# Notes to the Financial Statements

(Expressed in Hong Kong dollars unless otherwise indicated)

## 1 SIGNIFICANT ACCOUNTING POLICIES

### (a) Statement of compliance

These financial statements have been prepared in accordance with all applicable Hong Kong Financial Reporting Standards ("HKFRSs"), which collective term includes all applicable individual Hong Kong Financial Reporting Standards, Hong Kong Accounting Standards ("HKASs") and Interpretations issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA"), accounting principles generally accepted in Hong Kong and the disclosure requirements of the Hong Kong Companies Ordinance. These financial statements also comply with the applicable disclosure provisions of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited. A summary of the significant accounting policies adopted by the Group is set out below.

The HKICPA has issued certain new and revised HKFRSs that are first effective or available for early adoption for current accounting period of the Group and the Company. Note 2 provides information on the changes in accounting policies resulting from initial application of these developments to the extent that they are relevant to the Group for the current and prior accounting periods reflected in these financial statements.

### (b) Basis of preparation of the financial statements

The consolidated financial statements for the year ended 31 December 2006 comprise the Company and its subsidiaries (together referred to as the "Group").

The measurement basis used in the preparation of the financial statements is the historical cost basis except that available-for-sale securities and trading securities are stated at their fair value as explained in note 1(d).

The preparation of financial statements in conformity with HKFRSs requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets, liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

Judgements made by management in the application of HKFRSs that have significant effect on the financial statements and estimates with a significant risk of material adjustment in the next year relating to fixed assets, goodwill and available-for-sale securities have been discussed in notes 12, 14 and 16.

## 1 SIGNIFICANT ACCOUNTING POLICIES (continued)

### (c) Interest in subsidiaries and controlled entities

Subsidiaries are entities controlled by the Group. Control exists when the Group has the power, to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In accessing control, potential voting rights that presently are exercisable are taken into account.

An investment in a subsidiary is consolidated into the consolidated financial statements from the date that control commences until the date that control ceases.

Intra-group balances and transactions and any unrealised profits arising from intra-group transactions are eliminated in full in preparing the consolidated financial statements. Unrealised losses resulting from intra-group transactions are eliminated in the same way as unrealised gains but only to the extent that there is no evidence of impairment.

Minority interests represent the portion of the net assets of subsidiaries attributable to interests that are not owned by the Company, whether directly or indirectly through subsidiaries, and in respect of which the Group has not agreed any additional terms with the holders of those interests which would result in the Group as a whole having a contractual obligation in respect of those interests that meets the definition of a financial liability. Minority interests are presented in the consolidated balance sheet and statement of changes in equity within equity, separately from equity attributable to the equity shareholders of the Company. Minority interests in the results of the Group are presented on the face of the consolidated income statement as an allocation of the total profit or loss for the year between minority interests and the equity shareholders of the Company.

Where losses applicable to the minority exceed the minority's interest in the equity of a subsidiary, the excess, and any further losses applicable to the minority, are charged against the Group's interest except to the extent that the minority has a binding obligation to, and is able to, make additional investment to cover the losses. If the subsidiary subsequently reports profits, the Group's interest is allocated all such profits until the minority's share of losses previously absorbed by the Group has been recovered.

In the Company's balance sheet, an investment in a subsidiary is stated at cost less impairment losses (see note 1(g)), unless the investment is classified as held for sale, in which case it is stated at the lower of its carrying amount and fair value less costs to sell. An investment in a subsidiary is classified as held for sale if it is highly probable that its carrying amount will be recovered through a sale transaction rather than through continuing use and the investment is available for sale in its present condition.

## 1 SIGNIFICANT ACCOUNTING POLICIES (continued)

### (d) Other investments in debt and equity securities

The Group's policies for investments in debt and equity securities, other than investments in subsidiaries, are as follows:

Investments in securities held for trading are classified as current assets and are initially stated at fair value. At each balance sheet date the fair value is remeasured, with any resultant gain or loss being recognised in profit or loss.

Investments in equity securities that do not have a quoted market price in an active market and whose fair value cannot be reliably measured are recognised in the balance sheet at cost less impairment losses (see note 1(g)).

Other investments in securities are classified as available-for-sale securities and are initially recognised at fair value plus transaction costs. At each balance sheet date the fair value is remeasured, with any resultant gain or loss being recognised directly in equity, except for impairment losses (see note 1(g)) and, in the case of monetary items such as debt securities, foreign exchange gains and losses which are recognised directly in profit or loss. Where these investments are interest-bearing, interest calculated using the effective interest method is recognised in profit or loss. When these investments are derecognised, the cumulative gain or loss previously recognised directly in equity is recognised in profit or loss.

Investments are recognised/derecognised on the date the Group commits to purchase/sell the investments or they expire.

### (e) Investment properties and other property, plant and equipment

Investment properties are land and/or buildings which are owned or held under a leasehold interest (see note 1(f)) to earn rental income, or for capital appreciation or for a currently undetermined future use.

Both investment properties and other items of property, plant and equipment are stated in the balance sheet at cost less accumulated depreciation/amortisation and impairment losses (see note 1(g)).

When the Group holds a property interest held under an operating lease to earn rental income and/or for capital appreciation, the interest is classified and accounted for as an investment property on a property-by-property basis. Any such property interest which has been classified as an investment property is accounted for as if it were held under a finance lease, and the same accounting policies are applied to that interest as are applied to other investment properties leased under finance leases. Lease payments are accounted for as described in note 1(f)).

Depreciation is calculated to write off the cost of items of investment properties and property, plant and equipment, using the straight line method over their estimated useful lives as follows:

| | |
|---|---|
| – Investment properties | 33 years |
| – Leasehold land | Over the lease term |
| – Buildings | 40 years |
| – Plant and machinery | 2 to 7 years |
| – Tools and equipment | 2 to 5 years |
| – Others | 2 to 5 years |

## 1 SIGNIFICANT ACCOUNTING POLICIES (continued)

### (e) Investment properties and other property, plant and equipment (continued)

The useful life of an asset is reviewed annually.

Gains or losses arising from the retirement or disposal of an investment property or an item of property, plant and equipment are determined as the difference between the net disposal proceeds and the carrying amount of the asset and are recognised in profit or loss on the date of retirement or disposal.

### (f) Leased assets

An arrangement, comprising a transaction or a series of transactions, is or contains a lease if the Group determines that the arrangement conveys a right to use a specific asset or assets for an agreed period of time in return for a payment or a series of payments. Such a determination is made based on an evaluation of the substance of the arrangement and is regardless of whether the arrangement takes the legal form of a lease.

