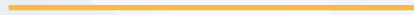




TELLY TOY LIMITED



BUSINESS ANALYSIS

CONTENTS

1 Profitability Analysis

2 Strategy Evaluation

- 2.1 Situation Analysis
- 2.2 Strategy Selection

3 Proposed Strategies

- 3.1 Internal Control
- 3.2 Related Diversification Strategies

4 Implementation Plan & Financial Prediction

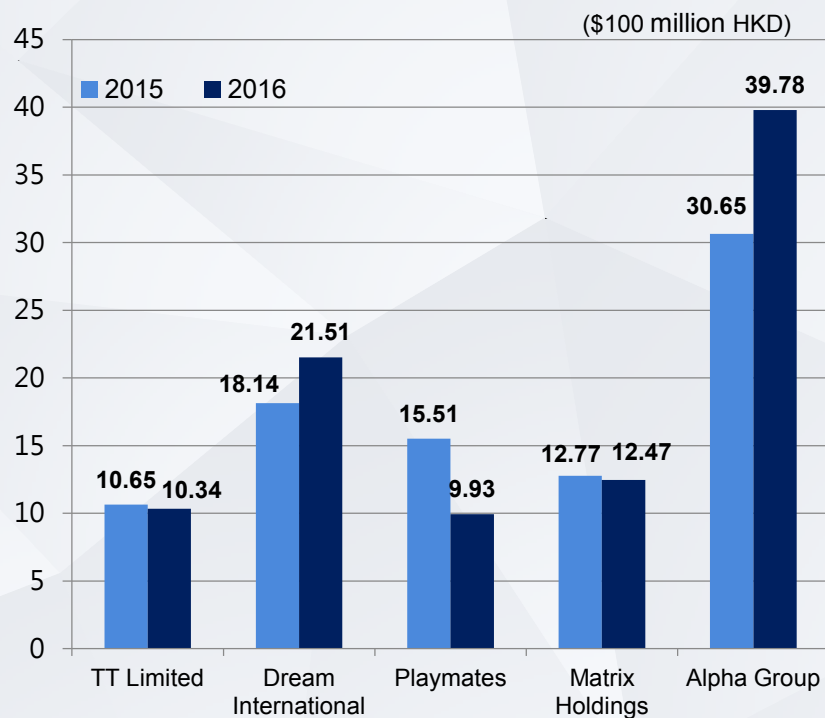
5 Ethical Issues

**Profitability
Analysis**

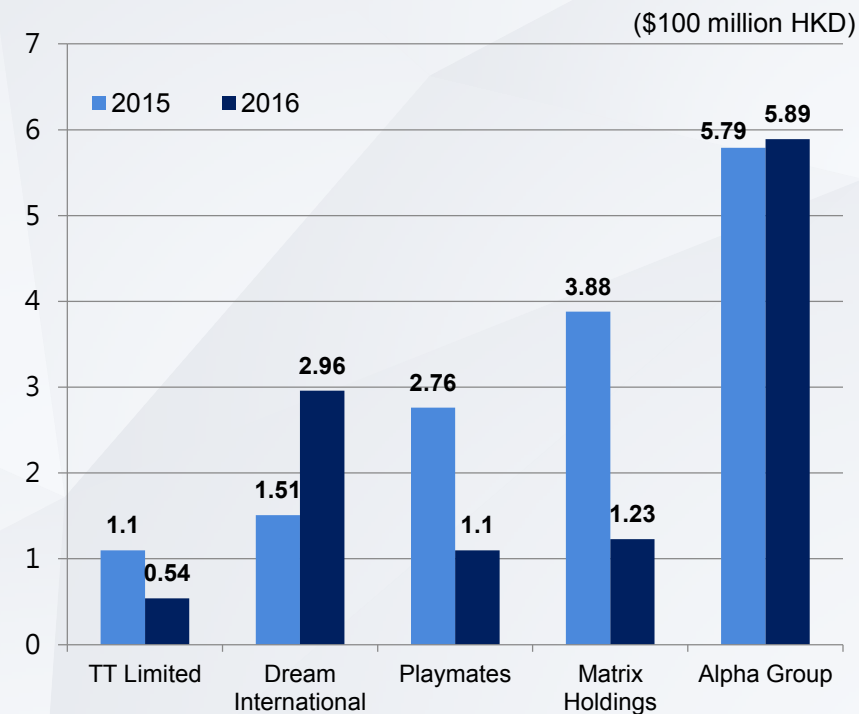
01

Profitability Analysis | Peer Comparison

Revenue



Net Profit



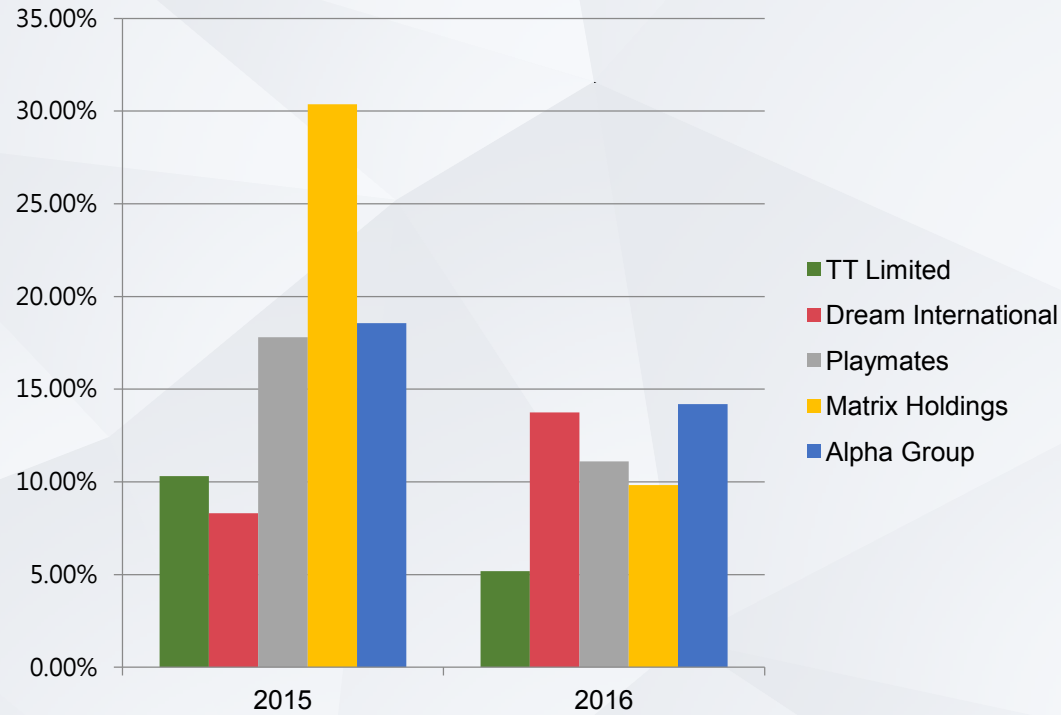
- Relatively low revenue & profit among industry

- **Discrepancy:** Revenue 2.9% ↓

Net Profit 50.9% ↓

Profitability Analysis | Peer Comparison

Profit Margin



Bad performance on converting income to profit

- Insufficient generated income
- Poor cost control
- External factors

Profitability Analysis | Cost Problem

1. Increasing Inventory Cost

