

NOTES TO THE FINANCIAL STATEMENTS

31 December 2001

1. BASIS OF PREPARATION

a) General

The Company was incorporated in Bermuda as an exempted company with limited liability and its shares are listed on The Stock Exchange of Hong Kong Limited (the "Stock Exchange").

The Company acts as an investment holding company. The Group is principally engaged in the design, manufacture, sale and distribution of baby products comprising mainly musical toys and components, plastic and electronic toys, ride-on cars and motorised toy vehicles.

b) Group accounts

The group accounts include the accounts of the company and its subsidiaries made up to 31st December. The results of subsidiaries acquired or disposed of during the year are included in the consolidated income statement from the effective date of acquisition or up to the effective date of disposal, as appropriate.

All significant intercompany transactions and balances within the group are eliminated on consolidation.

2. PRINCIPAL ACCOUNTING POLICIES

The financial statements have been prepared in accordance with generally accepted accounting principles in Hong Kong and comply with Statements of Standard Accounting Practice ("SSAP") issued by the Hong Kong Society of Accountants.

a) Revenue recognition

- i) Revenue from the sale of goods is recognised on the transfer of risks and rewards of ownership, which generally coincides with the time when the goods are delivered to customers and title has passed.
- ii) Interest income is recognised on a time proportion basis, taking into account the principal amounts outstanding and the interest rates applicable.

NOTES TO THE FINANCIAL STATEMENTS

31 December 2001

2. PRINCIPAL ACCOUNTING POLICIES *(Continued)*

b) Borrowing costs

Borrowing costs are interests and other costs incurred in connection with the borrowings of funds. The borrowing costs that are directly attributable to the acquisition, construction or production of an asset that necessarily takes a substantial period of time to get ready for its intended use or sale are capitalised as part of the cost of that asset. All other borrowing costs are charged to the income statement in the year in which they are incurred.

c) Research and development costs

Research and development costs are expensed as incurred, except where the product or process is clearly defined and the costs attributable to the product or process can be separately identified and measured reliably; is technically feasible; the company intends to produce and market, or use, the product or process; the existence of a market for the product or process or, if it is to be used internally rather than sold, its usefulness to the company, can be demonstrated; and adequate resources exist, or their availability can be demonstrated, to complete the project and market or use the product or process.

Such development costs are recognised as an asset to the extent of the amount that, taken together with further development costs, related production costs, and selling and administrative costs directly incurred in marketing the product, is probable of being recovered from related future economic benefits. The excess amount is written off as incurred.

The development costs, recognised as an asset, are amortized on a straight-line basis over a period of 5 years to reflect the pattern in which the related economic benefits are recognised.

d) Property, plant and equipment

Property, plant and equipment other than investment properties and other properties are stated at cost less accumulated depreciation.

NOTES TO THE FINANCIAL STATEMENTS

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2. PRINCIPAL ACCOUNTING POLICIES *(Continued)*

d) **Property, plant and equipment** *(Continued)*

Property, plant and equipment are depreciated at rates sufficient to write off their cost over their estimated useful lives on a straight-line basis. The principal annual rates are as follows:

Leasehold land	Over the lease term
Buildings	Over the lease term
Furniture, fixtures and equipment	20%
Moulds	20%
Leasehold improvements	20%
Motor vehicles	33-1/3%
Plant and Machinery	20%

Major costs incurred in restoring property, plant and equipment to their normal working condition are charged to the income statement. Improvements are capitalised and depreciated over their expected useful lives to the company.

The carrying amount of property, plant and equipment are reviewed regularly to assess whether their recoverable amounts have declined below their carrying amounts. Expected future cash flows have not been discounted in determining the recoverable amount.

The gain or loss on disposal of property, plant and equipment other than investment properties is the difference between the net sales proceeds and the carrying amount of the relevant asset, and is recognised in the income statement.

e) **Assets under leases**

i) *Finance leases and hire purchase contracts*

Leases that substantially transfer to the company all the rewards and risks of ownership of assets are accounted for as finance leases and hire purchase contracts. At the inception of a finance lease and hire purchase contracts, the fair value of the asset is recorded together with the obligation, excluding the interest element, to pay future rentals.

Payments to the lessor are treated as consisting of capital and interest elements. Finance charges are debited to the income statement over the periods of the leases so as to produce an approximately constant periodic rate of charge on the remaining balances of the obligation for each accounting period.