*(i) Classification of assets leased to the Group*

Assets that are held by the Group under leases which transfer to the Group substantially all the risks and rewards of ownership are classified as being held under finance leases. Leases which do not transfer substantially all the risks and rewards of ownership to the Group are classified as operating leases, with the following exceptions:

– property held under operating leases that would otherwise meet the definition of an investment property is classified as an investment property on a property-by-property basis and, if classified as investment property, is accounted for as if held under a finance lease; and

– land held for own use under an operating lease, the fair value of which cannot be measured separately from the fair value of a building situated thereon at the inception of the lease, is accounted for as being held under a finance lease, unless the building is also clearly held under an operating lease. For these purposes, the inception of the lease is the time that the lease was first entered into by the Group, or taken over from the previous lessee.

*(ii) Operating lease charges*

Where the Group has the use of assets held under operating leases, payments made under the leases are charged to profit or loss in equal instalments over the accounting periods covered by the lease term, except where an alternative basis is more representative of the pattern of benefits to be derived from the leased asset. Lease incentives received are recognised in profit or loss as an integral part of the aggregate net lease payments made. Contingent rentals are charged to profit or loss in the accounting period in which they are incurred.

The cost of acquiring land held under an operating lease is amortised on a straight-line basis over the period of the lease term except where the property is classified as an investment property (see note 1(e)).

## 1 SIGNIFICANT ACCOUNTING POLICIES (continued)

### (g) Impairment of assets

*(i) Impairment of investments in debt and equity securities and other receivables*

Investments in debt and equity securities and other current and non-current receivables that are stated at cost or amortised cost or are classified as available-for-sale securities are reviewed at each balance sheet date to determine whether there is objective evidence of impairment. If any such evidence exists, any impairment loss is determined and recognised as follows:

– For unquoted equity securities and current receivables that are carried at cost, the impairment loss is measured as the difference between the carrying amount of the financial asset and the estimated future cash flows, discounted at the current market rate of return for a similar financial asset where the effect of discounting is material. Impairment losses for current receivables are reversed if in a subsequent period the amount of the impairment loss decreases. Impairment losses for equity securities are not reversed.

– For financial assets carried at amortised cost, the impairment loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the financial asset's original effective interest rate (i.e. the effective interest rate computed at initial recognition of these assets).

  If in a subsequent period the amount of an impairment loss decreases and the decrease can be linked objectively to an event occurring after the impairment loss was recognised, the impairment loss is reversed through profit or loss. A reversal of an impairment loss shall not result in the asset's carrying amount exceeding that which would have been determined had no impairment loss been recognised in prior years.

– For available-for-sale securities, the cumulative loss that had been recognised directly in equity is removed from equity and is recognised in profit or loss. The amount of the cumulative loss that is recognised in profit or loss is the difference between the acquisition cost (net of any principal repayment and amortisation) and current fair value, less any impairment loss on that asset previously recognised in profit or loss.

  Impairment losses recognised in profit or loss in respect of available-for-sale equity securities are not reversed through profit or loss. Any subsequent increase in the fair value of such assets is recognised directly in equity.

## 1 SIGNIFICANT ACCOUNTING POLICIES (continued)

### (g) Impairment of assets (continued)

*(ii) Impairment of other assets*

Internal and external sources of information are reviewed at each balance sheet date to identify indications that the following assets may be impaired or, except in the case of goodwill, an impairment loss previously recognised no longer exists or may have decreased:

– investments in subsidiaries; and

– fixed assets.

If any such indication exists, the asset's recoverable amount is estimated. In addition, for goodwill, the recoverable amount is estimated annually whether or not there is any indication of impairment.

– Calculation of recoverable amount

The recoverable amount of an asset is the greater of its net selling price and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of time value of money and the risks specific to the asset. Where an asset does not generate cash inflows largely independent of those from other assets, the recoverable amount is determined for the smallest group of assets that generates cash inflows independently (i.e. a cash-generating unit).

– Recognition of impairment losses

An impairment loss is recognised in profit or loss whenever the carrying amount of an asset, or the cash-generating unit to which it belongs, exceeds its recoverable amount. Impairment losses recognised in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to the cash-generating unit (or group of units) and then, to reduce the carrying amount of the other assets in the unit (or group of units) on a pro rata basis, except that the carrying value of an asset will not be reduced below its individual fair value less costs to sell, or value in use, if determinable.

– Reversals of impairment losses

In respect of assets other than goodwill, an impairment loss is reversed if there has been a favourable change in the estimates used to determine the recoverable amount. An impairment loss in respect of goodwill is not reversed.

A reversal of impairment losses is limited to the asset's carrying amount that would have been determined had no impairment loss been recognised in prior years. Reversals of impairment losses are credited to profit or loss in the year in which the reversals are recognised.

## 1 SIGNIFICANT ACCOUNTING POLICIES (continued)

### (g) Impairment of assets (continued)

*(iii) Interim financial reporting and impairment*

Under the Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong Limited, the Group is required to prepare an interim financial report in compliance with HKAS 34, Interim financial reporting, in respect of the first six months of the financial year. At the end of the interim period, the Group applies the same impairment testing, recognition, and reversal criteria as it would at the end of the financial year (see notes 1(g)(i) and (ii)).

Impairment losses recognised in an interim period in respect of goodwill, available-for-sale equity securities and unquoted equity securities carried at cost are not reversed in a subsequent period. This is the case even if no loss, or a smaller loss, would have been recognised had the impairment been assessed only at the end of the financial year to which the interim period relates.

### (h) Trade and other receivables

Trade and other receivables are initially recognised at fair value and thereafter stated at amortised cost less impairment losses for bad and doubtful debt (see note 1(g)), except where the effect of discounting would be immaterial. In such cases, the receivables are stated at cost less impairment losses for bad and doubtful debts.

### (i) Trade and other payables

Trade and other payables are initially recognised at fair value and thereafter stated at amortised cost unless the effect of discounting would be immaterial, in which case they are stated at cost.

### (j) Inventories

Inventories are carried at the lower of cost and net realisable value.

Cost is calculated using the first-in first-out method and comprises all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition.

Net realisable 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.

When inventories are sold, the carrying amount of those inventories is recognised as an expense in the period in which the related revenue is recognised. The amount of any write-down of inventories to net realisable value and all losses of inventories are recognised as an expense in the period in which the write-down or loss occurs. The amount of any reversal of any write-down of inventories is recognised as a reduction in the amount of inventories recognised as an expense in the period in which the reversal occurs.

### (k) Cash and cash equivalents

Cash and cash equivalents comprise cash at bank and on hand, demand deposits with banks and other financial institutions, and short-term, highly liquid investments that are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value, having been within three months of maturity at acquisition. Bank overdrafts that are repayable on demand and form an integral part of the Group's cash management are also included as a component of cash and cash equivalents for the purpose of the cash flow statement.