	2015	2016	Change
TT Limited	6.40	5.56	13%↓

- Inventory turnover rate declined
- Extra storage cost

2. Increasing Financing Cost

	TT Limited		Dream International		Playmates		Matrix Holdings		Alpha Group	
	2015	2016	2015	2016	2015	2016	2015	2016	2015	2016
Equity Multiplier	2.03	2.04	1.27	1.30	1.22	1.17	1.17	1.21	1.56	1.71

- Relatively high equity multiplier - too much use of **debts**
- Base-rate margin raised by bank

3. Currency Fluctuation Cost

- No hedging activity

Profitability Analysis

Low Income

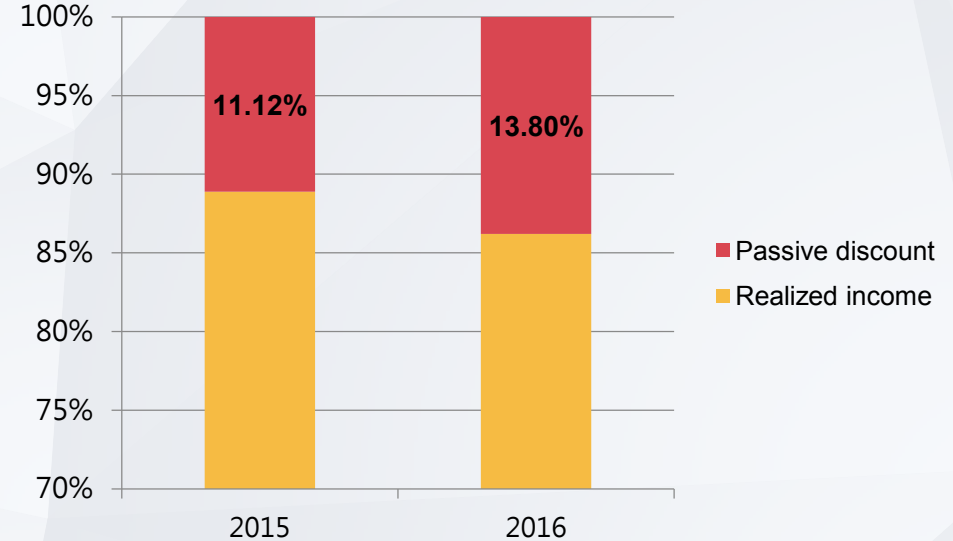
1. Lack of growth opportunity

- Low Plowback Ratio
- No new store opened
- No expansion plan

	2015	2016	Change (%)
Plowback Ratio	54.47%	6.78%	47.69 ↓

2. Unfavorable Product Price Discount

- Over 10% total discount each year
- Customer expectation mismatch



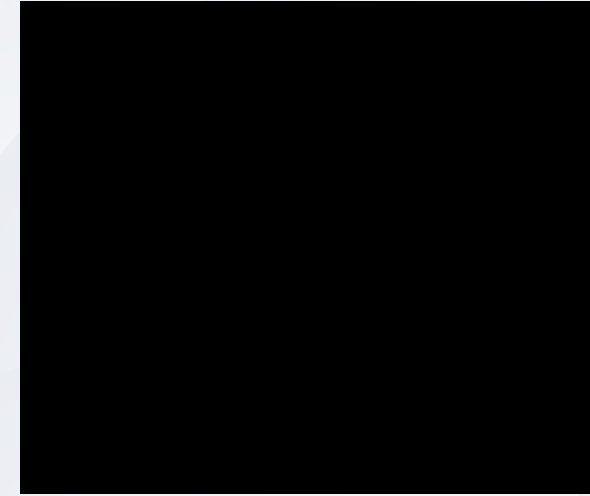
Profitability Analysis | External Factors



