Management Discussion and Analysis

RESULTS

Turnover of Fortuna International Holdings Limited (the "Company") and its subsidiaries (collectively the "Group") for the year ended 31 December 2006 was approximately HK$51.2 million (2005: HK$26.5 million) and net profit attributable to the shareholders was approximately HK$73.6 million (2005: net loss of HK$150.5 million). The results for the year is satisfactory, with turnover increased by almost 93% as compared with that of the last financial year, and the gross profit for the year was approximately HK$19.6 million (2005: HK$10.5 million), which is an increase of 86% as compared with that of the last financial year. The increase in turnover and gross profit was mainly attributable to the steady income stream from the Japanese restaurant operation (which was acquired by the Group in April 2005) and glass eel trading (which was set up by the Group in October 2005). The profit for the year was mainly due to the Group's realisation of its investment property at an attractive price. The disposal of the Right Emperor Commercial Building by the Group was completed on 28 December 2006, and the disposal had brought about a gain of approximately HK$40 million to the Group.

BUSINESS REVIEW

The refining of the Group's structure and business had always been the major consideration of the directors of the Company (the "Directors" or the "Board") for all these years. The business of the Group continued to undergo restructuring during the year. The Group had successfully trim down unsatisfactory operations, such as the trading of jewellery, artwork design and general trading. Resources were effectively utilized for the development of the Japanese restaurant operation and the glass eel trading. Despite the closing down of some of its operations (i.e. the trading of jewellery, artwork design and general trading), the Group was still able to maintain a steady income stream.

Restaurant operation

The Group has been engaging in the restaurant operation for almost 2 years. With the expertise of the staff and a good management team, the Group was able to maintain a steady income from this operation. It was acquired by the Group in April 2005 when the Directors at that time were confident that the Group's profit would be able to ride on the improving economic condition in Hong Kong. The results of the restaurant operation was proven to be satisfactory after one year from acquisition, and therefore the Group acquired a further 5% interests in the restaurant business in May 2006. The Group is now interested in 80% of the restaurant operation. In mid December 2006, the Group expanded its restaurant business by opening new outlet in Hong Kong. This segment contributes approximately HK$16.7 million revenue for the year and with a profit of HK$571,000 (2005: revenue HK$10.2 million, profit HK$478,000). Both revenue and profit of restaurant operation remained stable.

Glass eel trading business

The glass eel trading business provides a steady income base for the Group. The turnover and the profit from this segment were approximately HK$26.8 million and HK$205,000 for the year respectively (2005: for the 2 months period from setting up of the business in October 2005 to 31 December 2005, the turnover was HK$8.4 million and profit was HK$400,000). The glass eel trading business is subject to seasonal fluctuations. The peak and active months of trading are usually starting from October to April of next year in line with breeding months of glass eel. The Group so far has adopted conservative strategy in the glass eel trading business, instead of putting massive efforts in expansion or brand building.

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Property investment

On 18 September 2006, the Company announced that Harbour Wealth Investment Company Limited, its wholly owned subsidiary, had entered into a provisional agreement with an independent third party to dispose of Right Emperor Commercial Building at a consideration of HK$159.8 million. The disposal of the Property was completed on 28 December 2006. Details of the disposal were stated in a circular of the Company dated 25 October 2006. The disposal was a responsive decision of the Directors to the robust economic condition of Hong Kong during the fourth quarter of 2006. The return on the investment was satisfactory and a gain of approximately HK$40 million was recorded from disposal. Other than the Right Emperor Commercial Building, the Group has 2 residential and 1 industrial premises for long term investment and for rental purpose. The disposal of Right Emperor Commercial Building and the rental from the other properties of the Group contributed a profit of approximately HK$43 million for the year (2005: HK$2.2 million). Despite that the gain from the disposal of the Right Emperor Commercial Building is a non-recurring income, the Directors consider that with the cash obtained from the disposal, the Group is able to invest into new business or property.

Skin and health care business

The skin and health care business had been operating at loss for years. Therefore, the Group discontinued its skin and health care business at the end of May 2006. No turnover or profit has been recorded since the beginning of the year. The gain on disposal of this operation is approximately HK$11 million.

Trading of jewellery and other products and provision of artwork design services

No turnover has been recorded for the year from the trading of jewellery (2005: HK$3.7 million), the trading of other products (2005: HK$28,000) and the provision of artwork design (2005: HK$1.1 million). Most of these operations have been operating at loss for years and the Directors do not envisage any prospect in these businesses. Instead of allocating resources to revive the business, the Board resolved to trim down these businesses since last year. The Directors believe that it would be beneficial to the Group and the shareholders of the Company to dispose of these debt-laden and loss-making businesses. As such, the Directors decided to dispose of these operations and had been seeking for purchaser since mid December 2006. During the preparation of the annual audit of the Group for the year ended 31 December 2006, the management of the jewellery and other products trading segment refused to provide accounting records and documents for audit. Despite repeated demands for the accounts, there were still no sign of cooperation from the management of the subsidiaries. During the year, the Directors had reviewed the measures in controlling the management of the subsidiaries from time to time, however, such attempts to reinforce control over them were not successful. The financial statements of the Group for the year was prepared on the basis that the results of the trading of jewellery and other products segments were excluded from the consolidated financial statements of the Group with effect from 1 January 2006.