## 1 SIGNIFICANT ACCOUNTING POLICIES (continued)

### (l) Revenue recognition

Provided it is probable that the economic benefits will flow to the Group and the revenue and costs, if applicable, can be measured reliably, revenue is recognised in profit or loss as follows:

(i) Revenue arising from the sale of goods is recognised on delivery of goods to customers which is taken to be the point in time when the customer has accepted the goods and the related risks and rewards of ownership. Revenue excludes value added or other sales taxes and is after deduction of returns and any trade discounts.

(ii) Interest income is recognised as it accrues using the effective interest method.

(iii) Income from other securities is recognised when the Group's right to receive such income is established.

### (m) Employee benefits

*(i) Short term employee benefits and contributions to defined contribution retirement plans*

Salaries, annual bonuses, paid annual leave and the cost to the Group of non-monetary benefits are accrued in the year in which the associated services are rendered by employees of the Group. Where payment or settlement is deferred and the effect would be material, these amounts are stated at their present values.

Contributions to defined contribution plans and Mandatory Provident Funds as required under the Hong Kong Mandatory Provident Fund Schemes Ordinance are recognised in profit or loss as incurred.

*(ii) Share based payments*

The fair value of share options granted to employees is recognised as an employee cost with a corresponding increase in a capital reserve within equity. The fair value is measured at grant date using the Black-Scholes model, taking into account the terms and conditions upon which the options were granted. Where the employees have to meet vesting conditions before becoming unconditionally entitled to the share options, the total estimated fair value of the share options is spread over the vesting period, taking into account the probability that the options will vest.

During the vesting period, the number of share options that is expected to vest is reviewed. Any adjustment to the cumulative fair value recognised in prior years is charged/credited to profit or loss for the year of the review, unless the original employee expenses qualify for recognition as an asset, with a corresponding adjustment to the capital reserve. On vesting date, the amount recognised as an expense is adjusted to reflect the actual number of share options that vest (with a corresponding adjustment to the capital reserve) except where forfeiture is only due to not achieving vesting conditions that relate to the market price of the Company's shares. The equity amount is recognised in the capital reserve until either the option is exercised (when it is transferred to the share premium account) or the option expires (when it is released directly to retained profits).

## 1 SIGNIFICANT ACCOUNTING POLICIES (continued)

### (n) Financial guarantees issued, provisions and contingent liabilities

*(i) Financial guarantees issued*

Financial guarantees are contracts that require the issuer (i.e. the guarantor) to make specified payments to reimburse the beneficiary of the guarantee (the "holder") for a loss the holder incurs because a specified debtor fails to make payment when due in accordance with the terms of a debt instrument.

Where the Group issues a financial guarantee, the fair value of the guarantee (being the transaction price, unless the fair value can otherwise be reliably estimated) is initially recognised as deferred income within trade and other payables. Where consideration is received or receivable for the issuance of the guarantee, the consideration is recognised in accordance with the Group's policies applicable to that category of asset. Where no such consideration is received or receivable, an immediate expense is recognised in profit or loss on initial recognition of any deferred income.

The amount of the guarantee initially recognised as deferred income is amortised in profit or loss over the term of the guarantee as income from financial guarantees issued. In addition, provisions are recognised in accordance with note 1(n)(ii) if and when (i) it becomes probable that the holder of the guarantee will call upon the Group under the guarantee, and (ii) the amount of that claim on the Group is expected to exceed the amount currently carried in trade and other payables in respect of that guarantee i.e. the amount initially recognised, less accumulated amortisation.

*(ii) Other provisions and contingent liabilities*

Provisions are recognised for liabilities of uncertain timing or amount when the Group or the Company has a legal or constructive obligation arising as a result of a past event, it is probable that an outflow of economic benefits will be required to settle the obligation and a reliable estimate can be made. Where the time value of money is material, provisions are stated at the present value of the expenditures expected to settle the obligation.

Where it is not probable that an outflow of economic benefits will be required, or the amount cannot be estimated reliably, the obligation is disclosed as a contingent liability, unless the probability of outflow of economic benefits is remote. Possible obligations, whose existence will only be confirmed by the occurrence or non-occurrence of one or more future events are also disclosed as contingent liabilities unless the probability of outflow of economic benefits is remote.

### (o) Income tax

(i) Income tax for the year comprises current tax and movements in deferred tax assets and liabilities. Current tax and movements in deferred tax assets and liabilities are recognised in profit or loss except to the extent that they relate to items recognised directly in equity, in which case they are recognised in equity.

(ii) Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted on substantively enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

## 1 SIGNIFICANT ACCOUNTING POLICIES (continued)

### (o) Income tax (continued)

(iii) Deferred tax assets and liabilities arise from deductible and taxable temporary differences respectively, being the differences between the carrying amounts of assets and liabilities for financial reporting purposes and their tax bases. Deferred tax assets also arise from unused tax losses and unused tax credits. Apart from differences which arise on initial recognition of assets and liabilities, all deferred tax liabilities, and all deferred tax assets to the extent that it is probable that future taxable profits will be available against which the asset can be utilised are recognised.

The amount of deferred tax recognised is measured based on the expected manner of realisation or settlement of the carrying amount of the assets and liabilities, using tax rates enacted or substantively enacted at the balance sheet date. Deferred tax assets and liabilities are not discounted.

The carrying amount of a deferred tax asset is reviewed at each balance sheet date and is reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow the related tax benefit to be utilised. Any such reduction is reversed to the extent that it becomes probable that sufficient taxable profit will be available.

Additional income taxes that arise from the distribution of dividends are recognised when the liability to pay the related dividends is recognised.

(iv) Current tax balances and deferred tax balances, and movements therein, are presented separately from each other and are not offset. Current tax assets are offset against current tax liabilities, and deferred tax assets against deferred tax liabilities, if the Company or the Group has the legally enforceable right to set off current tax assets against current tax liabilities and the following additional conditions are met:

- in the case of current tax assets and liabilities, the Company or the Group intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously; or

- in the case of deferred tax assets and liabilities, if they relate to income taxes levied by the same taxation authority on either:

  - the same taxable entity; or

  - different taxable entities, which, in each future period in which significant amounts of deferred tax liabilities or assets are expected to be settled or recovered, intend to realise the current tax assets and settle the current tax liabilities on a net basis or realise and settle simultaneously.

## 1 SIGNIFICANT ACCOUNTING POLICIES (continued)

### (p) Convertible notes

Convertible notes that can be converted to share capital at the option of the holder, where the number of shares that would be issued on conversion and the value of the consideration that would be received at that time do not vary, are accounted for as compound financial instruments which contain both a liability component and an equity component. At initial recognition the liability component of the convertible notes is measured as the present value of the future interest and principal payments, discounted at the market rate of interest applicable at the time of initial recognition to similar liabilities that do not have a conversion option. Any excess of proceeds over the amount initially recognised as the liability component is recognised as the equity component. Transaction costs that relate to the issue of a compound financial instrument are allocated to the liability and equity components in proportion to the allocation of proceeds.