Depressed global economy



Downturn of the whole
toy industry



Less visitor to Hong Kong

Cannot easily change

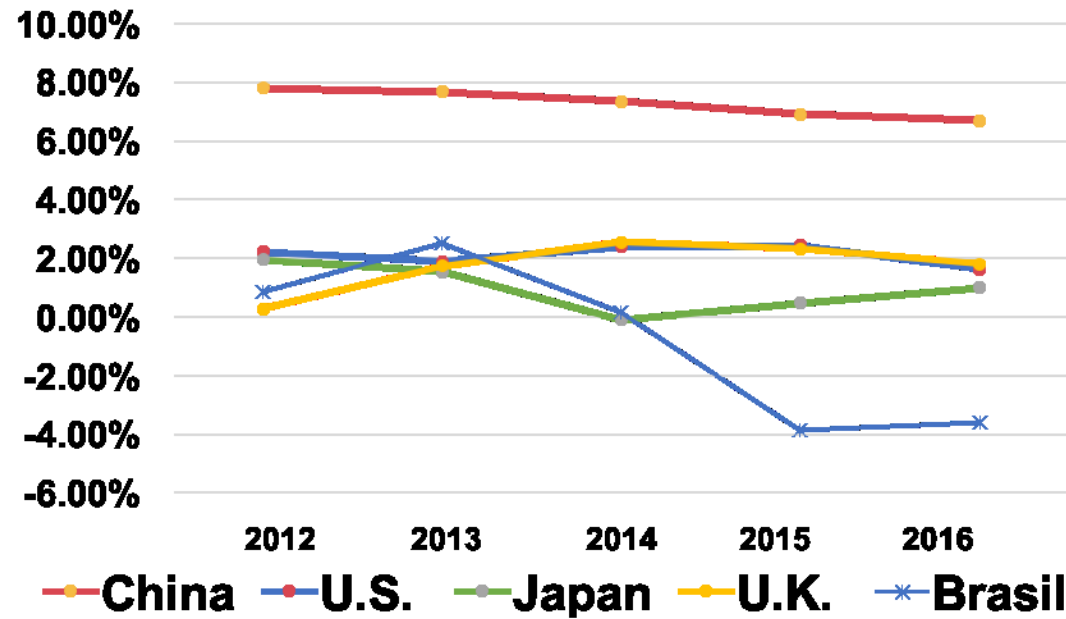
Take into consideration

**Strategy
Evaluation**

02

Situation Analysis | Macro Factor

Annual GDP Growth Rate



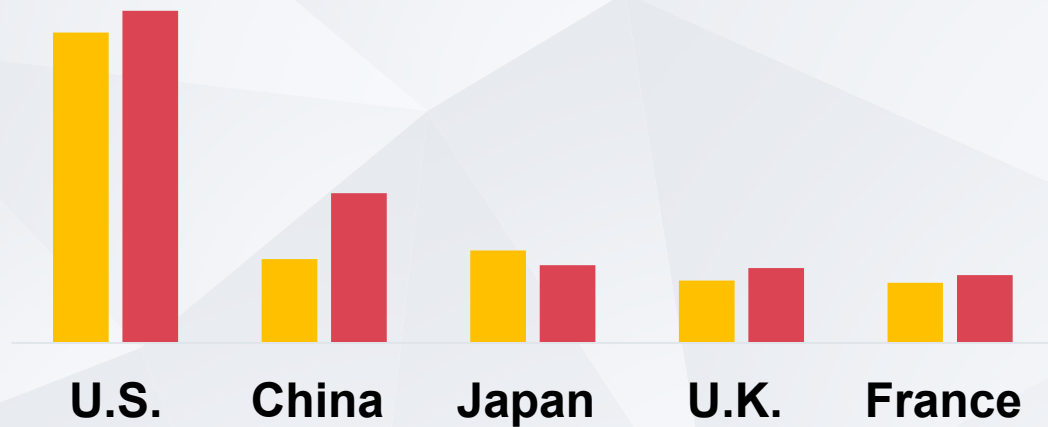
- ◆ High annual GDP growth rate of China
- ◆ Relatively stable
- ◆ Potential market

Situation Analysis

Macro Factor

Toys Retail Sales

■ Year 2010(\$million) ■ Year 2015 (\$ million)



Overseas Market:

Limited growth space



Domestic Market:

Stable compounding growth

(Annual compounding rate around 8.63% in 2002-2016)

Reached 12.33% in 2015

Industry Analysis | SWOT Analysis

Competitors Perspectives

Inside

Industry rivalry: High

- ◆ International and domestic competitors
(The first 5 top companies occupied 15.5% market share in domestic market in 2016)

Outside

Threat of substitutes: High

- ◆ Attractive alternatives to replace toys.