NOTES TO THE FINANCIAL STATEMENTS

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2. PRINCIPAL ACCOUNTING POLICIES *(Continued)*

e) **Assets under leases** *(Continued)*

i) *Finance leases and hire purchase contracts (Continued)*

Assets held under finance leases and hire purchase contracts are depreciated over the shorter of the lease terms and their estimated useful lives on the same basis as owned assets.

ii) *Operating leases*

Leases where substantially all the rewards and risks of ownership of assets remain with the leasing company are accounted for as operating leases. Rentals payables under such operating leases are accounted for in the income statement on a straight-line basis over the periods of the respective lease.

f) **Subsidiaries**

A subsidiary is a company in which the company directly or indirectly, controls more than half of its voting power or issued share capital or controls the composition of its board.

Investments in subsidiaries in the balance sheet are stated at cost less provision, if necessary, for any permanent diminution in value. The results of subsidiaries are accounted to the extent of dividends received and receivable.

g) **Associates**

An associate is a company in which the company has significant influence and which is neither a subsidiary nor a joint venture of the company.

The investments in associates are stated at cost less provision, if necessary, for any permanent diminution in value, such provision being determined for each associate individually. The results of associates are accounted for to the extent of dividends received and receivable.

The investments in associates are accounted for in the consolidated balance sheet under the equity method whereby the investments are initially recorded at cost and adjusted thereafter for the post acquisition change in the company's share of net assets of the associates. The results of the associates are accounted for in the consolidated income statement to the extent of the company's share of the associates' results of operations.

NOTES TO THE FINANCIAL STATEMENTS

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2. PRINCIPAL ACCOUNTING POLICIES *(Continued)*

h) Related Parties

Two parties are considered to be related if one party has the ability, directly or indirectly, to control the other party or exercise significant influence over the other party in making financial and operating decisions. Parties are also considered to be related if they are subject to common control or common significant influence.

i) Inventories

Inventories are stated at the lower of cost and net realizable value. Cost, calculated on a first-in, first-out basis, comprises all costs of purchases, costs of conversion and other costs incurred in bringing the inventories to their present location and condition.

Net realizable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

j) Trade receivables

Provision is made against trade receivables to the extent that they are considered to be doubtful. Trade receivable in the balance sheet is stated net of such provision.

k) Cash equivalents

Cash equivalents are short-term, highly liquid investments which are readily convertible into known amounts of cash without notice and which were within three months of maturity when acquired; less advances from banks repayable within three months from the date of the advance. Cash equivalents include investments and advances denominated in foreign currencies provided that they fulfil the above criteria.

l) Deferred taxation

Deferred taxation is accounted for under the liability method in respect of timing differences between profit as computed for taxation purposes and profit as stated in the accounts to the extent that a liability or asset is expected with reasonable probability to crystallise in the foreseeable future. Deferred tax asset is not recognised unless its realization is assured beyond reasonable doubt.

NOTES TO THE FINANCIAL STATEMENTS

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2. PRINCIPAL ACCOUNTING POLICIES *(Continued)*

m) Translation of foreign currencies

Transactions in foreign currencies during the year are translated at exchange rates ruling at the transaction dates. Monetary assets and liabilities expressed in foreign currencies at the balance sheet date are translated at rates of exchange ruling at the balance sheet date. Exchange differences arising in these cases are dealt with in the income statement.

The accounts of subsidiaries and associates expressed in foreign currencies are translated at the rates of exchange ruling at the balance sheet date.

3. SEGMENTAL INFORMATION

The Group has one business segment only. The Group turnover analysed by geographical market is as follows:

	1/1/2001 to 31/12/2001 HK\$'000	1/1/2000 to 31/12/2000 HK\$'000
North America (principally the United States of America)	84,255	109,962
Asia	21,553	15,541
Europe	5,350	7,276
South America	187	958
Others	1,599	304
	<u>112,944</u>	<u>134,041</u>

Contribution to net loss by geographical market has not been presented as the contribution to net loss from each market is substantially in line with the overall Group ratio of net loss to turnover.

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4. TURNOVER AND REVENUE

	2001 <i>HK\$'000</i>	2000 <i>HK\$'000</i>
Turnover		
Sale of goods	112,944	134,041
Other revenue		
Gain on disposal of property, plant and equipment	109	—
Interest income	150	891
Exchange gain	9	483
Others	3,300	3,543
	3,568	4,917
Total revenue	116,512	138,958

5. COST OF SALES

Included in the cost of sales is an amount of HK\$10,743,000 (2000: HK\$9,899,000) being provision for slow moving stocks.

