Chairman's Statement and Management's Discussion and Analysis

Final Results

For the year ended 31st March, 2006, the Group recorded a consolidated turnover of HK$2,022 million (2005: HK$2,041 million). This 0.95% change resulted from strong competition in the market. The gross profit has increased 6.9%, from HK$196.47 million to HK$210.12 million. Due to significant increases in rental costs and in investments into new shops, both the distribution and administrative costs have increased. Thus, the profit attributable to shareholders of HK$65.27 million is 11.79% lower than the previous year (2005: HK$73.99 million). Basic earnings per share for the year was 23.71 Hong Kong cents per share (2005: 26.88 Hong Kong cents per share).

Business Review and Prospect

Overview

During the past year the Group continued with its intensive investing in new shops both in Hong Kong and PRC. These investments have put pressure on the short term performance of the Group. In addition, the recent spike in rental costs of shops in Hong Kong has further added to our expenses. Both instances were fully anticipated by the management. We have confidence that such investment will in the future generate positive results for the Group.

Hong Kong Market

The Hong Kong market remains the central to the business of the Group. During the year, we opened a flagship store in the central Causeway Bay. To date, this store is the largest amongst the group's ten stores in Hong Kong. It provides a spacious and luxurious shopping environment for our customers. This boutique-style shop has been a growing trend for the luxurious retailing market. This can be seen by the establishment of more and more flagship stores for world renowned fashion and accessories brands. In this new store, only a selected number of luxurious brand name watches are carried and each individual brand was invited to build its own concept area. With the establishment of this store, we are announcing our intention to expand our market share of the luxury watch customer base. To date, the performance of this Causeway Bay flagship store has been very satisfactory. In the future, we will continue to pursue opportunities to open up more flagship stores in the major shopping areas of Hong Kong. This may take place in the form of consolidating smaller scale shops into one large shop, or moving individual shops to better locations within Hong Kong. Instead of saturation, we aim for more exclusivity.

Although the effect of mainland Chinese shoppers has gradually subsided, they still remain a very significant share of the business in Hong Kong. Due to the PRC's import duties, the VAT (Value Added Tax), and the recently implemented Luxury Tax, there is still a favorable difference between watch retail prices in PRC and Hong Kong which continues to contribute to our retail sales. With our distribution network in the PRC, we will be able to provide after-sales services to watches tourists bring back to the mainland. This is a very important consideration for the mainland tourists in choosing a watch. Being able to provide such service to our customers will allow us to have an advantage over our competitors.

Chairman's Statement and Management's Discussion and Analysis

PRC Market

The China market is to us a precious treasure mine hidden deep underground. It will require a substantial investment in finances and time to successfully excavate. Any mistakes made during the excavation will cause extra time and money. If the mistake is not handled properly, it will eventually cause the whole investment to collapse. However, we are not the only company that is trying to open up the retail market in China and competition is very strong. Thus, the company will have to seize each opportunity cautiously. We aim to have a long-term presence in the PRC, which is why we expect our investment to be a long-term one. Our Group has been in the watch business for more than 40 years and we have a strong determination to continue for another 40-plus years. We are not in the business for only short term gains. We believe a good foundation is very important for any future success.

During the year, the Group established 11 new outlets throughout the PRC, increasing our point of sales to 21 shops. All the shops are 100% managed by the Group. The management strongly believes that this is the best way to have total control over our investment.

In addition, we have opened up more Rolex and Tudor stores throughout the PRC. The performances of these shops have been very encouraging. As both brands get more exposure in China, their results will be much more significant. A new Rolex store will be opened later this year in the capital city of Beijing. It will be located on the renowned ChangAn Avenue on the Ground level of the latest LG Twins Tower. With its prime location, this new store will be able to target and capture the high-end consumer market of Beijing. We will continue the policy of opening up more stores for Rolex and Tudor in the best available locations throughout China.

The introduction of a luxury goods tax will put short-term pressure on the sales of watches within China, but the effect is not expected to be permanent. Having outlets on both sides of the borders will further minimize the effect.