Threat of new entrants: Moderate

- ◆ Increasing customers' need (**Two-child Policy**)
- ◆ Low entrants barriers

Industry Analysis | SWOT Analysis

Buyers: High



- ◆ Low cost of changing brands
- ◆ Give priority to quality of toys

Bargaining Power Perspectives

Suppliers: Moderate



- ◆ Limited qualified suppliers
- ◆ Suppliers stand on relatively advantage position in supply and demand relationship

Market Analysis | SWOT Analysis

Internal Perspectives



Strengths

- ◆ Established product portfolio
(Jungle Land)
- ◆ Mature Listed Company

Weaknesses



- ◆ Cost control
Dangerous **financial leverage** (Equity Multiplier: 2.04%)
- ◆ Lack of growth opportunity
- ◆ Mismatch customer expectation

Market Analysis

SWOT Analysis

External Perspectives



Opportunity

- ◆ High **value-added** IP products
(6.55% sale compounding growth rate
in 2016)
- ◆ **Consumer experience** Trend
(Consumption upgrade)



Threats

- ◆ Intense competition
- ◆ The declining traditional toys industry

Strategy Selection



	Market Penetration	Market Development	Product Development	Withdrawal	Internal Control
Expand potential market ★★★★★		✓			
Meet increasing demand of potential customers ★★★★		✓	✓		
Differentiate products ★★★			✓		
Satisfy fast changing tastes ★★★	✓		✓		
Prevent fraud and protect company's assets ★★					✓
Reduce the cost ★★★★★				✓	✓

- The greater the number of stars, the more effective and important of the strategy
- Expand potential market & meet customer's demand: **enlarge the business scale**
- Differentiate products & satisfy fast changing tastes: **enhance competitiveness and attractiveness**
- Reduce cost: **improve operational efficiency**

Strategy Selection Results



Internal control:

- Seasonality Issue
- Supply chain management
- Improvements on IT system and Online shopping system

Related diversification strategy:

- Experiential consumption
- “TTid” online customization & design-sharing platform
- Educational institution cooperation

**Proposed
Strategy**

03

Internal control | Seasonality Issue



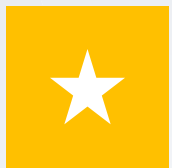
Problem:

Sales volumes are seasonal. TT Limited seeks to dispose of their unsold items in the late summer and in January.



Solutions:

- Calculate **Reorder Point**
- Follow the **big data trend**



Effects on discounted goods during 2017:

The rate of discounted good sold : ↓ 4%, from 27% to 23%

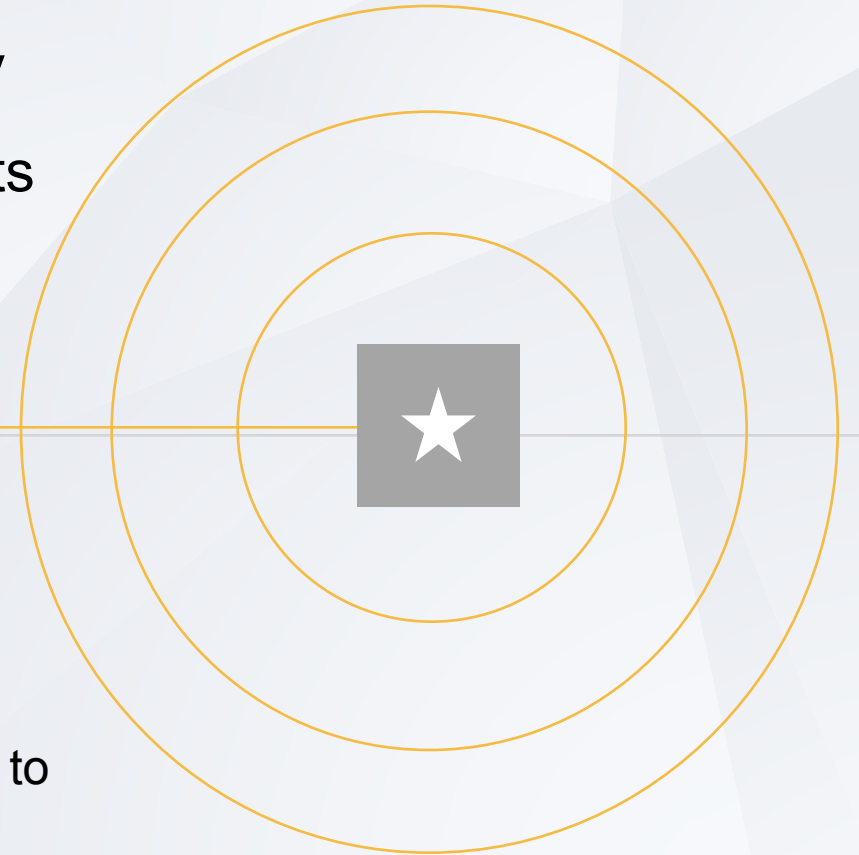
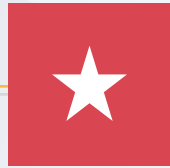
The rate of items give away: ↓ 1%, from 3% to 2%

Gross profit: ↑ 4%, from 58.8% to 62.9%

Internal control | Supply Chain Management

Difficulties in negotiating with suppliers:

- **Failure** in using **just-in-time** method to reduce inventory
- **Supply shortages** for some of the most popular products
- **High** inventory purchasing **price**



Solutions:

- Sign **long-term contracts**
 - Build up the confidence to the stable business relationship to have a better negotiation with suppliers
- Purchase in a large amount before sales peak
 - Get the discount price

Internal control | IT and Online-shopping System

Improvements on IT system:

- Solve **discrepancies problems** on inventory
 - Theft of items from stores
 - Unrecorded customer returns
- Provide **technology support** for customized products



Improvements on Online-shopping system:

- **Expand** small scale of online-shopping business
 - Opening online stores on Alibaba and JD.