6. FINANCE COSTS

	2001 <i>HK\$'000</i>	2000 <i>HK\$'000</i>
Interest on:		
Bank loans and overdrafts wholly repayable within 5 years	2,175	2,959
Loans from a director wholly repayable within 5 years	1,033	2,451
Other borrowings wholly repayable within 5 years	2,333	8
Obligations under finance leases and hire purchase contracts	103	280
	5,644	5,698

NOTES TO THE FINANCIAL STATEMENTS

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7. LOSS BEFORE TAXATION

Loss before taxation is stated after crediting and charging the following:

	2001 <i>HK\$'000</i>	2000 <i>HK\$'000</i>
Crediting		
Gain on disposal of property, plant and equipment	109	—
Interest income	150	891
Exchange gain	9	483
	<u> </u>	<u> </u>
Charging		
Amortisation of research and development costs	928	1,506
Auditors' remuneration	474	594
Staff costs, included directors' emoluments	20,232	23,086
Bad debts written off	1,307	615
Depreciation		
Owned assets	8,582	9,326
Assets held under finance leases and hire purchase contracts	88	1,322
Provision for impairment loss of property, plant and equipment	2,500	8,000
Provision for doubtful debts	2,625	3,625
Operating leases		
Moulds	168	—
Premises	1,487	1,428
Exchange loss	19	—
	<u> </u>	<u> </u>

8. TAXATION

The amount of taxation charged to the income statement represents:

	2001 <i>HK\$'000</i>	2000 <i>HK\$'000</i>
Overprovision of Hong Kong profits tax in prior years	—	5
Overseas taxation	(9)	(4)
	<u> </u>	<u> </u>
	(9)	1
	<u> </u>	<u> </u>

NOTES TO THE FINANCIAL STATEMENTS

31 December 2001

8. TAXATION (Continued)

No Hong Kong profits tax has been provided for in the financial statements as the Group has no assessable profits for the year.

No provision for deferred taxation has been made for the year as the effect of all timing differences is not material.

9. DIRECTORS' REMUNERATION

Remuneration of the company's directors disclosed pursuant to section 161 of the Hong Kong Companies Ordinance is as follows:

	2001 <i>HK\$'000</i>	2000 <i>HK\$'000</i>
Directors' fees:		
Executive	—	—
Independent non-executive	120	120
	120	120
Other emoluments (executive directors)		
Salaries (including benefits in kind)	1,026	3,233
Contribution to retirement benefits scheme	101	292
Long service payment	413	660
	1,660	4,305

The directors' emoluments were within the following bands:

	1/1/2001 to 31/12/2001 Number of directors	1/1/2000 to 31/12/2000 Number of directors
Nil - HK\$1,000,000	5	4
HK\$1,000,001 - HK\$1,500,000	—	1
HK\$1,500,001 - HK\$2,000,000	—	1

NOTES TO THE FINANCIAL STATEMENTS

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10. EMPLOYEES' EMOLUMENTS

Details of emoluments paid to the five highest paid individuals (including directors and other employees) are:

	2001 <i>HK\$'000</i>	2000 <i>HK\$'000</i>
Basic salaries, allowances and benefits in kind	2,438	3,984
Contributions to retirement benefits scheme	216	687
	<hr/> 2,654 <hr/>	<hr/> 4,671 <hr/>

The five highest paid individuals included two (2000: five) directors of the Company, details of whose emoluments have been included in note 9 above.

Analysis of emoluments of the five highest paid individuals (including directors and other employees) by number of individuals and emolument range is as follows:

	2001 Number of employees	2000 Number of employees
Nil - HK\$1,000,000	5	3
HK\$1,000,001 to HK\$1,500,000	—	1
HK\$1,500,001 to HK\$2,000,000	—	1
	<hr/> 5 <hr/>	<hr/> 5 <hr/>

11. NET LOSS FOR THE YEAR

Of the Group's net loss for the year of HK\$45,859,000 (2000: HK\$44,875,000), a net loss of HK\$70,560,000 (2000: HK\$56,318,000) has been dealt with in the financial statements of the Company.

NOTES TO THE FINANCIAL STATEMENTS

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12. LOSS PER SHARE

The calculation of the basic loss per share is based on the net loss for the year of HK\$45,859,000 (2000: HK\$44,875,000) and on the weighted average number of 615,213,726 shares (2000: 443,577,978 shares) in issue during the year.

No diluted loss per share figures have been presented as the effect of the potential ordinary shares outstanding during these two years would be anti-dilutive.