The liability component is subsequently carried at amortised cost. The interest expense recognised in profit or loss on the liability component is calculated using the effective interest method. The equity component is recognised in the capital reserve until either the note is converted or redeemed.

If the note is converted, the capital reserve, together with the carrying value of the liability component at the time of conversion, is transferred to share capital and share premium as consideration for the shares issued. If the note is redeemed, the capital reserve is released directly to retained profits.

### (q) Translation of foreign currencies

Foreign currency transactions during the year are translated at the foreign exchange rates ruling at the transaction dates. Monetary assets and liabilities denominated in foreign currencies are translated at the foreign exchange rates ruling at the balance sheet date. Exchange gains and losses are recognised in profit or loss, except those arising from foreign currency borrowings used to hedge a net investment in a foreign operation which are recognised directly in equity.

Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the foreign exchange rates ruling at the transaction dates. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are translated using the foreign exchange rates ruling at the dates the fair value was determined.

The results of foreign operations are translated into Hong Kong dollars at the exchange rates approximating the foreign exchange rates ruling at the dates of the transactions. Balance sheet items, including goodwill arising on consolidation of foreign operations acquired on or after 1 January 2005, are translated into Hong Kong dollars at the foreign exchange rates ruling at the balance sheet date. The resulting exchange differences are recognised directly in a separate component of equity. Goodwill arising on consolidation of a foreign operation acquired before 1 January 2005 is translated at the foreign exchange rate that applied at the date of acquisition of the foreign operation.

On disposal of a foreign operation, the cumulative amount of the exchange differences recognised in equity which relate to that foreign operation is included in the calculation of the profit or loss on disposal.

# 1 SIGNIFICANT ACCOUNTING POLICIES (continued)

## (r) Related parties

For the purposes of these financial statements, a party is considered to be related to the Group if:

(i) the party has the ability, directly or indirectly through one or more intermediaries, to control the Group or exercise significant influence over the Group in making financial and operating policy decisions, or has joint control over the Group;

(ii) the Group and the party are subject to common control;

(iii) the party is an associate of the Group or a joint venture in which the Group is a venturer;

(iv) the party is a member of key management personnel of the Group or the Group's parent, or a close family member of such an individual, or is an entity under the control, joint control or significant influence of such individuals;

(v) the party is a close family member of a party referred to in (i) or is an entity under the control, joint control or significant influence of such individuals; or

(vi) the party is a post-employment benefit plan which is for the benefit or employees of the Group or of any entity that is a related party of the Group.

Close family members of an individual are those family members who may be expected to influence, or be influenced by, that individual in their dealings with the entity.

## (s) Segment reporting

A segment is a distinguishable component of the Group that is engaged either in providing products or services (business segment), or in providing products or services within a particular economic environment (geographical segment), which is subject to risks and rewards that are different from those of other segments.

In accordance with the Group's internal financial reporting system, the Group has chosen business segment information as the primary reporting format and geographical segment information as the secondary reporting format for the purposes of these financial statements.

Segment revenue, expenses, results, assets and liabilities include items directly attributable to a segment as well as those that can be allocated on a reasonable basis to that segment. For example, segment assets may include inventories, trade receivables and property, plant and equipment. Segment revenue, expenses, assets and liabilities are determined before intra-group balances and intra-group transactions are eliminated as part of the consolidation process, except to the extent that such intra-group balances and transactions are between Group enterprises within a single segment. Inter-segment pricing is based on similar terms as those available to other external parties.

Segment capital expenditure is the total cost incurred during the period to acquire segment assets (both tangible and intangible) that are expected to be used for more than one period.

Unallocated items mainly comprise financial and corporate assets, interest-bearing loans, borrowings, tax balances, corporate and financing expenses and minority interests.

## 2 CHANGES IN ACCOUNTING POLICIES

The HKICPA has issued a number of new and revised HKFRSs that are first effective or available for early adoption for the current accounting period of the Group.

The accounting policies of the Group and/or the Company after the adoption of these new and revised HKFRSs to the extent that they are relevant to the Group have been summarised in note 1. The following sets out information on the significant changes in accounting policies for the current and prior accounting periods reflected in these financial statements.

The Group has not applied any new standard or interpretation that is not yet effective for the current accounting period (see note 34) except for HK(IFRIC) 10, Interim financial reporting and impairment, which is effective for accounting periods beginning on or after 1 November 2006.

### (a) Financial guarantees issued (Amendments to HKAS 39, Financial instruments: Recognition and measurement: Financial guarantee contracts)

In prior years, financial guarantees issued by the Group were disclosed as contingent liabilities in accordance with HKAS 37, Provisions, contingent liabilities and contingent assets. No provisions were made in respect of these guarantees unless it was more likely than not that the guarantee would be called upon.

With effect from 1 January 2006, in order to comply with the amendments to HKAS 39 in respect of financial guarantee contracts, the Group has changed its accounting policy for financial guarantees issued. Under the new policy, financial guarantees issued are accounted for as financial liabilities under HKAS 39 and measured initially at fair value, where the fair value can be reliably measured. Subsequently, they are measured at the higher of the amount initially recognised, less accumulated amortisation, and the amount of the provision, if any, that should be recognised in accordance with HKAS 37. Further details of the new policy are set out in note 1(n)(i).

The change in accounting policy has no financial effect on the consolidated and Company financial statements. Details of the financial guarantees currently issued by the Company are set out in note 31.

### (b) Reversal of impairment losses on available-for-sale equity securities (HK(IFRIC) 10, Interim financial reporting and impairment)

In prior years, impairment losses on available-for-sale equity securities recognised in the interim period were reversed through profit or loss in a subsequent interim period of the same year if no loss, or a smaller loss, would have been recognised had the impairment been assessed on a year-to-date basis.

In 2006, the Group has early adopted HK(IFRIC) 10. With effect from 1 January 2006, in accordance with HK(IFRIC) 10, the Group has changed its accounting policy relating to the reversal of impairment losses on available-for-sale equity financial instruments recognised in an interim period. Under the new policy, impairments reported in the interim period profit or loss will also be reported in profit or loss for the full financial year which includes that interim period, irrespective of whether conditions have improved at the year-end balance sheet date. Further details of the new policy are set out in note 1(g)(iii).

## 3 TURNOVER

The principal activity of the Company is investment holding. The principal activities of the Group are the design, manufacture and sale of liquid crystal displays and related products.

Turnover represents the invoiced value of goods supplied to customers by the Group less returns and discounts.

