# Chairman's Statement

I am pleased to present my review of the results and operations of the Herald Group (the "Group") for the year ended 31 March 2004.

## RESULTS

For the financial year under review, the Group achieved very favorable results. Both the turnover and profitability for the year ended 31 March 2004 were the best in the past ten financial years. Despite the negative impact from the SARS epidemic and the war in Iraq, the Group's turnover for the year increased by HK$178 million or 19% to HK$1,104 million, from last year's turnover of HK$926 million. Net profit attributable to shareholders was HK$61.9 million, an increase of 76% from HK$35.2 million (as restated) in the prior year. The earnings per share for the year was HK10.07 cents as compared to last year's HK5.66 cents (as restated).

## REVIEW OF OPERATIONS

### *Timepiece Division*

Compared to last year, the Timepiece Division recorded a very substantial improvement in the year ended 31 March 2004. The Division's turnover for the year was HK$284 million, an increase of HK$128 million or 82% from HK$156 million of last year. The Division made a net profit of HK$22 million compared to a loss of HK$2 million a year earlier. After the closure of the Division's operations in France and Germany, the management has focused more on its business in the UK which has had very strong growth since then. The Division has successfully developed a business model based on recognized brands in the UK and other markets. The Division markets and distributes a wide range of timepieces including products with licensed brands such as Elle, Fila, Head, Playboy and Ted Baker. In addition, the Division also distributes in-house brands such as Zeon, Ingersoll and Eligio.

### *Computer Head Division*

After suffering a significant loss in the last financial year, we are pleased to see that the Computer Head Division has returned to profitability. The overall turnover of the Division had an increase of 19% over the turnover in the previous year. This was due to the strong demand of thin-film tape heads which largely offset the negative impact due to the stagnancy of the business of ferrite tape heads. Furthermore, as a result of the continuous efforts in streamlining the operation, the Division now benefits from much lower operating costs. The Division had a net profit of HK$12 million which included a write-back of HK$3 million in respect of stock provision.

### *Houseware Division*

For the year under review, the business of the Houseware Division was stable. The overall sales of the Division for the year increased by 7%, as compared to the sales a year ago. The stainless steel and carbon steel cookware business, which accounted for 33% of the Division's total turnover, continued to grow by 36% while the aluminum cookware business had a mild decrease of 3%. The Division was negatively affected by continuous increases in the price of aluminum and stainless steel.

***Toy and Gift Division***

In general, the toy industry had a very tough year in 2003. Competition among the toy manufacturers led to reduced gross margin for the industry. Though the Division had a modest growth of 3% in its turnover, the net profit of the Division dropped from HK$35 million to HK$10 million. In addition, the negative impact of SARS and the increase of plastic materials prices were also important factors that further hurt the Division's profitability.

## FINANCIAL POSITION

The Group has maintained its sound financial position. At the end of the financial year, the Group had a strong balance sheet with a healthy liquidity position. As at 31 March 2004, the Group had total assets of HK$648 million (2003 as restated: HK$573 million) which were financed by current liabilities of HK$121 million (2003: HK$94 million), non-current liabilities of HK$6 million (2003 as restated: HK$6 million), minority interests of HK$28 million (2003 as restated: HK$26 million) and shareholders' equity of HK$493 million (2003 as restated: HK$447 million).

At 31 March 2004, the Group's cash balances aggregated to HK$172 million representing an increase of HK$12 million over the balance of HK$160 million in last year's balance sheet. The Group's current assets position as at 31 March 2004 was HK$454 million compared to HK$373 million as at 31 March 2003. The inventories increased to HK$143 million from HK$118 million and the trade and other receivables increased to HK$139 million from HK$95 million. The increases were largely due to increase of sales activity of the Timepiece Division.

The Group's current liabilities increased from HK$94 million to HK$121 million primarily due to increase in trade and other payables that is attributed to the same factor affecting the level of current assets above-mentioned.

At 31 March 2004, the Group had no bank borrowings (2003: HK$1 million). None of the Group's assets are charged to secure the Group's banking facilities. Furthermore, the Group has no long-term borrowings. As at 31 March 2004, the working capital ratio, an indicator of a company's liquidity represented by a ratio between the current assets over the current liabilities, was 3.75 compared to 3.96 last year. The quick ratio, another ratio that gauges the short-term liquidity of a company measured by trade debtors and cash and cash equivalents over the current liabilities, slightly decreased to 2.23 from 2.45.

## CONTINGENT LIABILITIES

As at 31 March 2004 the Group did not have any significant contingent liabilities.

## FOREIGN EXCHANGE EXPOSURE

During the year under review, approximately 38% of the Group's turnover was denominated in sterling. From time to time, the Group enters forward foreign exchange contracts to hedge its foreign exchange exposure.

## PROSPECTS AND GENERAL OUTLOOK

The Group entered the new financial year with a strong order position. The sales in the first quarter of the new fiscal year were higher than the sales in the same quarter a year earlier. However, the management believes that 2004 will be a very challenging year. Due to geopolitical uncertainties, oil prices continue to be at very high levels leading to substantial increases for raw materials prices. Furthermore, the volatility of the foreign exchange markets adds additional uncertainties to our business as a large portion of the Group's sales in the UK market are denominated in sterling. Our gross profit margins may be affected if the sterling depreciates against the U.S. dollar. We are concerned by the rapid rise in the cost of electricity in China as well as the ongoing supply shortage. We are also concerned by increasing wages due to a shortage of labour in Southern China. Moreover, there is an increasing pressure from the U.S. that the renminbi be revalued. As the Group's manufacturing facilities are all in the PRC, such revaluation may significantly increase our production cost structures.

## DIVIDENDS

At the forthcoming Annual General Meeting to be held on 17 September 2004, the Directors will recommend a final dividend of HK3 cents per share (2003: HK2 cents). Together with the interim dividend of HK1.5 cents (2003: HK1 cent), the dividend for the year of HK4.5 cents (2003: HK3 cents) would represent an annual return of 10% on the Company's average share price of HK45 cents in the year ended 31 March 2004.

The total final dividend will amount to HK$18,418,000 and is calculated based on the total number of shares in issue as at 14 July 2004 being the latest practicable date prior to the announcement of the results. Dividend will be payable on 30 September 2004 to shareholders registered in the Register of Members on 17 September 2004.

## APPRECIATION

On behalf of the Board of Directors and shareholders, I should like to extend my sincere thanks to all the Group's employees for their efforts and hard work. Their commitment to the Group, along with the support of customers and suppliers, has been crucial to the success of Group.

**George Bloch**
*Chairman*

Hong Kong, 15 July 2004