

## **Octagon Consolidated Berhad**

### **Commentary on unaudited financial performance for the financial year ended 31 October 2006**

1. The Group's turnover has increased slightly from RM75.037 million recorded in the financial year ended 31 October 2005 to RM75.107 million registered in the current financial year due to the improved contribution from its subsidiary in China, which has offset the drop in turnover of its other subsidiaries. Turnover contribution from its subsidiary in China has increase by approximately RM4.8 million or 72.6% from RM6.6 million recorded in the financial year ended 31 October 2005.
2. However, the Group's net profit has decreased by RM2.975 million or 22.47% from RM13.237 million recorded in financial year 2005 to RM10.262 million. The gross profit margin and net profit margin has also dropped from 41.6%% and 17.6% in 2005 to 38.4% and 13.7% in 2006, respectively. These are mainly due to the following:-
  - (a) Cost of goods sold has increased by approximately RM2.5 million from financial year 2005 although turnover has only increased by RM70,000. The ratio of raw material cost to turnover has increased by 3.2% to 61.6% in 2006.
  - (b) Selling expenses (which includes, among others, travelling, transportation and salaries) has also increased by approximately RM467,000 from RM1.915 million recorded in 2005 to RM2.382 million in 2006. The ratio of selling expenses to turnover has increased from 2.55% in 2005 to 3.17% in 2006.
  - (c) The higher overheads and other expenses amounting to approximately RM0.639 million pursuant to the Group's new waste to energy and continuous process pyrolysis projects, which are still under development.
  - (d) Higher amortisation cost of goodwill, which has increased by approximately RM360,000 as a result of full year consolidation of the subsidiary acquired in 2005.

The higher cost of goods sold, which has resulted in lower margin for certain products, e.g. plastic paints, and selling expenses are mainly as a result of the following:

- (a) the weaken consumer electrical products sector, where most of the products of the Group are applied. The gross export of consumer electrical products has registered average negative growth of more than 17% for the first three quarters of 2006 despite the electronics and electrical products registering positive growth.
- (b) As a result of the weaken consumer electrical products sector, the customers of the Group, namely major brand owner, are also affected by slow down in demand as well as increase in competitions.
- (c) Increase in oil prices has also affected the raw material costs. Due to the above-mentioned situation, the increased in raw material costs cannot be completely pass on to the customers. The increase in oil prices has also resulted in higher transportation and travelling costs.

- (d) Further, the customers are not in the position to increase their product pricing as a result of intense competitions from other local and overseas players. Hence, the pricing as well as margin for the coating products as a whole, including those of the Group's products, has been lower than previous years.
3. The Group has noted this trend and has implemented/are implementing various measures to further expand the customer and product base to improve turnover and margin.
  4. As one of the measures to expand customers base for its existing coatings products in the Original Equipment Manufacturer (OEM)'s Business, the Group is planning to set-up additional manufacturing plant in this region where ready market is available, i.e., where the customers of the Group has established operations and required support from the Group.
  5. The Group is also increasing its focus on higher margin products such as ultra-violet (UV) paints as well as the developing of higher end products for its OEM Business.
  6. In its effort to improve products base, the Group has also through its associated company, Advanced Coatings and Surface Technologies Sdn Bhd ("ACST"), ventured into coatings for the Aviation industry. ACST has been appointed by Majlis Amanah Raya ("MARARA") as the Master Business Incubator under the AIROD-MARA Aviation Vendor Development Program for Aircraft Paint Stripping and Painting. In addition, ACST has recently received orders from MHS Aviation Berhad and Fly Asian Xpress Sdn Bhd.
  7. Meanwhile, the Group's investment in the new ventures, namely the renewable energy business under Green Energy and Technology Sdn Bhd and Melaka Waste to Energy Sdn Bhd, the continuous process pyrolysis project undertaken by Advanced Pyrotech Sdn Bhd are under development and has yet to contribute to the Group's earnings but are expected to contribute positively to the Group's earnings once fully operational.