Trading of wine

The trading of wine segment was able to generate approximately HK$3.8 million of turnover for the year (2005: HK$2.3 million). Although the turnover increased by 65% this year, the business was still operating at loss. As such, the Directors considered that it did not worth the resources and effort to maintain the trading of wine segment in the long run.

PROSPECTS

To restructure the Group's business by disposing those poorly performed business and uncooperative subsidiaries has always been the Group's strategy and the Directors' major concern. Active steps have been taken by the Directors since 2004.

On 2 March 2007, the Group has entered into a conditional sale and purchase agreement to dispose the non-core business, including the trading of jewellery, trading of steel, trading of other products, trading of wine and the provision of artwork design to a director of its subsidiaries. The disposal was completed on 16 April 2007 and it was a strategic move of the Group to dispose all of its loss-making operations. The Directors believe that, after the disposal, the Group will be able to turn itself from a loss-making Group to a healthy one with stable income and profit.

With the improvement in the cash and gearing position as a result of the disposal of the Right Emperor Commercial Building and those loss-making companies, the Group can now concentrate on its remaining business, including the restaurant operation and the trading of glass eels. The Company can also concentrate on its resources in expanding the Group's business by acquiring or setting up new restaurants, or invest into new businesses. The Directors are open to all investment opportunities that are beneficial to the Group. The Directors will also use their best effort to improve the internal control over the Group's subsidiaries.

FINANCIAL INFORMATION

The Group financed its operations by cash generated from operations, proceeds from open offer of Company's shares and banking facilities granted by its principal bankers to its subsidiaries.

As at 31 December 2006, the Group's gearing ratio was 0.005 (2005: 0.51) (calculated on the basis of total bank and other borrowings over shareholders' fund).

The Group's total bank and other borrowings amounted to approximately HK$701,000 (2005: HK$18 million) as at 31 December 2006. As at 31 December 2006, the Group had no secured bank loans and overdrafts. At 31 December 2005, the Group's secured bank loan and overdrafts are mainly secured by investment properties, long term investment, and guarantees granted by directors of certain subsidiaries.

The Group's core operation was in Hong Kong and had limited exposure to the fluctuations in exchange rates, bank balances and borrowings were mainly denominated in Hong Kong dollars.

EMPLOYEES AND REMUNERATION POLICY

As at 31 December 2006, the Group has 86 employees (2005: 79). Total staff costs were approximately HK$9.7 million (2005: HK$12.6 million). Employee remuneration was determined in accordance with individual's responsibility, performance and experience. Staff benefits include contributions to Mandatory Provident Fund Scheme, share option scheme, medical allowances and other fringe benefits.

CONTINGENT LIABILITY

The Group did not have any significant contingent liability at the balance sheet date.

CAPITAL STRUCTURE

(a) By a special resolution passed by the shareholders of the Company on 20 March 2006, the share capital of the Company reorganised as follows with effect from 20 March 2006:

(i) cancelled paid up capital to the extent of HK$0.0099 on each ordinary share of the Company so that the nominal value of each issued share was reduced from HK$0.01 to HK$0.0001 ("Capital Reduction");

(ii) subdivided each of the authorised but unissued share of HK$0.01 into 100 ordinary shares of nominal value of HK$0.0001 each;

(iii) subdivided each of the authorised but unissued convertible preference share of the Company of HK$1,000,000 each into 100 convertible preference shares of nominal value of HK$10,000 each;

(iv) cancelled the entire amount standing to the credit of the share premium account of the Company as at 20 March 2006 ("Share Premium Reduction"); and

(v) transferred the credit arising from the Share Premium Reduction and the Capital Reduction totalling HK$698,781,000 to the contributed surplus account of the Company and applied the amount therein to set off against the Company's accumulated losses of HK$688,054,000 in accordance with the applicable laws, including the laws of Bermuda and the bye-laws of the Company.

(b) By an ordinary resolution passed by the shareholders of the Company on 20 March 2006, every 10 of the ordinary shares of the Company (both issued and unissued) of HK$0.0001 each were consolidated into one new share of HK$0.001 each and every 10 of the convertible preference shares of the Company of HK$10,000 each were consolidated into one new convertible preference share of HK$100,000 each.

(c) On 25 April 2006, 2,720,363,644 ordinary shares ("Offer Shares") of HK$0.001 were issued at HK$0.01 per share through an open offer ("Open Offer") to the shareholders of the Company. The Offer Shares rank pari passu in all respects with the then existing shares of the Company. The premium arose from the issue of the Offer Shares of approximately HK$24,483,000, net of share issuing expenses of approximately HK$1,212,000 was credited to the share premium account. The Company used the net proceeds from the Open Offer of approximately HK$992,000 for the Group's general working capital and approximately HK$25,000,000 used for settling part of the consideration payable of the acquisition of State Empire Limited by the Group.

(d) By an ordinary resolution passed by the shareholders of the Company on 14 November 2006, every 20 of the ordinary shares of the Company (both issued and unissued) of HK$0.001 each were consolidated into one new share of HK$0.02 each.

CHARGE OF ASSETS

None of the Group's investment properties were pledged as security for banking facilities of the Group (2005: HK$22 million).