Management Discussion and Analysis

Business Review and Financial Performance

The Group is principally engaged in the manufacturing of polishing compounds and polishing wheels in Mainland China under its own brand name ***Pme*** and the trading of various branded industrial abrasive products. Over 90% of the Group's turnover and profits was contributed from the markets in Hong Kong and the Pearl River Delta in Mainland China.

The Group's turnover for the year 2005 has increased by 17.3% from approximately HK$163.6 million in 2004 to approximately HK$192.0 million. The net profit for the year under review decreased from approximately HK$21.2 million in 2004 to approximately HK$5.1 million.

The increase in turnover is mainly due to increase in sales of trading products and increase in sales to Mainland China market. However, the continued increase in raw materials costs, manufacturing overheads and the costs of trading products, which have not been able to fully transfer to our customers due to keen competition in market, reduced the Group's profit margin. The increase in marketing expenses to promote the Group's products to Mainland China market and bad debt provisions made during the year also resulted in a decrease in net profit.

Liquidity and Financial Resources

At 31 December 2005, the Group had interest-bearing bank borrowings of approximately HK$12.2 million (31 December 2004: HK$12.3 million), which were of maturity within one year. The Directors expect that all the bank borrowings will be repaid by internal generated funds or rolled over upon the maturity and continue to provide funding to the Group's operations. At 31 December 2005, the Group's leasehold land and buildings and prepaid lease payments with aggregate carrying value of approximately HK$94.3 million (31 December 2004: HK$94.6 million) have been pledged to banks to secure the banking facilities granted to the Group.

At 31 December 2005, current assets of the Group amounted to approximately HK$129.2 million (31 December 2004: HK$127.0 million). The Group's current ratio was approximately 5.46 as at 31 December 2005 as compared with 5.84 as at 31 December 2004. At 31 December 2005, the Group had total assets of approximately HK$264.0 million (31 December 2004: HK$258.2 million) and total liabilities of approximately HK$28.0 million (31 December 2004: HK$25.5 million), representing a gearing ratio (measured as total liabilities to total assets) of 10.6% as at 31 December 2005 as compared with 9.9% as at 31 December 2004.

Foreign Exchange Exposures

The Group's purchases and sales are mainly denominated in US dollars, Hong Kong dollars and Renminbi. The operating expenses of the Group are either in Hong Kong dollars or Renminbi. As Hong Kong dollars have been pledged with US dollars, and the exchange rate of Renminbi against Hong Kong dollars is relatively stable, the directors consider that the Group has no material currency exchange risk exposures.

Contingent Liabilities

The Group had no material contingent liabilities as at 31 December 2005 and 31 December 2004.

Capital Commitments

At 31 December 2005, the Group had capital commitment of HK$29,000 (2004: HK$96,000) in respect of acquisition of property, plant and equipment contracted for but not provided in financial statements.

Employees and Remuneration

At 31 December 2005, the Group had approximately 260 employees in Hong Kong and Mainland China. The employees are remunerated with basic salary, bonus and other benefits in kind with reference to industry practice and their individual performance. The Group also operates a share option scheme of which the Directors may, at its discretion, grant options to employees of the Group. No option has been granted since the adoption of the share option scheme.