Human Resources

As at 31st March, 2006, our Group has approximately 180 employees in Hong Kong, and approximately 300 staff located at different provinces in Mainland China.

The Group's compensation package, which includes basic salary, commission, annual bonus, statutory MPF, medical insurance, and other common benefits, is structured by reference to marketplace and individual merits, and is reviewed on an annual basis based on the Group policy's performance system and objective specification performance appraisal.

We believe "people excellence" is one of the key factors to the success of a company. Several ongoing internal communication schemes were introduced during the year to communicate the Group's direction and strategies. In addition, several task force teams were established with the aim of promoting the "most valued Oriental Culture" through dynamic communications among all levels and the implementation of systematized new technology.

Furthermore, the Group continuously commits to its employees, with attractive remuneration packages, good working conditions and clear career path, supported by professional training programs and workshops to enhance and hone their skills, knowledge and attitudes.

System Control

During the period, the Group contracted with SAP, the world's most renowned (Enterprise Resource Planning) system provider, to license their software. The management believes that SAP's total solution concept and their expertise in the ERP system will not only help us to monitor our operations better but will also help us to integrate all data and processes to further develop and streamline our business work flow. We will first be implementing the system in our PRC market. Since our retail network in the China market is much more geographically dispersed, this system will help us to monitor the operation much more closely than before. In the near future, the Group's operations will be completely supported by the SAP system.

Prospects

The watch business is a very capital intensive business. The inventory turnover of new shops in China is longer than that of the Hong Kong shops, making returns on the investment slower. We are continuing the process of laying the foundations for a successful retail network in the PRC. We choose the few best partners available to be our suppliers and service providers to shorten the investment period.

With this in mind, our short-term results will understandably be put under some short term pressure. However, we anticipate that these investments into developing the China market and the overhaul of our operating systems will give us great returns in the future. We strongly believe that only a good foundation can guarantee future prospects. We are now laying the foundation for the China market.

We continue to commit to our dividend policy of providing a consistent return to our shareholders, as we hope that you will continue to commit to the Oriental Watch Group during all its ventures leading to a solid and successful future.

Financial Review

Liquidity and financial resources

Liquidity and financial resources position remain strong as the Group continues to adopt prudent approach in maintaining its financial resources. Based on the cash position and banking facilities, the Group has adequate working capital and liquidity to meet its operating and expansion needs. At the end of the financial year under review, the Group's net assets amounted to HK$765 million (2005: HK$715 million) with a net asset value per share HK$2.77 (2005: HK$2.60). The Group's net current assets increased by approximately 1.53% to HK$602 million (2005: HK$593 million). Total equity at 31st March, 2006 reached HK$765 million, up by 7.0% (2005: HK$715 million). The Group had cash on hand of HK$102.3 million (2005: HK$150.2 million) as at 31st March, 2006 whilst bank loans and overdrafts totalled HK$190.5 million (2005: HK$85.8 million).

Chairman's Statement and Management's Discussion and Analysis

As at 31st March, 2006, the Group's gearing ratio was 0.25 (2005: 0.12), and was calculated based on the Group's bank borrowing and total equity of HK$765 million (2005: HK$715 million). Management still considers that the financial position of the Group is healthy.

Foreign exchange exposure

The Group has minimal currency exposure as the majority of all sales were denominated in the functional currency of the relevant group entities. The management conducted periodical review of exposure and requirements of various currencies, and will consider hedging significant foreign currency exposures should the need arises.

Charge on group assets

At 31st March, 2006, the Group has pledged certain investment properties which have an aggregate carrying value of HK$24.86 million (2005: 25.26 million) to secure the bank loans granted to the Group.

At 31st March, 2005, the Group pledged a fixed deposit of HK$3.15 million which carries interest at 0.72% to the bank in respect of the credit facilities granted by this bank to the Company.

Appreciation

On behalf of the Board, I would like to take this opportunity to express gratitude to our shareholders, customers, suppliers and colleagues for their support and contributions to the Group in the past fiscal year. I look forward to continuing and improving their valuable relationships with the Group for many more periods ahead.

By order of the Board
Yeung Ming Biu
Chairman

Hong Kong, 19th July, 2006