Mr. Wang Xingdong

BUSINESS OVERVIEW

During the year under review, although the consolidated turnover for ONFEM Holdings Limited ("**Company**") and its subsidiaries ("**Group**") declined from approximately HK$332.2 million in 2002 to approximately HK$160.9 million in 2003, the Group recorded a decline of approximately HK$47.1 million or 36% in the total administrative and finance costs, and a net loss of approximately HK$35.7 million, a decrease of 74% as compared with the previous year, with the Group's implementation of stringent cost controls at all levels, the strengthening of its operations and quality management and an aggressive reduction of its administrative expenses.

Currently, the Group is principally engaged in three types of businesses: manufacturing and trading, specialised construction contracting, and property development and leasing.

1. Manufacturing and Trading

The Group is mainly engaged in the manufacturing and trading of two types of industrial products: industrial lubricant products and doors and timber products. During the year under review, the total external turnover for this segment amounted to approximately HK$57.8 million, a decrease of 8% as compared with the previous year, and contributing 36% to the consolidated turnover. However, as the Group imposed stringent and effective cost reduction measures during the year, its operating efficiencies improved and the segment loss from manufacturing and trading decreased from approximately HK$7.1 million in 2002 to approximately HK$3.7 million in 2003.

i) Industrial Lubricant Products

Jaeger Oil & Chemical Holdings Limited (a subsidiary of the Group) and its subsidiaries ("**Jaeger**") are engaged in the manufacturing and distribution of industrial lubricants. Among its sales in 2003, 17% came from Hong Kong and South East Asia while 83% came from China.

The surge of oil price because of the war in Iraq, coupled with the effect of a weaker US dollar, have reduced the competitiveness of Jaeger's imported agency products and increased cost of sales. The outbreak of Severe Acute Respiratory Syndrome ("**SARS**") early in the year had also adversely affected Jaeger's sales for a short period. These factors led to a slight decrease of 3% in its annual turnover of 2003 as compared with 2002.

From right to left: Mr. Lin Xizhong, Mr. Wang Xingdong, Ms. He Xiaoli, Mr. Yan Xichuan and Mr. Qian Wenchao

During the year, Jaeger aggressively developed its domestic sales market in the Yangtze Delta by strengthening its distribution network in Eastern and Central China. With continuous efforts, Jaeger achieved satisfactory sales in these districts with 58% increase in turnover as compared with the previous year. Jaeger will strategically expand its major end-user markets and establish comprehensive distribution networks in Southern China. At the same time, it will focus on the mid to high-end products to improve the overall gross profit margin. In addition, as turnover generated from the sales of the United Kingdom brand "Korniche" increased 24% as compared with the previous year, Jaeger will put additional effort to increase the market share of this brand and better realise its sales potential. At the same time, after securing the distribution rights for the brand "Rite-Lok" from the United Kingdom, Jaeger will further broaden the sales of "Rite-Lok" by building up comprehensive sales channels progressively.

The Group is very pleased to report that Jaeger's manufacturing facility in China were awarded SGS ISO9001 international quality management system certification in 2003. This will greatly strengthen Jaeger's competitiveness in the markets for high-end metalworking and die-casting lubricant products.

Jaeger will aggressively develop markets in Eastern and Northwestern China in the near future. It planned to establish comprehensive sales networks in Nanjing and Suzhou, and will continue to strengthen its distribution network in new areas such as Yangzhou, Yancheng, Wenzhou and Jiashan. Besides, Jaeger will also participate in a number of exhibitions in Central China and to identify quality distributors and major users to broaden its customer base. Jaeger will continue to develop industrial users and consumer goods markets in Southern China by setting up distribution points in Shunde, Wuyi and Huizhou.

In order to strengthen cooperation with distributors, Jaeger will organise product seminars and business conferences for its distributors in China in order to enhance their product knowledge and business operations.

Following China's accession to the World Trade Organisation, a large number of foreign companies have since established their manufacturing facilities in China. As a result, this will accelerate the increase in demand for high-end industrial lubricants. Furthermore, in view of the gradual decline in import tax, the cost of imported products is expected to fall accordingly. Jaeger will explore the potential of setting up venture with foreign suppliers to establish manufacturing facility for adhesives and die-casting lubricant products in China to fully leverage the opportunities offered by these favourable conditions. Specifically, it aims to lower the production cost, expand the scope of its business and enhance overall profitability.

ii) *Doors and Timber Products*

Enful Holdings Limited (a subsidiary of the Group) and its subsidiaries ("**Enful**") are principally engaged in the business of doors and timber products. It recorded segment external turnover of approximately HK$6.8 million in 2003, representing a decrease of 27% as compared with the previous year. The majority of the turnover from external sales came from China. The losses for the year under review were primarily due to the provisions for accounts receivable and inventories, which amounted to approximately HK$1.3 million and HK$1.9 million respectively.