13. RESEARCH AND DEVELOPMENT COSTS

The Group

	2001 <i>HK\$'000</i>	2000 <i>HK\$'000</i>
Cost		
At 1 January and 31 December	<u>9,464</u>	<u>9,464</u>
Accumulated amortization		
At 1 January	5,804	4,298
Amortization for the year	<u>928</u>	<u>1,506</u>
At 31 December	<u>6,732</u>	<u>5,804</u>
Net book value		
At 31 December	<u><u>2,732</u></u>	<u><u>3,660</u></u>

NOTES TO THE FINANCIAL STATEMENTS

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14. PROPERTY, PLANT AND EQUIPMENT

The Group

	Leasehold land and buildings	Furniture, fixtures and equipment	Moulds	Leasehold improvements	Motor vehicles	Plant and machinery	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Cost							
At 1/1/2001	100,606	11,896	27,137	8,219	1,939	40,723	190,520
Additions	1,855	615	3,321	44	324	285	6,444
Disposals	(10,533)	—	—	—	(341)	—	(10,894)
Provision for impairment loss	(2,500)	—	—	—	—	—	(2,500)
At 31/12/2001	89,408	12,511	30,458	8,263	1,922	41,008	188,570
Accumulated depreciation							
At 1/1/2001	8,478	8,324	22,831	7,799	1,838	35,165	84,435
Charge	2,163	1,491	2,281	246	119	2,370	8,670
Written back	(316)	—	—	—	(341)	—	(657)
At 31/12/2001	10,325	9,815	25,112	8,045	1,616	37,535	92,448
Net book value							
At 31/12/2001	79,083	2,696	5,346	218	306	3,473	91,122
At 31/12/2000	92,128	3,572	4,306	420	101	5,558	106,085

NOTES TO THE FINANCIAL STATEMENTS

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14. PROPERTY, PLANT AND EQUIPMENT *(Continued)*

The Company

	Furniture, fixtures and equipment <i>HK\$'000</i>
Cost	
At 1/1/2001 and 31/12/2001	38
Accumulated depreciation	
At 1/1/2001 and 31/12/2001	38
Net book value	
At 31/12/2001 and 31/12/2000	—

Notes:

- (a) The Group's interests in leasehold land and buildings at their net book values are analysed as follows:

	2001 <i>HK\$'000</i>	2000 <i>HK\$'000</i>
Outside Hong Kong, held on: Leases of between 10 to 50 years	79,083	92,128
(b) At 31 December 2001, the carrying amount of property, plant and equipment held by the Group under finance leases and hire purchase contract amounted to HK\$229,000 (2000: HK\$2,320,000).		

15. INTERESTS IN SUBSIDIARIES

	The Company	
	2001 <i>HK\$'000</i>	2000 <i>HK\$'000</i>
Unlisted shares	40,275	40,275
Amounts due from subsidiaries	158,750	164,517
Provision on amounts due from subsidiaries	(127,000)	(56,318)
	72,025	148,474

NOTES TO THE FINANCIAL STATEMENTS

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15. INTERESTS IN SUBSIDIARIES (Continued)

Notes:

- (a) The carrying value of the unlisted shares is based on the book values of the underlying net assets of the subsidiaries attributable to the Group as at the date of which the Company became the holding company of the Group under the group reorganisation in 1994, less dividends distributed from pre-reorganisation reserve to the subsidiaries.
- (b) The amounts due from subsidiaries are unsecured, non-interest bearing and have no fixed terms of repayment.
- (c) Details of the Company's principal subsidiaries at 31 December 2001, all of which are held indirectly by the Company except Rockapetta Investment Limited, are as follows:

Name	Place of incorporation or registration/ operations	Attributable equity interest of the Group		Nominal value of issued ordinary share capital/ registered capital	Principal activities
		2001	2000		
Rockapetta Investment Limited	British Virgin Islands/ Hong Kong	100%	100%	US\$10,000	Investment holding
Rockapetta International Limited	British Virgin Islands/ Hong Kong	100%	100%	US\$1	Sale and distribution of plastic toys
Rockapetta Industrial Company Limited	Hong Kong	100%	100%	HK\$1,200,000	Sale and distribution of plastic toys
Rockapetta Toys Limited	Hong Kong	100%	100%	HK\$2	Inactive
Rockapetta Toys Manufacturing Company Limited	Hong Kong	100%	100%	HK\$1,000,000	Sale and distribution of plastic toys
Grand Extend Investments Limited	Hong Kong	100%	100%	HK\$10	Inactive
Mitsuyo Seiki (H.K.) Company Limited	Hong Kong	100%	100%	HK\$2	Manufacture and sale of musical movements and components
Shenzhen Rockapetta Toys Company Limited (Note)	PRC	100%	100%	US\$7,530,000	Manufacture and sale of plastic toys
Rockasport Limited	British Virgin Islands/ Hong Kong	100%	—	US\$10	Sales and distribution of plastic toys