## 4 OTHER REVENUE AND NET INCOME

| | **2006** | 2005 |
|---|---|---|
| | **$'000** | $'000 |
| **Other revenue** | | |
| Consultancy fee income | **17,246** | – |
| Dividend income from listed equity securities | **7,526** | 425 |
| Commission income | **5,667** | – |
| Interest income from listed debt securities | **1,648** | 2,367 |
| Interest income from unlisted debt securities | **287** | 1,119 |
| Interest income from unlisted investment funds | **852** | 545 |
| Other interest income | **9,362** | 12,426 |
| Rental income under operating leases | **429** | 367 |
| Other income | **5,951** | 3,409 |
| | **48,968** | 20,658 |
| **Other net income** | | |
| Profit on disposal of fixed assets | **2,276** | 6,573 |
| Transfer from equity on disposal of available-for-sale securities | **28,909** | 70 |
| Realised and unrealised (losses)/gains on trading securities | **(14,508)** | 12,708 |
| Discount on redemption of convertible notes | **3,740** | – |
| Exchange gain/(loss) | **17,113** | (6,885) |
| | **37,530** | 12,466 |

## 5 PROFIT/(LOSS) BEFORE TAXATION

**Profit/(loss) before taxation is arrived at after charging:**

| | | 2006 $'000 | 2005 $'000 |
|---|---|---|---|
| (a) | Finance costs: | | |
| | Interest on bank advances and other borrowings repayable within five years | **3,146** | 4,723 |
| | Interest on convertible notes | **151** | 1,872 |
| | Amortisation of convertible notes | **–** | 190 |
| | | **3,297** | 6,785 |
| (b) | Other items: | | |
| | Cost of inventories | **1,394,137** | 1,478,600 |
| | Auditors' remuneration - audit services | **2,685** | 2,005 |
| | Research and development costs | **22,958** | 21,335 |
| | Rental charges under operating leases | **6,256** | 3,122 |
| | Contributions to defined contribution retirement plan | **4,472** | 6,452 |
| | Other retirement scheme costs | **522** | 1,437 |
| | Amortisation of intangible assets | **–** | 1,622 |
| (c) | Impairment losses: | | |
| | Trade and other receivables | **3,629** | 6,420 |

## 6 DIRECTORS' REMUNERATION

Directors' remuneration disclosed pursuant to section 161 of the Hong Kong Companies Ordinance is as follows:

**Year ended 31 December 2005**

| | **Directors' fees** | **Salaries, allowances and benefits in kind** | **Discretionary bonuses** | **Share-based payments** | **Retirement scheme contributions** | **Total** |
|---|---|---|---|---|---|---|
| | $'000 | $'000 | $'000 | $'000 | $'000 | $'000 |
| *Executive Directors* | | | | | | |
| Dr Chang Chu Cheng | – | 2,054 | 1,460 | 2,886 | 12 | 6,412 |
| Johnson Ko Chun Shun | – | 1,400 | 1,460 | 2,886 | 50 | 5,796 |
| Tony Tsoi Tong Hoo | – | 1,916 | 1,460 | 2,714 | 80 | 6,170 |
| Cecil Ho Te Hwai | – | 209 | 400 | 2,886 | 9 | 3,504 |
| Chung Shun Ming | – | 960 | – | – | 48 | 1,008 |
| Kwok Siu Kwan | – | 960 | – | – | 48 | 1,008 |
| Dr Yan Sze Kwan | – | 960 | – | – | 48 | 1,008 |
| *Non-executive Directors* | | | | | | |
| Dr William Lo Wing Yan | 200 | – | – | – | – | 200 |
| Yuen Kin | 161 | – | – | – | – | 161 |
| Hou Ziqiang | 161 | – | – | – | – | 161 |
| Professor Charles Kao Kuen | 110 | – | – | – | – | 110 |
| Anthony Lui Chi Shing | 110 | – | – | – | – | 110 |
| Total | 742 | 8,459 | 4,780 | 11,372 | 295 | 25,648 |

## 6 DIRECTORS' REMUNERATION (continued)

Directors' remuneration disclosed pursuant to section 161 of the Hong Kong Companies Ordinance is as follows: (continued)

**Year ended 31 December 2006**

| | Directors' fees $'000 | Salaries, allowances and benefits in kind $'000 | Discretionary bonuses $'000 | Retirement scheme contributions $'000 | Total $'000 |
|---|---|---|---|---|---|
| *Executive Directors* | | | | | |
| Dr Chang Chu Cheng | – | 2,054 | 2,000 | 13 | 4,067 |
| Johnson Ko Chun Shun | – | 2,400 | 1,500 | 120 | 4,020 |
| Tony Tsoi Tong Hoo | – | 2,400 | 4,000 | 120 | 6,520 |
| Cecil Ho Te Hwai | – | 240 | 500 | 12 | 752 |
| *Non-executive Directors* | | | | | |
| Dr William Lo Wing Yan | 200 | – | – | – | 200 |
| Yuen Kin | 200 | – | – | – | 200 |
| Hou Ziqiang | 200 | – | – | – | 200 |
| Total | 600 | 7,094 | 8,000 | 265 | 15,959 |

The above emoluments include the estimated value of share options granted to the directors under the Company's share option scheme. The value of these share options is measured according to the Group's accounting policies for share-based payment transactions as set out in note 1(m)(ii). The details of these benefits in kind, including the principal terms and number of options granted, are disclosed under the paragraph "Share Option Scheme" in the director's report and note 25.

## 7 FIVE HIGHEST PAID INDIVIDUALS' REMUNERATION

The five highest paid individuals in the Group includes three (2005: four) Directors, whose emoluments are disclosed in note 6, and two (2005: one) others whose emoluments are as follows:

| | 2006 $'000 | 2005 $'000 |
|---|---|---|
| Salaries and allowances | 2,972 | 1,288 |
| Retirement scheme contributions | 59 | 246 |
| | 3,031 | 1,534 |

## 7 FIVE HIGHEST PAID INDIVIDUALS' REMUNERATION (continued)

The emoluments of the two (2005: one) individuals with the highest emoluments are within the following bands:

| | **2006 Number of individuals** | 2005 Number of individuals |
|---|---|---|
| $1,000,001 - $1,500,000 | **1** | 1 |
| $1,500,001 - $2,000,000 | **1** | – |

## 8 INCOME TAX IN THE CONSOLIDATED INCOME STATEMENT

### (a) Taxation in the consolidated income statement represents:

| | **2006 $'000** | 2005 $'000 |
|---|---|---|
| **Current tax - Provision for Hong Kong Profits Tax** | | |
| Provision for Hong Kong Profits Tax for the year | **14,998** | 22,007 |
| Under-provision in respect of prior years | **3,967** | 13,503 |
| | **18,965** | 35,510 |
| **Current tax - Overseas** | | |
| Tax for the year | **12,039** | 8,223 |
| Over-provision in respect of prior years | **(281)** | – |
| | **11,758** | 8,223 |
| **Deferred tax** | | |
| Reversal of temporary differences (note 24(b)) | **2,635** | (12,729) |
| | **33,358** | 31,004 |

The provision for Hong Kong Profits Tax for 2006 is calculated at 17.5% (2005: 17.5%) of the estimated assessable profits for the year. Taxation for overseas subsidiaries is charged at the appropriate current rates of taxation ruling in the relevant countries.