In the first half of the year, the outbreak of SARS had a material adverse impact on the doors market and consequently, business for this segment was also adversely affected. Despite the intense competition in the marketplace, Enful managed to secure a contract for a "timber and fire proof door" supply and installation project for each of Zhongshan Zhangzhou Green View Bay (中山長州翠景灣) and New Century Home (新世紀華庭) during the year under review.

Over the past year, the management focused its resources on developing potential sales points in major construction materials supermarkets and at the same time rationalising under-performing sales points so as to better capture opportunities arising from the market recovery. In the coming year, Enful will continue to impose stringent cost control measures and enhance quality management for its production processes in order to increase profit margin from its operation. At the same time, Enful will streamline its operational structure for the purpose of avoiding duplication of duties. This is in conjunction with the implementation of the accountability system of management by objectives so that the remunerations of staff are linked to Enful's performance. As such, staff will be better motivated and their interests will be better aligned with Enful's profitability. Notwithstanding these measures, further effort is required on the part of Enful in order to alleviate itself from the difficult trading situation faced by it, which will also depend on the outcome of the restructuring of its operating structure.

2. Specialised Construction Contracting

In 2003, the Group achieved a turnover in specialised construction contracting business of approximately HK$86.1 million, representing a decline of 66% as compared with the previous year. The contribution from this business to the Group's consolidated turnover decreased from 75% in the previous year to 53% in the year under review. The segment loss from this business also decreased significantly from approximately HK$91.8 million in 2002 to approximately HK$38.2 million in 2003.

i) *Enful*

The specialised construction contracting business of Enful is principally carried out in Hong Kong. Enful completed a number of construction and environmental protection contracts in 2003. It recorded a segment turnover of approximately HK$6.0 million, representing a decrease from the previous year. However, it achieved an increase in its gross profit margin due to the implementation of its effective cost control measures during the year. The loss for the year under review was mainly attributable to the provision for accounts receivable of approximately HK$3.0 million.

During the year, the projects completed by Enful included the environmental and acoustic projects for the West Rail Tin Shui Wai Station and a renovation project for Bird Garden in Yuen Po Street. In view of the recovery of Hong Kong economy in the second half of the year, several infrastructure projects such as the project at the East Rail Ma On Shan Station also commenced. Building on its extensive experience in infrastructure projects, it is believed that Enful will be able to successfully secure several projects of larger scale in the coming years so as to enhance its profitability.

ii) *Polycrown Engineering (Holdings) Limited and its subsidiaries ("**Polycrown**")*

In 2003, the turnover for Polycrown amounted to approximately HK$68.1 million, of which 96% came from Hong Kong and 4% came from China. During the year, Polycrown also reduced its administrative expenses and operating costs aggressively. At the same time, it also speed up the collection of its accounts receivable. These austerity measures successfully led to a substantial decline in its operating loss.

During the year, Polycrown completed the project at the West Rail Mei Foo Station on schedule. Currently, it is focusing on the project at the Kwai Chung Container Port-Terminal No. 9, which is expected to be completed by mid-2005. Other electrical and mechanical engineering projects of smaller scale are also scheduled to be completed in 2004. Nevertheless, Polycrown has yet to exit from its difficult operating and management situation.

iii) *Condo Group Limited and its subsidiaries ("**Condo**")*

As two subsidiaries under Condo were unable to repay their debts, the Group made numerous attempts to implement the proposed voluntary debt restructuring of each of these two companies during the period. However, such restructuring proposals were unsuccessful due to the failure in reaching any agreement with the Condo's minority shareholders.

Following the failure of the aforesaid voluntary debt restructurings, winding-up orders against these two companies were made by the High Court of Hong Kong on 8 September 2003. As a result, these two companies are currently put under receivership. The Group will now focus on recovering the debts owed to the Group by these two companies.

3. Property Development and Leasing

The Group's core property businesses include the Zhuhai Haitian Garden project in China and the ONFEM Tower in Hong Kong for leasing purpose.

In 2003, the Group's property leasing business achieved a turnover of approximately HK$10.8 million, representing an increase of 3% as compared with the previous year; the segment loss in the property leasing business therefore fell from approximately HK$19.4 million in 2002 to HK$4.7 million in 2003. As the property market rebounded at the end of the year, loss on revaluation of investment properties decreased by 70% as compared with the previous year to approximately HK$8.3 million.

Since the several remaining units of the Garret, the residential development project in Sydney, Australia, were sold in 2002 while the Zhuhai Haitian Garden project was still under construction and no income was generated from this project either, no turnover was recorded as regard to property development business for the year under review.

i) *ONFEM Tower, 29 Wyndham Street, Central, Hong Kong*

The adverse impact of the outbreak of SARS on the economy was reflected in the results of the first three quarters of 2003. Nevertheless, as at 31 December 2003, ONFEM Tower recorded an occupancy rate of 91% with an increased rental revenue as compared with the previous year. In addition, the Group is very satisfied with the quality of its tenants, which included a number of multinational enterprises. Since the Group appointed a renowned property management company to provide professional property management services for the ONFEM Tower in early 2003, the quality of this building was significantly enhanced and in turn an increasing recognition was gained from its tenants. In 2004, the Group will focus on further enhancing the building's quality with a view to providing its tenants with excellent services.

ii) *Haitian Garden, Zhuhai, China*

In January 2004, the Group successfully acquired the remaining 20% equity interest in Zhuhai (Oriental) Blue Horrison Properties Company Limited from Zhuhai Shining Metals Group Inc. and the Group now holds a 100% equity interests in Haitian Garden. The substructure works of the project have been completed. The superstructure works are scheduled to commence in the second half of 2004 and are expected to be substantially completed by the end of 2005.