Note: Shenzhen Rockapetta Toys Company Limited was established in the People's Republic of China ("PRC") under a joint venture agreement with a PRC party. Under a separate agreement, the Group is responsible for managing the operations and production facilities. The Group is responsible for its assets and liabilities and is entitled to share 100% of its results after the payment of a fixed amount of management fee to the PRC party each year during the term of the joint venture.

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16. INTERESTS IN ASSOCIATES

The Group

	2001 HK\$'000	2000 HK\$'000
Share of net assets	<u>1,530</u>	<u>1,540</u>

Notes:

- (a) At 31 December 2001, the Group has not paid up its share of the capital of an associate which is represented by the amount due to an associate amounting to HK\$2,168,000 (2000: HK\$2,168,000).
- (b) Particulars of the associates at 31 December 2001 are as follows:

Name	Business structure	Place of operation	Place of incorporation	Principal activities	Percentage of interest in ownership
Sanyu (B.V.I.) Limited	Incorporated	Hong Kong	British Virgin Islands	Investment holding	40%
Sanyu Engineering Company Limited	Incorporated	Hong Kong	Hong Kong	Inactive	40%

17. INVENTORIES

	The Group	
	2001 HK\$'000	2000 HK\$'000
Raw materials	12,237	28,044
Work in progress	3,312	11,145
Finished goods	9,830	21,071
	<u>25,379</u>	<u>60,260</u>

At 31 December 2001, the carrying amount of inventories that are carried at net realizable value amounted to HK\$11,854,000 (2000: HK\$8,927,000).

NOTES TO THE FINANCIAL STATEMENTS

31 December 2001

18. TRADE RECEIVABLES, PREPAYMENTS, DEPOSITS AND OTHER RECEIVABLES

Included in trade receivables, prepayments, deposits and other receivables are trade receivables of HK\$13,148,000 (2000: HK\$14,122,000). The Group allows an average credit period of 60 days to trade customers. The aged analysis of trade receivables is as follows:

	The Group	
	2001 HK\$'000	2000 HK\$'000
Aged:		
0 to 60 days	4,206	3,658
61 to 90 days	1,222	3,774
91 to 120 days	100	4,530
More than 120 days	7,620	2,160
	<u>13,148</u>	<u>14,122</u>

19. BORROWINGS

The Group

	Interest-bearing		Non interest-bearing	
	2001 HK\$'000	2000 HK\$'000	2001 HK\$'000	2000 HK\$'000
Loans				
Unsecured	44,500	44,500	—	—
Secured	19,973	28,349	639	—
	<u>64,473</u>	<u>72,849</u>	<u>639</u>	<u>—</u>
The analysis of the above balances is as follows:				
Bank borrowings	19,973	28,349	—	—
Loans from a director	—	44,500	—	—
Other loans	44,500	—	639	—
	<u>64,473</u>	<u>72,849</u>	<u>639</u>	<u>—</u>

Notes:

- (a) The bank borrowings are repayable within one year.
- (b) The loans from a director are reclassified as other loans since the lender resigned as director during the year. The loans are unsecured, bear interest at prime rate and have no fixed term of repayment.

NOTES TO THE FINANCIAL STATEMENTS

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20. OBLIGATIONS UNDER FINANCE LEASES AND HIRE PURCHASE CONTRACTS

Analysis of the capital elements due under finance leases and hire purchase contracts are as follows:

The Group

	2001	2000
	HK\$'000	HK\$'000
Repayable:		
within one year	—	494
in the second to fifth years inclusive	151	—
Current portion of obligations under finance leases and hire purchase contracts	(67)	(494)
	84	—

21. TRADE PAYABLES, OTHER PAYABLES AND ACCRUALS

Included in trade payables, other payables and accruals are trade payables of HK\$26,315,000 (2000: HK\$20,766,000). The aged analysis of trade creditors is as follows:

	The Group	
	2001	2000
	HK\$'000	HK\$'000
Aged:		
0 to 60 days	16,309	7,415
61 to 90 days	3,178	6,678
91 to 120 days	2,985	4,352
More than 120 days	3,843	2,321
	26,315	20,766

22. DUE TO SUBSIDIARIES

The amounts are unsecured, interest free and repayable on demand.