Internal & External Strategy

Internal control:

- Seasonality Issue
- Supply chain management
- Improvements on IT system and Online shopping system



Related diversification (mixed) strategy:

- Experiential consumption
- “TTid” online customization & design-sharing platform
- Educational institution cooperation

Related Diversification Strategies

Goals and uniqueness

Goals

- Improve brand awareness
- Enhance profitability

Features

- Omni-channel strategies
- Interaction between customers, stores and products – Experiential Consumption
- Be a component of commercial chain shopping malls – Experiential Consumption
- Online platform for customization and design-sharing – “TTid”
- B2B and early education-market – Educational institution cooperation

Experiential (to customer)

- Offer both products and service
- Emphasize on “experience” more than simply “price”
- Interaction-oriented

Shopping mall component (to cooperator)

- Family element
- Provide solution to parents
- Combine functions of resort and shop
- Consumption upgrade

Goals (benefit to TT Limited)

- Brand(IP) awareness
- Develop together with commercial estate
- Long-term contract to generate steady income

Related Diversification Strategies

Experiential Consumption

Place selection:



	2019	2020	2021
New stores	3	5	7
Cities	Zhuhai*1 Zhongshan* 1 Xiamen*1	Hangzhou*2 Tianjin*1 Suzhou*1 Nanjing*1	Chengdu*2 Changsha*2 Qingdao*1 Shenyang*1 Chongqing*1

- New tier-one, tier-two and tier-three cities
- Relatively low rent and low employee expense
- Increasing income level

Target customer:

- Indoor playground: 3-8 years old kids
- VR game zone: children above 10; adults

Related Diversification Strategies

“TTid” - Customizing Products

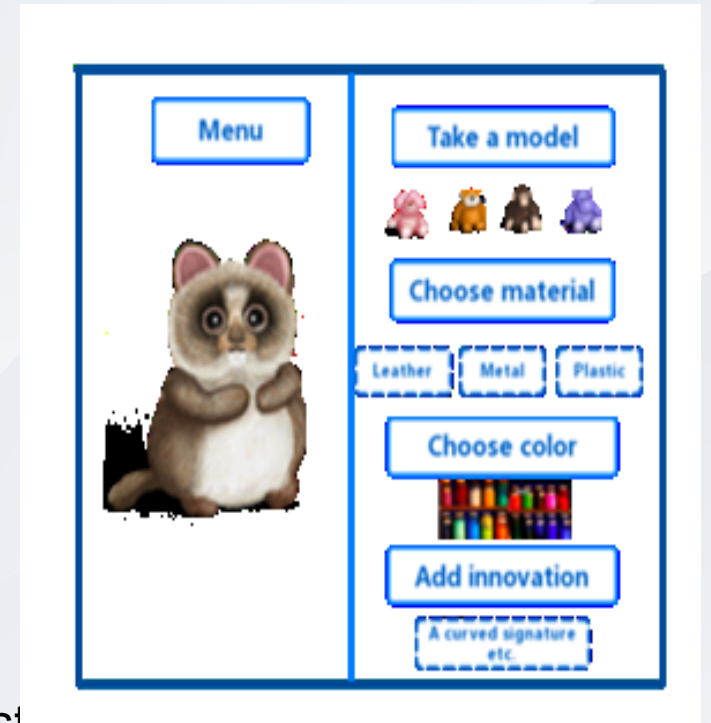
Customized products

- Online shopping platform
- High-end products
- Minimize mismatch of customer expectation

Design forum & competition

- Benign interaction between company and customer
- Stimulate more **IP awareness**
- Keep attractive with less cost

Target Customer: Diversified in age - suitable for customer in different ages.