As disclosed in the Group's financial statements for the year ended 31 December 2005, a subsidiary has received from the Hong Kong Inland Revenue Department ("IRD") additional assessments relating to the years of assessment 1994/95 to 2004/05 for taxation totalling $163 million. These additional assessments relate to a dispute over the deductibility of certain sub-contracting charges for tax assessment purposes. The subsidiary formally objected to the additional assessments. After lengthy negotiations, meetings and discussions with the IRD, the subsidiary has reached an agreement with the IRD for settlement of the objection for the years of assessment 1994/95 to 2003/04. Based on the outcome, the directors considered that no further provision is required for the years of assessment 1994/95 to 2006/07.

## 8 INCOME TAX IN THE CONSOLIDATED INCOME STATEMENT (continued)

### (b) Reconciliation between tax expense and accounting profit/(loss) at applicable tax rates:

| | **2006** | 2005 |
|---|---|---|
| | **$'000** | $'000 |
| Profit/(loss) before tax | **196,702** | (173,315) |
| Notional tax on profit/(loss) before tax calculated at the rates applicable to profits in the countries concerned | **14,493** | 15,743 |
| Tax effect of non-deductible expenses | **25,011** | 23,735 |
| Tax effect of non-taxable revenue | **(15,440)** | (26,853) |
| Tax effect of unused tax losses not recognised | **5,608** | 4,971 |
| Under-provision in prior years | **3,686** | 13,503 |
| Others | **–** | (95) |
| Actual tax expense | **33,358** | 31,004 |

## 9 PROFIT/(LOSS) ATTRIBUTABLE TO EQUITY SHAREHOLDERS OF THE COMPANY

The consolidated profit/(loss) attributable to equity shareholders of the Company includes a loss of $1,382,000 (2005: $12,159,000) which has been dealt with in the financial statements of the Company.

Reconciliation of the above amount to the Company's profit for the year:

| | **2006** | 2005 |
|---|---|---|
| | **$'000** | $'000 |
| Amount of consolidated profit/(loss) attributable to equity shareholders dealt with in the Company's financial statements | **(1,382)** | (12,159) |
| Dividends from subsidiaries attributable to the profits of subsidiaries, approved and paid during the year | **46,992** | 88,600 |
| Company's profit for the year (note 26(b)) | **45,610** | 76,441 |

## 10 DIVIDENDS

### (a) Dividends payable to equity shareholders of the Company attributable to the year

| | 2006 $'000 | 2005 $'000 |
|---|---|---|
| Interim dividend declared and paid of 9.0 cents (2005: 10.0 cents) per share | **29,108** | 32,120 |
| Final dividend proposed after the balance sheet date of 24.0 cents (2005: 28.0 cents) per share | **77,621** | 90,290 |
| | **106,729** | 122,410 |

The dividends attributable to the years ended 31 December 2005 and 2006 are scrip dividend with a cash option and cash dividend respectively.

The final dividend proposed after the balance sheet date has not been recognised as a liability at the balance sheet date.

### (b) Dividends payable to equity shareholders of the Company attributable to the previous financial year, approved and paid during the year

| | 2006 $'000 | 2005 $'000 |
|---|---|---|
| Final dividend in respect of the previous financial year, approved and paid during the year, of 28.0 cents (2005: 28.0 cents) per share | **90,290** | 88,607 |

(Expressed in Hong Kong dollars unless otherwise indicated)

## 11 EARNINGS/(LOSS) PER SHARE

### (a) Basic earnings/(loss) per share

The calculation of basic earnings/(loss) per share is based on the profit attributable to equity shareholders of $173,228,000 (2005: $178,976,000 loss) and the weighted average of 322,928,481 shares (2005: 318,304,488 shares) in issue during the year.

### (b) Diluted earnings/(loss) per share

The calculation of diluted earnings per share for the year ended 31 December 2006 was based on the profit attributable to equity shareholders of the Company of $173,228,000 and the weighted average number of shares of 323,120,103 shares after adjusting for the effects of all dilutive potential shares.

Diluted loss per share for the year ended 31 December 2005 was the same as the basic loss per share as the potential ordinary shares outstanding during the year ended 31 December 2005 were anti-dilutive.

### (c) Weighted average number of shares (diluted)

| | **2006 Number of shares** |
|---|---|
| Weighted average number of shares used in calculating basic earnings per share | **322,928,481** |
| Effect of deemed issue of shares for no consideration arising from the Company's share option scheme | **191,622** |
| Weighted average number of shares used in calculating diluted earnings per share | **323,120,103** |

## 12 FIXED ASSETS

### The Group

| | Land and buildings held for own use $'000 | Plant, machinery, tools and equipment $'000 | Others $'000 | Sub-total $'000 | Investment properties $'000 | Interest in leasehold land held for own use under operating leases $'000 | Total $'000 |
|---|---|---|---|---|---|---|---|
| **Cost:** | | | | | | | |
| At 1 January 2005 | 282,478 | 578,053 | 218,416 | 1,078,947 | – | 40,445 | 1,119,392 |
| Exchange adjustments | 486 | 1,285 | 272 | 2,043 | – | 127 | 2,170 |
| Additions | 3,039 | 99,452 | 12,671 | 115,162 | – | – | 115,162 |
| Transfer | (21,296) | (6,894) | 6,894 | (21,296) | 21,296 | – | – |
| Disposals | (16) | (603) | (4,234) | (4,853) | – | (4,457) | (9,310) |
| At 31 December 2005 | 264,691 | 671,293 | 234,019 | 1,170,003 | 21,296 | 36,115 | 1,227,414 |
| At 1 January 2006 | 264,691 | 671,293 | 234,019 | 1,170,003 | 21,296 | 36,115 | 1,227,414 |
| Exchange adjustments | 6,187 | 10,911 | 8,309 | 25,407 | – | 793 | 26,200 |
| Additions | 707 | 29,478 | 20,422 | 50,607 | – | – | 50,607 |
| Disposals | (9,782) | (40,756) | (88,931) | (139,469) | – | – | (139,469) |
| At 31 December 2006 | 261,803 | 670,926 | 173,819 | 1,106,548 | 21,296 | 36,908 | 1,164,752 |
| **Accumulated amortisation and depreciation and impairment losses:** | | | | | | | |
| At 1 January 2005 | 58,351 | 466,871 | 176,170 | 701,392 | – | 5,923 | 707,315 |
| Exchange adjustments | (56) | 422 | 9 | 375 | – | 8 | 383 |
| Charge for the year | 6,378 | 48,095 | 18,225 | 72,698 | 446 | 750 | 73,894 |
| Transfer | (10,238) | (4,823) | 4,823 | (10,238) | 10,238 | – | – |
| Impairment loss | 63,240 | 7,443 | – | 70,683 | – | 10,352 | 81,035 |
| Written back on disposals | (1) | (606) | (3,702) | (4,309) | – | (551) | (4,860) |
| At 31 December 2005 | 117,674 | 517,402 | 195,525 | 830,601 | 10,684 | 16,482 | 857,767 |
| At 1 January 2006 | 117,674 | 517,402 | 195,525 | 830,601 | 10,684 | 16,482 | 857,767 |
| Exchange adjustments | 2,549 | 7,389 | 7,249 | 17,187 | – | 355 | 17,542 |
| Charge for the year | 5,100 | 55,390 | 19,277 | 79,767 | 446 | 602 | 80,815 |
| Written back on disposals | (2,931) | (40,179) | (83,881) | (126,991) | – | – | (126,991) |
| At 31 December 2006 | 122,392 | 540,002 | 138,170 | 800,564 | 11,130 | 17,439 | 829,133 |
| **Net book value:** | | | | | | | |
| At 31 December 2006 | 139,411 | 130,924 | 35,649 | 305,984 | 10,166 | 19,469 | 335,619 |
| At 31 December 2005 | 147,017 | 153,891 | 38,494 | 339,402 | 10,612 | 19,633 | 369,647 |