23. OTHER PAYABLE

The amount is unsecured, interest free and repayable after one year.

NOTES TO THE FINANCIAL STATEMENTS

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24. CONVERTIBLE NOTES

Convertible notes of HK\$13,200,000 were issued on 22 June 2000. The convertible notes are unsecured, interest free and are repayable on the second anniversary of the issue date. The noteholders have the rights to convert all or part of the principal amount of the convertible notes outstanding into shares of the Company of HK\$0.10 each at an initial conversion price of HK\$0.22 per share, within two years of the issue of the convertible notes.

In July 2001, the remaining convertible notes with a nominal value of HK\$6,600,000 were converted into shares of the Company at a conversion price of HK\$0.22 per share resulting in the issue of 30,000,000 shares of HK\$0.10 each of the Company.

25. DEFERRED TAXATION

	The Group		The Company	
	2001 HK\$'000	2000 HK\$'000	2001 HK\$'000	2000 HK\$'000
The potential deferred tax asset not provided for in the accounts amount to:				
Accelerated depreciation allowances	672	739	—	1
Tax losses	9,050	8,488	618	671
	9,722	9,227	618	672

At the balance sheet date, there was no material unprovided deferred tax liabilities. Deferred tax assets arising from tax losses has not been recognised as it is uncertain that such an asset will be crystallised in the foreseeable future. At the balance sheet date, the amount of deferred tax asset of the Group and the Company in respect of tax losses not recognised in the financial statements amounted to HK\$9,050,000 (2000: HK\$8,488,000) and HK\$618,000 (2000: HK\$671,000) respectively.

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26. SHARE CAPITAL

	Number of shares	Value
	<i>000</i>	<i>HK\$'000</i>
Ordinary shares of HK\$0.10 each:		
Authorised:		
At 1/1/2001 and 31/12/2001	<u>5,000,000</u>	<u>500,000</u>
Issued and fully paid:		
At 1/1/2001	559,760	55,976
Issued of shares upon subscription (note a)	111,000	11,100
Exercise of options	11,540	1,154
Exercise of conversion right of convertible notes (note b)	<u>30,000</u>	<u>3,000</u>
At 31/12/2001	<u>712,300</u>	<u>71,230</u>

Notes:

- (a) On 29 August 2001, the Company allotted and issued 111,000,000 ordinary shares of HK\$0.10 each in the share capital of the Company at a price of HK\$0.15 per share. The proceeds were used as general working capital for the day to day operations of the Group. These shares rank pari passu with other shares in issue in all respects.
- (b) In July 2001, the Company allotted an aggregate of 30,000,000 new shares of HK\$0.10 each at HK\$0.22 per share as a result of the exercise of conversion rights of convertible notes as detailed in note 24. These shares rank pari passu with other shares in issue in all respects.

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27. SHARE OPTIONS

Under the Company's share option scheme, the directors may at their discretion grant options to employees of the Group, including directors in full time employment with the Company and its subsidiaries, to subscribe for shares in the Company. The subscription price of the option shares shall be a price to be determined by the directors being not less than 80% of the average of the closing prices of the Company's shares on the Stock Exchange for the five trading days immediately preceding the date of offer of the option or the nominal value of a share, whichever is higher. The maximum number of shares in respect of which options may be granted under the share option scheme shall not exceed 10% of the issued share capital of the Company from time to time. The movement in the number of share options during the period and the balance outstanding at 31 December 2001 are as follows:

Exercise price	Number of share options				
	At 1/1/2001	Lapsed/ cancelled during the year	Granted during the year	Exercised during the year	At 31/12/2001
HK\$0.62 per share	2,260,000	2,260,000	—	—	—
HK\$0.61 per share	600,000	600,000	—	—	—
HK\$0.17 per share	11,600,000	11,600,000	11,600,000	11,540,000	60,000
	<u>14,460,000</u>	<u>14,460,000</u>	<u>11,600,000</u>	<u>11,540,000</u>	<u>60,000</u>

During the year ended 31 December 2001, no consideration was received from the granting of share options.