Opportunity

- High compounded market size growth rate of childhood education



- Immature market: lack of industry leader

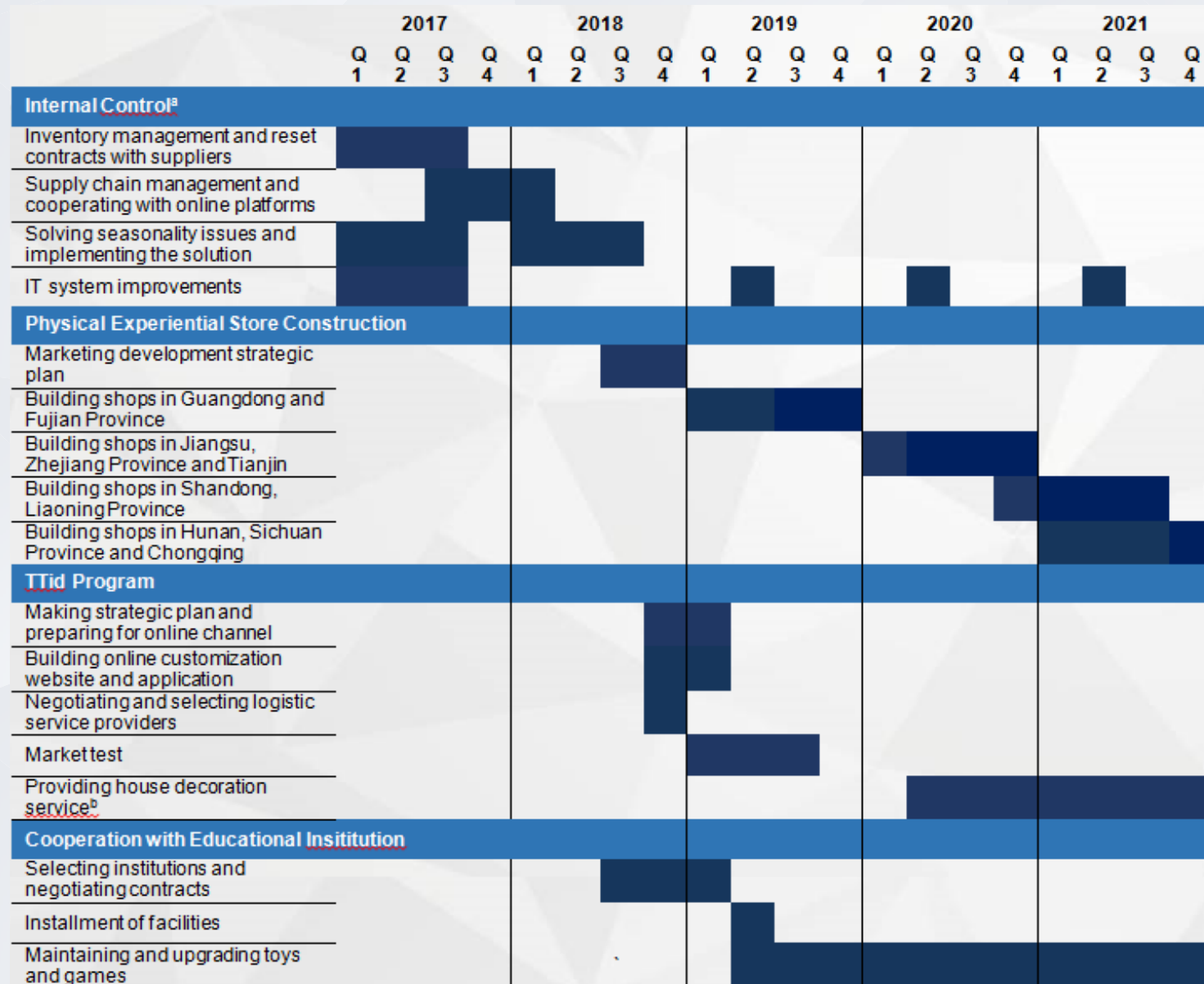
Educational facilities

- Playground series
 - IP characters
- Application for better communication between teachers, parents and kids
 - Teachers: assign and check homework
 - Parents: in-time communication
 - Kids: discussion and competition

**Implementation Plan
& Financial Predictions**

04

Implementation Plan | Working Schedule



2017-2018

- Internal control strategy

2019-2021

- Related diversification strategy

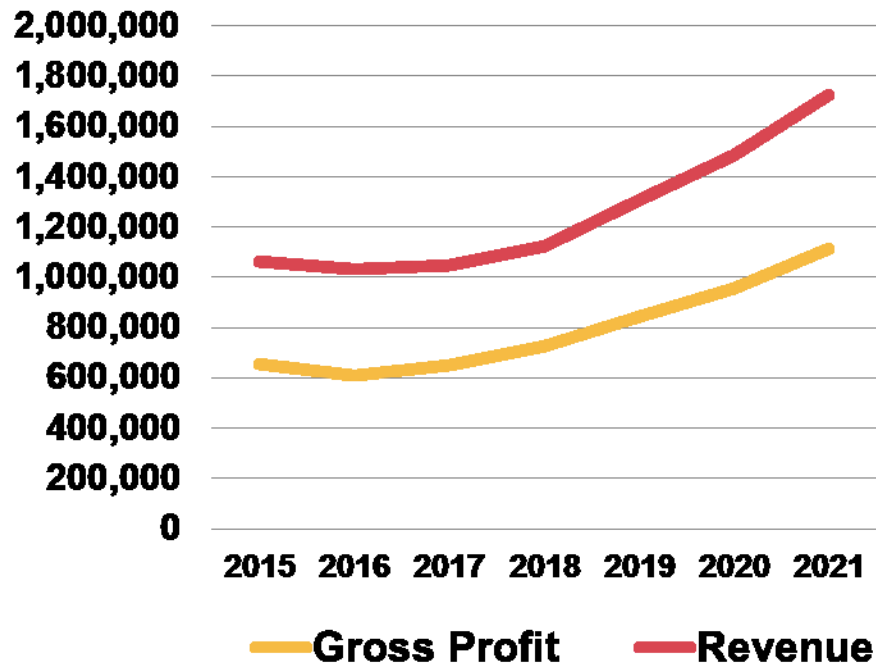
Implementation Plan

Projected Income Statement

	2015	2016	2017	2018	2019	2020	2021
	HK\$000	HK\$000	HK\$000	HK\$000	HK\$000	HK\$000	HK\$000
Revenue	1,065,257	1,034,237	1,048,248	1,126,291	1,308,011	1,486,155	1,724,456
Cost of goods sold	(407,502)	(426,108)	(400,116)	(401,072)	(462,905)	(528,328)	(611,837)
Gross profit	657,755	608,129	648,132	725,219	845,106	957,827	1,112,619
Gross profit ratio	61.75%	58.80%	61.83%	64.39%	64.61%	64.45%	64.52%
Operating Costs							
Employee costs	(211,861)	(221,768)	(228,398)	(242,102)	(262,923)	(281,327)	(309,460)
Occupancy costs(rent)	(106,167)	(108,325)	(109,408)	(111,879)	(169,342)	(224,145)	(284,154)
Property repairs and maintenance	(18,080)	(16,730)	(22,586)	(30,490)	(31,100)	(33,099)	(40,874)
Depreciation	(77,594)	(77,621)	(80,726)	(83,955)	(88,153)	(96,968)	(113,452)
Other costs	(96,295)	(102,130)	(103,151)	(104,183)	(107,308)	(111,601)	(128,341)
Total operating costs	(509,997)	(526,574)	(544,269)	(572,609)	(658,826)	(747,140)	(876,281)
Operating profit	147,758	81,555	103,863	152,610	186,280	210,687	236,338
Finance costs	(16,226)	(17,321)	(14,726)	(12,053)	(9,475)	(6,897)	(4,347)
Profit before taxation	131,532	64,234	89,137	140,557	176,805	203,790	231,991
Taxation	(21,703)	(10,599)	(14,708)	(23,192)	(29,173)	(33,625)	(38,279)
Profit after taxation	<u>109,829</u>	<u>53,636</u>	<u>74,429</u>	<u>117,365</u>	<u>147,632</u>	<u>170,165</u>	<u>193,712</u>