## 12 FIXED ASSETS (continued)

**The Group** (continued)

(a) Other fixed assets comprise mainly leasehold improvements, furniture, fixtures, office equipment and motor vehicles.

(b) As a part of the Group's development strategy, the Group decided to relocate the production operation in Malaysia to the Group's Shenzhen and Heyuan plants and the Hong Kong office premise in Tseung Kwan O to Kwun Tong in 2005. As a result, the directors assessed the recoverable amount of the related buildings and plant, machinery, tools and equipment and an impairment loss of $81,035,000 was recognised for the year ended 31 December 2005.

(c) The analysis of the net book value of properties is as follows:

| | **2006** **$'000** | 2005 $'000 |
|---|---|---|
| In Hong Kong | | |
| – medium-term leases | **80,279** | 89,982 |
| Outside Hong Kong | | |
| – freehold | **547** | 523 |
| – long-term leases | **26,895** | 26,127 |
| – medium-term leases | **51,883** | 50,887 |
| – no specified lease term | **9,442** | 9,743 |
| | **88,767** | 87,280 |
| | **169,046** | 177,262 |
| Representing: | | |
| Land and buildings held for own use | **139,411** | 147,017 |
| Investment properties | **10,166** | 10,612 |
| Interest in leasehold land held for own use under operating leases | **19,469** | 19,633 |
| | **169,046** | 177,262 |

(d) Investment properties of the Group are stated at cost less accumulated depreciation.

## 12 FIXED ASSETS (continued)

**The Group** (continued)

(e) Fixed assets leased out under operating leases

The Group leases out investment properties under operating leases. The leases typically run for an initial period of one to two years, with an option to renew the lease after that date at which time all terms are renegotiated.

All properties held under operating leases that would otherwise meet the definition of investment property are classified as investment property. The fair value of the investment properties as at 31 December 2006, as determined by the directors of the Company by reference to recent market transactions in comparable properties, amounted to $20,765,000 (2005: $19,208,000). Investment properties have not been valued by an independent valuer who holds a recognised and professional qualification and has recent experience in the location and category of the investment properties being valued.

The Group's total future minimum lease payments under non-cancellable operating leases are receivable as follows:

| | **2006** | 2005 |
|---|---|---|
| | **$'000** | $'000 |
| Within 1 year | **320** | 100 |
| After one year but within 5 years | **160** | – |
| | **480** | 100 |

## 13 INTANGIBLE ASSETS

**The Group**

| | **The Group Patent rights** | |
|---|---|---|
| | **2006** | 2005 |
| | **$'000** | $'000 |
| **Cost:** | | |
| At 1 January and 31 December | **30,845** | 30,845 |
| **Accumulated amortisation and impairment losses:** | | |
| At 1 January | **(30,845)** | (3,795) |
| Charge for the year | **–** | (1,622) |
| Impairment loss | **–** | (25,428) |
| At 31 December | **(30,845)** | (30,845) |
| **Net book value:** | | |
| At 31 December | **–** | – |

The amortisation charge for the year ended 31 December 2005 was included in "other operating expenses" in the consolidated income statement.

## 14 GOODWILL

As a part of the Group's development strategy, the Group decided to relocate the production operation in Malaysia to the Group's Shenzhen and Heyuan plants in 2005. As a result, the directors reassessed the recoverable amount of the related goodwill and an impairment loss was recognised for the year ended 31 December 2005 to write off the entire carrying amount of goodwill.

## 15 INTEREST IN SUBSIDIARIES

| | The Company | |
|---|---|---|
| | **2006** | 2005 |
| | **$'000** | $'000 |
| Unlisted shares, at cost | **101,453** | 101,453 |
| Amounts due from subsidiaries | **786,837** | 853,415 |
| | **888,290** | 954,868 |

All of these are controlled subsidiaries as defined under note 1(c) and have been consolidated into the Group's financial statements.

Details of these subsidiaries are as follows:

| | | | Proportion of ownership interest | | | |
|---|---|---|---|---|---|---|
| **Name of company** | **Place of incorporation/ operation** | **Particulars of issued/registered capital** | **Group's effective interest** | **Held by the Company** | **Held by a subsidiary** | **Principal activities** |
| * Varitronix (B.V.I.) Limited | British Virgin Islands/ Hong Kong | 18,480 ordinary shares of US$1 each | 100% | 100% | – | Investment holding |
| * Varintelligent (BVI) Limited | British Virgin Islands/ Hong Kong | 1 ordinary share of US$1 each | 100% | 100% | – | Holding and licensing of trademarks |
| Vogue Industries Limited | British Virgin Islands/ Hong Kong | 100 ordinary shares of US$1 each | 100% | 100% | – | Investment holding |
| Varitronix Limited | Hong Kong | 2 ordinary shares of $1,000 each 1,848 non-voting deferred ordinary shares of $1,000 each | 100% | – | 100% | Design, manufacture and sale of liquid crystal displays and related products |