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28. RESERVES

The Group

	Share premium	Contributed surplus	Capital reserve	Deficit	Total
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
At 1/1/2000	42,247	—	2,099	(14,155)	30,191
Premium arising from exercise of options	365	—	—	—	365
Shares issue expenses	(1,627)	—	—	—	(1,627)
Premium arising from issue of shares upon subscription	43,399	—	—	—	43,399
Premium arising from exercising conversion right of convertible notes	3,600	—	—	—	3,600
Net loss for the year	—	—	—	(44,875)	(44,875)
At 31/12/2000	87,984	—	2,099	(59,030)	31,053
Premium arising from exercise of options	808	—	—	—	808
Shares issue expenses	(54)	—	—	—	(54)
Premium arising from issue of shares upon subscription	5,550	—	—	—	5,550
Premium arising from exercising conversion right of convertible notes	3,600	—	—	—	3,600
Net loss for the year	—	—	—	(45,859)	(45,859)
At 31/12/2001	<u>97,888</u>	<u>—</u>	<u>2,099</u>	<u>(104,889)</u>	<u>(4,902)</u>

NOTES TO THE FINANCIAL STATEMENTS

31 December 2001

28. RESERVES (Continued)

The Company

	Share premium <i>HK\$'000</i>	Contributed surplus <i>HK\$'000</i>	Capital reserve <i>HK\$'000</i>	Deficit <i>HK\$'000</i>	Total <i>HK\$'000</i>
At 1/1/2000	42,247	50,492	—	(2,539)	90,200
Premium arising from exercise of options	365	—	—	—	365
Shares issue expenses	(1,627)	—	—	—	(1,627)
Premium arising from issue of shares upon subscription	43,399	—	—	—	43,399
Premium arising from exercising conversion right of convertible notes	3,600	—	—	—	3,600
Net loss for the year	—	—	—	(56,318)	(56,318)
At 31/12/2000	87,984	50,492	—	(58,857)	79,619
Premium arising from exercise of options	808	—	—	—	808
Shares issue expenses	(54)	—	—	—	(54)
Premium arising from issue of shares upon subscription	5,550	—	—	—	5,550
Premium arising from exercising conversion right of convertible notes	3,600	—	—	—	3,600
Net loss for the year	—	—	—	(70,560)	(70,560)
At 31/12/2001	<u>97,888</u>	<u>50,492</u>	<u>—</u>	<u>(129,417)</u>	<u>18,963</u>

NOTES TO THE FINANCIAL STATEMENTS

31 December 2001

28. RESERVES *(Continued)*

Notes:

- (a) The contribution surplus of the Company represents the difference between the underlying net tangible assets of the subsidiaries which were acquired by the Company and the nominal value of the share capital issued by the Company to acquire the assets.

Under the Companies Act 1981 of Bermuda (as amended), the contributed surplus of the Company is available for distribution. However, the Company cannot declare or pay a dividend, or make a distribution out of contributed surplus if:

- (i) it is, or would after the payment be, unable to pay its liabilities as they become due; or
 - (ii) the realisable value of its assets would thereby be less than the aggregate of its liabilities and its issued share capital and share premium accounts.
- (b) The capital reserve arising from the group reorganisation represents the difference between the nominal value of the share capital issued by the Company in exchange for the aggregate nominal values of the share capital of the subsidiaries.

The Company has no reserves available for distribution to shareholders.

NOTES TO THE FINANCIAL STATEMENTS

31 December 2001

29. NOTES TO CONSOLIDATED CASH FLOW STATEMENT

(a) Reconciliation of loss before taxation to net cash inflow/(outflow) from operating activities

	2001	2000
	HK\$'000	HK\$'000
Loss before taxation	(45,850)	(44,876)
Share of losses of associates	10	156
Amortization of research and development costs	928	1,506
Provision for impairment loss of property, plant and equipment	2,500	8,000
Provision for slow moving inventories	10,743	9,899
Provision for doubtful debts	2,625	3,625
Bad debts written off	1,307	615
Depreciation	8,670	10,648
Gain on disposal of property, plant and equipment	(109)	—
Interest income	(150)	(891)
Interest expenses	5,541	5,418
Interest expenses on obligations under finance leases and hire purchase contracts	103	280
Increase in amounts due from an associate	(18)	(68)
Decrease/(increase) in inventories	24,138	(3,015)
(Increase)/decrease in trade receivables, prepayments, deposits and other receivables	(6,341)	1,060
Increase/(decrease) in trade payables, other payables and accruals	8,121	(4,376)
Decrease in other payables	(4,662)	—
(Decrease)/increase in amounts due to Directors	(2,444)	622
	<hr/>	<hr/>
Net cash inflow/(outflow) from operating activities	5,112	(11,397)
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NOTES TO THE FINANCIAL STATEMENTS