In view of the current demand in property market in Zhuhai, the Group has repositioned the project as "The New Generation of Panoramic Seaview Deluxe Apartments in Zhuhai".

The proposed construction of the Hong Kong-Zhuhai-Macau Bridge is expected to be finalised shortly, the completion of which will facilitate transportation between Zhuhai, Hong Kong, Macau and the Western part of China. Taking into account the unique advantages in Zhuhai's natural environment and resources, together with the promotion by the Zhuhai municipal government, an increasing demand for properties in Zhuhai from Hong Kong and Macau residents is expected. Sales price of recently launched luxurious properties in Zhuhai increased over 10% in the past six months. Currently, Haitian Garden is one of the few deluxe panoramic seaview developments under construction in Zhuhai. In view of such favourable market conditions, the offer for sale of Haitian Garden units is expected to be well received by the market.

OUTLOOK

Looking forward, the Group will focus on property development as its principal business which is to be supplemented by the specialised construction contracting business and with high technology investment as an ancillary business. The Group will use Hong Kong as its base to vigorously develop its core businesses into China with a view to providing customers with quality services and products and at the same time enhancing its competitiveness so that it will return to profitability and achieve a better return for the shareholders.

In addition, the Group plans to expand through appropriate value driven means such as direct investments, mergers and acquisitions in order to build a portfolio of quality assets and to establish a superior brand.

LIQUIDITY AND FINANCIAL RESOURCES

As at 31 December 2003, the gearing ratio of the Group, representing a ratio of total borrowings to total assets, reduced to 9.2% (2002: 14.3%). Cash and bank deposits, as at 31 December 2003, amounted to approximately HK$199.3 million (2002: HK$210.6 million).

The Group obtained its source of fund through various means in order to maintain a balance between cost and risk. Apart from the fund generated from normal operations and the cash and bank deposits, the Group also obtained financial resources from bank borrowings, finance lease obligations and loan from a minority investor which amounted to approximately HK$66.7 million (2002: HK$130.9 million), HK$0.1 million (2002: HK$0.2 million) and HK$4.5 million (2002: HK$3.3 million) respectively as at 31 December 2003.

The bank borrowings denominated in Renminbi ("**RMB**"), as at 31 December 2003, were approximately RMB28.6 million (2002: RMB38.6 million) while the remaining balances were denominated in Hong Kong dollars. Except this RMB bank loan with fixed interest rate, all the Group's bank borrowings are on a floating rate basis.

Capital commitments of the Group are to be partly financed by bank borrowings.

FINANCIAL RISKS AND MANAGEMENT

The Group's strategies towards financial risk management include diversification of funding sources and extension of credit periods. For the year ended 31 December 2003, finance costs reduced to approximately HK$4.9 million (2002: HK$7.7 million).

The total borrowings of the Group as at 31 December 2003 amounted to approximately HK$71.3 million (2002: HK$134.4 million). The borrowings were repayable as follows:

	2003 **HK$'000**	2002 HK$'000
Within one year	**71,304**	134,364
In the second year	**–**	58
	71,304	134,422

EXPOSURE TO THE FLUCTUATION IN EXCHANGE RATES

Most of the transactions of the Group were denominated in Hong Kong dollars, RMB and US dollars. Given that the exchange rates of Hong Kong dollar against RMB and US dollar are stable, no hedging or other alternative measures have been implemented by the Group. As at 31 December 2003, the Group had no significant exposure under foreign exchange contracts, interest or currency swaps or other financial derivatives.

CHARGES ON GROUP ASSETS

As at 31 December 2003, the Group pledged an investment property with carrying amount of approximately HK$195.0 million (2002: HK$206.4 million) as collateral for the Group's banking facilities. Besides, fixed deposits amounted to approximately HK$53.2 million (2002: HK$101.6 million) have been pledged by the Group as securities for general banking facilities and issuance of performance bonds. Certain inventories of the Group were also held under trust receipt loan arrangements.

CONTINGENT LIABILITIES

Details of the contingent liabilities of the Company and the Group are set out in Note 32 to the accounts.

EMPLOYEES

As at 31 December 2003, the Group employed 309 staff (2002: 482 staff). The total remunerations and benefits of the Directors of the Company and staff of the Group during the year were approximately HK$43.1 million (2002: HK$64.0 million). The Group adopts a remuneration policy in line with market practice.

By Order of the Board
Wang Xingdong
Managing Director

Hong Kong, 19 April 2004