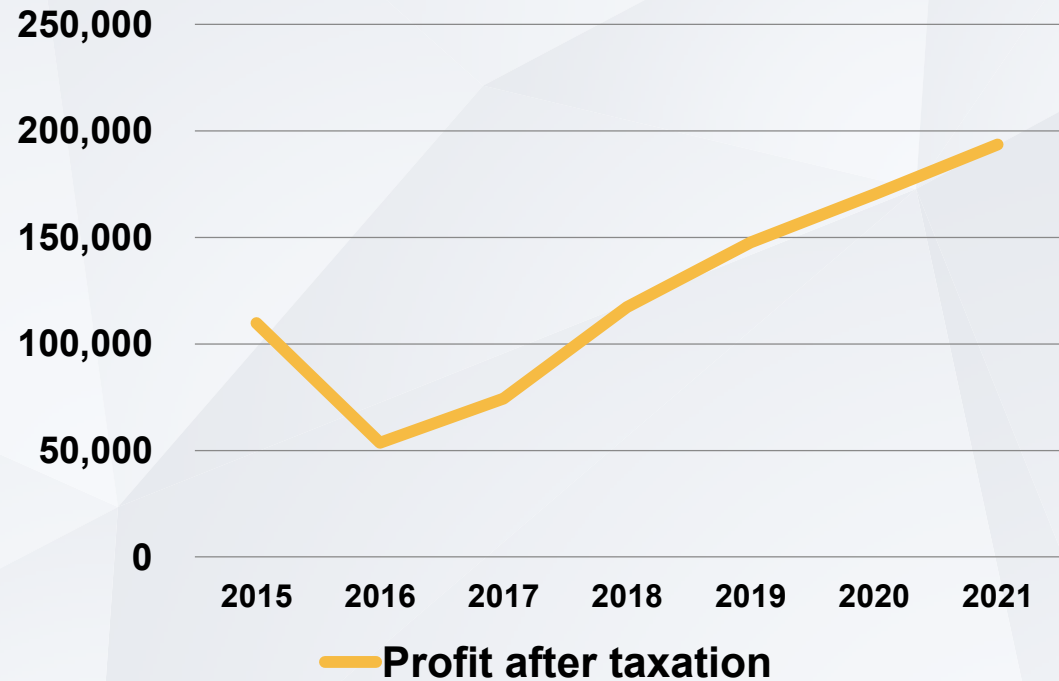
- Revenue & Gross Profit
- GP Ratio
- Net profit

Gross Profit and Revenue



- Revenue increase by 64.5% in five years
- Accelerated growth rate from 2019 to 2021

Profit after taxation



- Profit bounce back start from 2017
- Relatively steady growth rate

Implementation Plan

Projected Cash Flow Statement

	2017	2018	2019	2020	2021
	HK\$000	HK\$000	HK\$000	HK\$000	HK\$000
Operating activities					
Income before taxes	89,137	140,557	176,805	203,790	231,991
Depreciation, amortization and impairment loss	-47,726	-70,736	-74,980	-81,728	-90,718
Operating profit before working capital changes:	41,411	69,821	101,825	122,062	141,273
Increase in receivables and other assets	-135	-274	-356	-463	-602
Increase in inventories	-14,032	-19,720	-23,664	-28,396	-32,940
Increase in accounts payable and other liabilities	11,468	12,350	14,449	15,462	16,235
Pay back loans and debts	-28,561	-41,125	-41,309	-41,368	-41,401
Cash generated from operations before interest and taxes	10,151	21,052	50,945	67,297	82,565
Income tax paid	-1,675	-3,474	-8,406	-11,104	-13,623
Net cash generated from operating activities	8,476	17,578	42,539	56,193	68,942
Investing activities					
Purchase of property, plant and equipment	-21,870	-26,654	-41,353	-56,137	-72,428
Net cash used in investing activities	-21,870	-26,654	-41,353	-56,137	-72,428
Financing activities					
Dividend paid to shareholders of TT Limited	-51,646	-55,584	-71,321	-83,857	-97,360
Payout ratio	69.39%	47.36%	48.31%	49.28%	50.26%
Cash received from issuing shares	453,131	0	0	0	0
Net cash generate from financing activities	401,485	-55,584	-71,321	-83,857	-97,360
Net change in cash and cash equivalents	388,091	-64,660	-70,135	-83,801	-100,846
cash balance at prior year-end	105,008	493,099	428,439	358,304	274,503
cash balance at current year-end	493,099	428,439	358,304	274,503	173,657

- Inadequate profit
- Lack of adequate capital to support development strategies
- Constant dividend growth
- Stable and sufficient cash flow

Fund Raising Analysis

01

Bank loan and issuing bond



02

Reducing dividend



03

Issuing additional shares

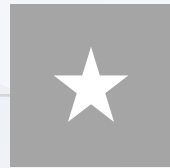


Reasons

- High financial leverage
- High interest rate
- Hurt the reputation of company
- Influence the benefit of existing shareholders
- Protect the equity structure