31 December 2001

29. NOTES TO CONSOLIDATED CASH FLOW STATEMENT (Continued)

(b) Analysis of changes in financing during the year

	Share capital and share premium <i>HK\$'000</i>	Loans from a director <i>HK\$'000</i>	Amount due to a director <i>HK\$'000</i>	Trust receipt loans <i>HK\$'000</i>	Bank loans <i>HK\$'000</i>	Obligations under finance leases and hire purchase contracts <i>HK\$'000</i>	Convertible notes <i>HK\$'000</i>	Other loan <i>HK\$'000</i>
Balance at 1/1/2000	71,257	83,000	2,320	857	28,552	2,411	—	—
Proceeds from issue of shares upon subscription and exercise of options	67,730	—	—	—	—	—	—	—
Shares issue expenses	(1,627)	—	—	—	—	—	—	—
New borrowings	—	—	622	55,301	—	—	13,200	—
Repayments	—	(38,500)	—	(53,657)	(4,699)	(1,917)	—	—
Proceeds from issue of shares upon exercise of conversion right of convertible notes	6,600	—	—	—	—	—	(6,600)	—
Balance at 31/12/2000	143,960	44,500	2,942	2,501	23,853	494	6,600	—
Proceeds from issue of shares upon subscription and exercise of options	18,612	—	—	—	—	—	—	—
Shares issue expenses	(54)	—	—	—	—	—	—	—
New borrowings	—	—	498	—	8,000	201	—	639
Repayments	—	—	—	(2,501)	(11,880)	(544)	—	—
Proceeds from issue of shares upon exercise of conversion right of convertible notes	6,600	—	—	—	—	—	(6,600)	—
Reclassification due to resignation of director	—	(44,500)	(2,942)	—	—	—	—	44,500
Balance at 31/12/2001	169,118	—	498	—	19,973	151	—	45,319

NOTES TO THE FINANCIAL STATEMENTS

31 December 2001

30. RELATED PARTY TRANSACTIONS

During the year, the Group sold its products to one related party (2000: two related parties) for an aggregate amount of HK\$2,348,000 (2000: HK\$16,715,000). The parties concerned are related to the Company since they are enterprises controlled by a shareholder of the Company. The transactions were carried out on cost plus mark up basis.

Total loans from Mr. Kwok Chin Wing, who retired as director on 11 April 2001, outstanding as at 31 December 2001 amounted to HK\$44,500,000 (2000: HK\$44,500,000). The loans bear interest at prime rate. Interest amounting to HK\$Nil (2000: HK\$3,167,000) was waived by the director, accordingly interest payable by the Group on the loans for the period of which Mr. Kwok Chin Wing was a director amounted to HK\$1,033,253 (2000: HK\$2,451,000).

The amount due from an associate and the amount due to a director are unsecured, non-interest bearing and have no fixed terms of repayment.

31. CONTINGENT LIABILITIES

	The Group		The Company	
	2001 HK\$'000	2000 HK\$'000	2001 HK\$'000	2000 HK\$'000
Guarantees given to banks in respect of banking facilities utilised by subsidiaries	—	—	—	6,674

NOTES TO THE FINANCIAL STATEMENTS

31 December 2001

32. COMMITMENTS

(a) Capital commitments

	The Group	
	2001	2000
	HK\$'000	HK\$'000
Contracted but not provided for acquisition of		
— furniture, fixtures and equipment	—	97
— land and buildings	—	190
	<u>—</u>	<u>287</u>
Authorised but not contracted for acquisition of		
— land and buildings	<u>—</u>	<u>212</u>

The Company did not have any capital commitments at the balance sheet date.

(b) Commitment under operating leases

At 31 December 2001, the Group had commitments to make payment in the next twelve months under operating leases which expire as follows:

	Other properties	
	2001	2000
	HK\$'000	HK\$'000
Within one year	—	237
In the second to fifth years inclusive	<u>1,465</u>	<u>1,394</u>
	<u><u>1,465</u></u>	<u><u>1,631</u></u>

The Company did not have any operating leases commitments at the balance sheet date.

33. CHARGES ON ASSETS

- (a) Certain of the Group's bank deposits with carrying amount of HK\$2,579,000 (2000: HK\$8,267,000) have been pledged to banks to secure banking facilities granted a subsidiary.
- (b) Certain of the Group's leasehold land and buildings with carrying amount of HK\$79,083,000 (2000: HK\$82,053,000) have been pledged to banks to secure bank loans granted to a subsidiary.