

Management Discussion and Analysis of the Operations

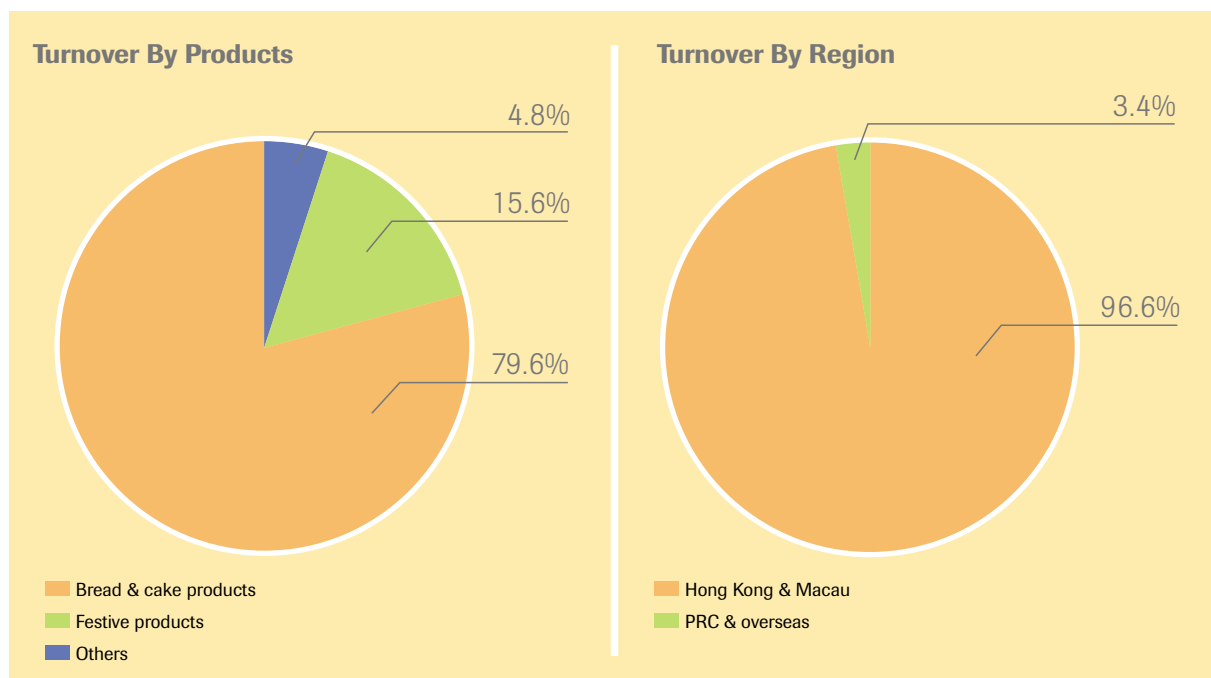
SAINT HONORE CAKE SHOP

We are enjoying the full year effect of the migration of certain production lines to Shenzhen which have lowered our production costs yet without foregoing our product quality. Our production capacity has been considerably expanded to support on-going large scale promotion campaigns which were interrupted by SARS during when we had to postpone our schedule, while effort was diverted to implement various hygienic measures to maintain public confidence on open shelved food products. We deliberately packed all cake and bread products individually as well as tightened up the hygiene standard at our production plants.

When we resumed our marketing campaigns, we invited a few well-known brands to be our joint promotion partners in order to create a higher noise level for our campaigns as well as opening up cross-selling opportunity to each other. The results were encouraging with sales growth enjoyed by both parties while there were savings in the promotion expenses. Our annual turnover in cake and bread products increased by 11%.

During the year, we replaced four loss-making outlets and relocated them to other residential areas. We have also renovated eight outlets to improve our image.

We continue to introduce new product lines of improved quality. After the launch of our 'Natural Yeast' bread products, we had brought in from Japan the 'Soup-based' technique and marketed it under a new bread product line which was well received by our customers. Our bread turnover increased by 13%. We also regularly push out new cake and bread items for our conventional lines to sustain their product lives. In deed "St Honore" is now recognized as one of the 'Hong Kong Superbrands' well accepted among the local consumers.





Our Managing Director, Mrs. Carrina Chan, receiving the "Superbrands" award

We only recorded a moderate growth of 5% for festive products sales in Hong Kong as the consumers are still reluctant to increase their spending on luxury products. Contrast to this, mooncake turnover in the PRC increased substantially with a booming economy there and our overall PRC turnover increased by 70% as a result. To prepare for an expanding market, we replaced a small outlet with two bigger and more lavishly decorated ones which were opened respectively in April and May 2004.

BREAD BOUTIQUE

Despite the replacement of our top sale outlet at Kowloon Bay by a smaller one, Bread Boutique still managed to maintain a moderate sales growth of 2% as occupancy rate continued to improve at the public estate at Lung Cheung where sales at this outlet was doubled. In order to enrich the product variety to customers, we have split certain premises and added "St Honore" to these shops in the past years. This strategy has been quite successful and our overall sales after the split improved and offset the impact of rising material costs to certain extent. Though we enjoyed rent concession during SARS period, the savings were more or less offset by increase in staff costs. As a result, our overall bottom line decreased by about 7%.



The newly opened Guangzhou Dong Chuan outlet



"Famous Mooncake" Award

EC EATERY

Our eatery business was able to recover the sales loss during the first quarter as a result of the outbreak of SARS to record a full year sales growth of 5%. Although the economy has recovered to some extent, consumers are still very cautious in spending and they keep looking out for creativity in the dining arena. To live up to their expectation, we are now changing our menu on a quarterly basis so as to preserve originality



New Designed Crunchy Nuts Waffles Gift Box



Chinese New Year Gold Pudding Gift Set



"Soup-based" Bread

EC EATERY (cont'd)

to our customers. We also upgraded the ingredients used in our menu. Our gross profit margin has been slightly affected in the second half of the year but our net profit has increased by 24% from the sales increment.

LIQUIDITY AND CAPITAL RESOURCES

Our freely-held cash on hand increased from approximately HK\$92.2 million as at 31 March 2003 to about HK\$131.0 million as at 31 March 2004 even though we have spent approximately HK\$37.1 million on new capital expenditure. The Group's financial position stays healthy with zero gearing. The Group plans to invest about HK\$45.0 million mainly to expand and upgrade the outlet network and production capacity. These projects will be financed internally and we do not have any need for external fund raising.

EMPLOYEES

At 31 March 2004, the Group had a total of 1,748 (2003: 1,670) full time employees. Employees are remunerated based on basic salaries and sales incentives which are only payable to some operational staff. Bonuses were discretionary in nature and were based on the performance of the employees and the Group. The Company has adopted a share option scheme to provide incentive to working staff. During the year, the employees of the Company exercised most of their share options granted under the share option scheme. Details of the scheme and the exercise are set out in the section headed "Share Options" in the report of the directors.

PLEDGE OF ASSETS

No assets were pledged as at 31 March 2004.

EXPOSURE TO FLUCTUATIONS IN EXCHANGE RATES AND RELATED HEDGES

The Group conducts most of its business transactions in currencies of Hong Kong dollars and Renminbi ("RMB"). To reduce the Group's exposure to the recent speculation of a revaluation of RMB, we have taken out forward contracts on a running twelve months basis to cover regular payments in this currency. As at 31 March 2004, the Group has committed in RMB forward exchange contracts which amounted to HK\$23 million and expiring within the next financial year (2003: Nil).

CONTINGENT LIABILITIES

The Group had no significant contingent liabilities as at 31 March 2004.