Right Issue

- **Additional issuing of shares:
453 million HK dollar in 2017**



- **Reissue around 48.9
million new shares**

- **The average price: 10.32 HKD**

Implement Method

- 1 Outsource**
- Toy production
 - Applications & website

- 2 Forward**
- Hedge foreign exchange risk

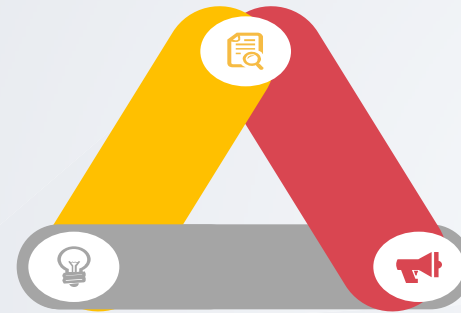
optimization

Customer
Relationship
Management

Improve service quality

Issue credit cards

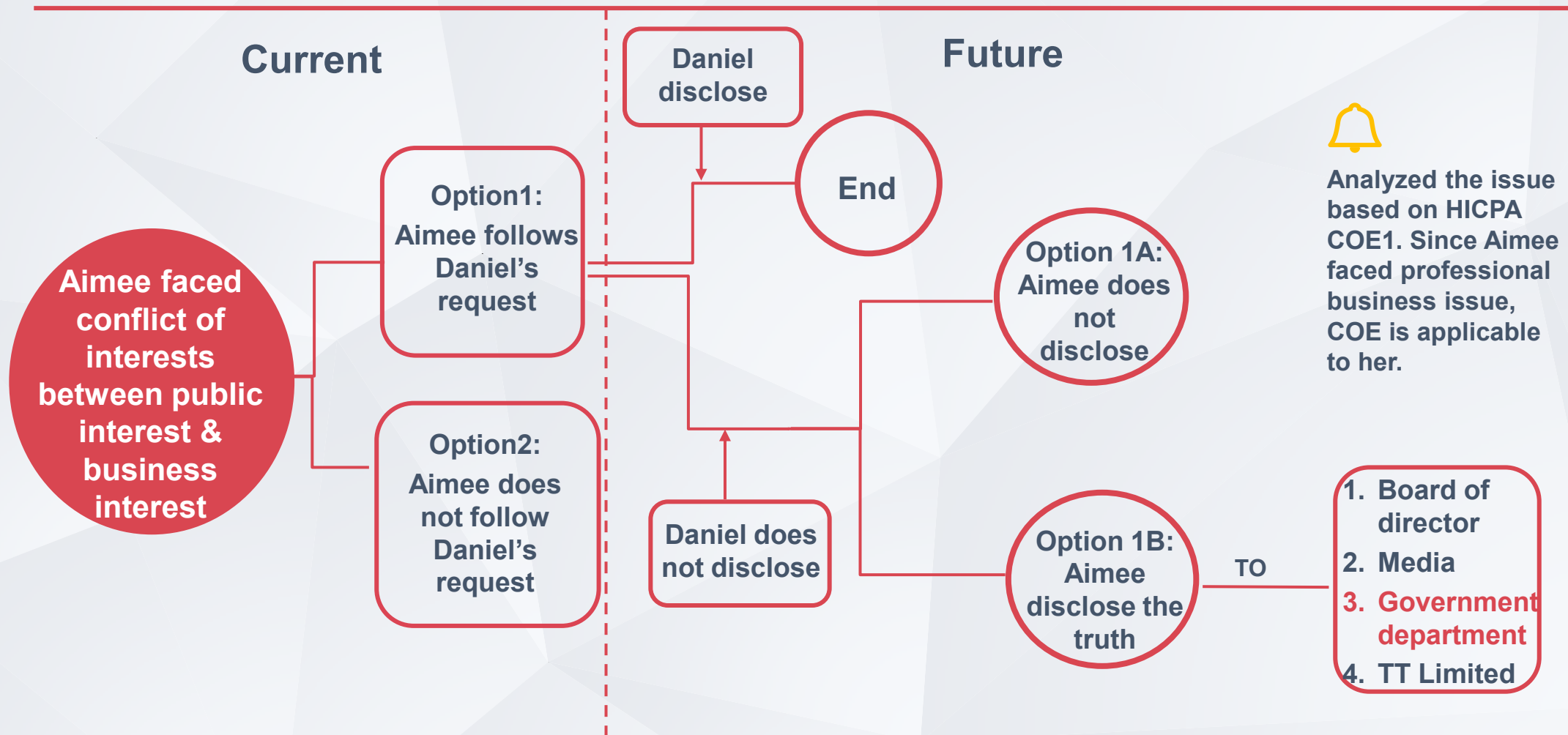
Gather feedback



Ethics Issue

05

Ethical Issue Analysis



Ethical Issue Analysis

Applied COE



Integrity



Objectivity



Profession



Confidentiality

Option 1
(Follow the request)

Disobey

Disobey

Obey
(General duty to protect
company's benefit)

Obey

Option 2
(Does not follow)

Obey

Obey

Disobey

Disobey
(Violate the confidentiality
regulation)

Ethical Issue Analysis | Additional Issue

To Board of Director

Possible to burry information and fire Aimee



Additional issue

Aimee should disclose to which party

To media

Damage reputation and long-term economic viability

To Government

Fair investigation and provide legal advice



Best Choice

To TT Limited

Possible to cheat to the public and cover the scandal