveness to the increasing demands from our valuable customers. The installation of the Group's first eight-colour sheetfed press in our Dongguan plant will be completed by the end of February 2006.

OUTLOOK

Following the acquisition of the new business lines in packaging printing, we continue to reinforce our prime focus on the development of the core printing business. Our joint venture with the Shanghai Expo Group is expected to commence operations in the third quarter of 2006, which represents a further stepping stone in the vast PRC market. With the full integration with



Pop-up Division

SNP Excel companies and SNP Yau Yue, we are optimistic that we will have an encouraging growth in 2006.

In addition to organic growth, the Group will continually explore value-enhancing merger and acquisition opportunities. We will also look at possibilities of vertical or horizontal integration within the SNP Group, so as to enlarge and strengthen our size, capacity and more importantly, our market share in the industry.

We continue to place priority on staff development. There will be continual talent recruitment and training for our staff. Technical and inter-company postings within the Group will be provided to enrich the professional knowledge of our dedicated employees.

Management Discussion & Analysis



Printing Facilities at SNP Leefung's Dongguan Plant

LIQUIDITY AND FINANCIAL RESOURCES

As at 31 December 2005, the Group's cash and bank balances amounted to HK\$154 million while the total assets and the net assets were approximately HK\$2,047 million and HK\$949 million respectively.

The current ratio at year end increased slightly from 1.81 to 1.92 and the total bank borrowings had increased to HK\$751 million. The net gearing ratio based on total borrowings less cash and bank balances to total equity has decreased from 68% to 64% as at year end as a result of the funds raised from the Rights Issue. In view of the Group's ability to generate cash from its operations, together with approximately HK\$846 million unutilised bank facilities at the balance sheet date, the Board considers that the Group has sufficient financial resources to finance future capital expenditure plans.

CAPITAL STRUCTURE

As at 31 December 2005, total equity was HK\$949 million, which had increased by HK\$202 million, as compared to HK\$747 million as at 31 December 2004.

As at 31 December 2005, the Group's total borrowings (including bank borrowings and obligation under finance leases) amounted to HK\$758.0 million (31 December 2004: HK\$661.5 million) which represents 80% (31 December 2004: 89%) of the total equity. Of the total borrowings, HK\$244.0 million, HK\$121.8 million, HK\$327.2 million and HK\$65 million will be repayable within one year, the second year, the third to fifth years and over five years respectively. The total borrowings comprise an amount of HK\$740.1 million denominated in Hong Kong Dollars; HK\$15.4 million denominated in Renminbi and HK\$2.5 million denominated in Thai Baht.

TREASURY POLICIES

The Group maintains a conservative approach on foreign exchange exposure management. The majority of the Group's borrowings, approximately 98% of the total borrowings at the year end date, were in Hong Kong Dollars while the remaining balance was in other currencies.

Management Discussion & Analysis



Assembly Workers at SNP Excel Thailand's Plant

The Group's borrowings are principally on a floating rate basis. When appropriate and at times of interest rate uncertainty or volatility, hedging instruments including swaps are used in managing the interest rate exposure.

PLEDGE OF ASSETS

As at 31 December 2005, the Group pledged its bank deposits and property, plant and equipment with an aggregate carrying value of approximately HK\$11.4 million (31 December 2004: HK\$10 million) as securities for generating banking facilities granted to the Group.

NUMBER OF EMPLOYEES AND REMUNERATION POLICY

At the end of 2005, the Group employed a total of approximately 200 employees in Hong Kong and a workforce of approximately 8,000 in the PRC and Thailand.

The Group's remuneration policies are primarily based on prevailing market salary levels and the performance of the respective companies and individuals concerned. In addition to salaries, the Group provides staff benefits including medical insurance, contribution to staff's provident fund, share options and discretionary training subsidies. Discretionary bonuses are also available to employees of the Group depending upon the financial performance of the Group.