## 15 INTEREST IN SUBSIDIARIES (continued)

| Name of company | Place of incorporation/ operation | Particulars of issued/registered capital | Proportion of ownership interest: Group's effective interest | Held by the Company | Held by a subsidiary | Principal activities |
|---|---|---|---|---|---|---|
| Varitronix (Malaysia) Sdn. Bhd. | Malaysia | 38,000,000 Ordinary shares of Myr$1 each | 100% | – | 100% | Design, manufacture and sale of liquid crystal displays and related products |
| # * Varitronix (Heyuan) Co. Ltd. | The People's Republic of China | Rmb78,910,000 | 90.1% | – | 90.1% | Manufacture of liquid crystal displays and related products |
| # * Varitronix (Heyuan) Display Technology Limited | The People's Republic of China | Rmb192,919,473 | 100% | – | 100% | Manufacture of liquid crystal displays and related products |
| * Varitronix Manufacturing (BVI) Limited | British Virgin Islands/The People's Republic of China | 100 ordinary shares of US$1 each | 100% | – | 100% | Subcontract and operate production plant in the People's Republic of China |
| # Varitronix Pengyuan Limited | The People's Republic of China | Rmb8,000,000 | 90% | – | 90% | Liquid crystal displays business |
| * Varitronix (Singapore) Pte Ltd. | Singapore | 200,000 ordinary shares of SGD 1 each | 100% | – | 100% | Research development centre |
| * Varitronix (U.K.) Limited | United Kingdom | 100 ordinary shares of £10 each | 100% | – | 100% | Marketing and sales consultants |
| * VL Electronics, Inc. | United States | 5,000 common stock of US$10 each | 100% | – | 100% | Marketing and sales consultants |
| * Varitronix (Canada) Limited | Canada | 100 ordinary shares of C$1 each | 100% | – | 100% | Marketing and sales consultants |

(Expressed in Hong Kong dollars unless otherwise indicated)

## 15 INTEREST IN SUBSIDIARIES (continued)

| | Name of company | Place of incorporation/ operation | Particulars of issued/registered capital | Proportion of ownership interest: Group's effective interest | Held by the Company | Held by a subsidiary | Principal activities |
|---|---|---|---|---|---|---|---|
| * | Varitronix Italia, s.r.l. | Italy | 25,000 ordinary shares of €0.52 each | 100% | – | 100% | Marketing and sales consultants |
| * | Varitronix GmbH | Germany | 100,000 shares of €0.51 each | 60% | – | 60% | Marketing and sales consultants |
| | Varitronix (France) SAS | France | 2,500 ordinary Shares of €15.25 each | 100% | – | 100% | Marketing and sales consultants |
| | Link Score Investment Limited | Hong Kong | 100 ordinary shares of $1 each | 100% | – | 100% | Property investment and investment holding |
| | Polysources Properties Limited | Hong Kong | 2 ordinary shares of $100 each 154 non-voting deferred ordinary shares of $100 each | 100% | – | 100% | Property investment |
| * | Starel Trading Limited | Republic of Cyprus/United Kingdom | 1,000 shares of Cyprus £1 each | 100% | – | 100% | Property investment |
| * | Quest Industries Limited | British Virgin Islands/The People's Republic of China | 100 ordinary shares of US$1 each | 100% | – | 100% | Property investment |
| | Cadac Electronic (M) Sdn. Bhd. | Malaysia | 276,002 ordinary shares of Myr$1 each | 100% | – | 100% | Property investment |
| | Varitronix Finance Limited | British Virgin Islands/ Hong Kong | 100 ordinary shares of US$1 each | 100% | – | 100% | Provision of financial co-ordination services for group companies and holding of trading securities |

## 15 INTEREST IN SUBSIDIARIES (continued)

| | Name of company | Place of incorporation/ operation | Particulars of issued/registered capital | Proportion of ownership interest: Group's effective interest | Proportion of ownership interest: Held by the Company | Proportion of ownership interest: Held by a subsidiary | Principal activities |
|---|---|---|---|---|---|---|---|
| | Varitronix Investment Limited | British Virgin Islands/ Hong Kong | 5,000 ordinary shares of US$1 each | 100% | – | 100% | Investment holding |
| * | Varitronix Marketing Limited | British Virgin Islands/ United Kingdom | 1,000 shares of US$1 each | 100% | – | 100% | Investment holding |
| * | Mcalpine Management Limited | British Virgin Islands/ United Kingdom | 1,000 shares of US$1 each | 100% | – | 100% | Investment holding |
| * | Varitronix Marketing (China) Limited | British Virgin Island/ The People's Republic of China | 1 share of US$1 | 90% | – | 90% | Investment holding |
| * | Varitronix (Shenzhen) Limited | British Virgin Island/ The People's Republic of China | 1 share of US$1 | 100% | – | 100% | Investment holding |
| | Varitronix Agencies Limited | British Virgin Islands/ Hong Kong | 50,000 shares of US$1 each | 100% | – | 100% | Dormant |
| * | Varitronix Optech Limited | Hong Kong | 100,000 ordinary shares of $1 each | 100% | – | 100% | Dormant |
| * | Great Boom Developments Limited | British Virgin Islands/ Hong Kong | 10,000 ordinary shares of US$1 each | 90% | – | 90% | Investment holding |
| * | Misdino Group Limited | British Virgin Islands/ Hong Kong | 1 ordinary share of US$1 each | 100% | – | 100% | Investment holding |

(Expressed in Hong Kong dollars unless otherwise indicated)

## 15 INTEREST IN SUBSIDIARIES (continued)

| | Name of company | Place of incorporation/ operation | Particulars of issued/registered capital | Proportion of ownership interest: Group's effective interest | Held by the Company | Held by a subsidiary | Principal activities |
|---|---|---|---|---|---|---|---|
| * | Sun Yik Group Limited | British Virgin Islands/ Hong Kong | 1 ordinary share of US$1 each | 100% | – | 100% | Investment holding |
| * | Varitronix Shenzhen Linkscore Limited | The People's Republic of China | Rmb500,000 | 100% | – | 100% | Trading of electronic components |
| * | Varitronix (Macao Commercial Offshore) Limited | Macau | Mop100,000 | 100% | – | 100% | Trading of electronic components |
| * | Eastriver Investments Limited | British Virgin Islands/ Hong Kong | 1,000 ordinary share of US$1 each | 100% | – | 100% | Investment holding |
| # | Varitronix Pengyuan Electronics Limited | The People's Republic of China | Rmb15,000,000 | 90% | – | 90% | Liquid crystal display business |
| * | Varitronix LEP Limited | British Virgin Islands/ Hong Kong | 1 ordinary share of US$1 each | 100% | – | 100% | Property investment |
| * | Varitronix OLED Limited | British Virgin Islands/ Hong Kong | 1 ordinary share of US$1 each | 100% | – | 100% | Investment holding |
| * | Le Grove Investments Limited | British Virgin Islands/ Hong Kong | 1 ordinary share of US$1 each | 100% | – | 100% | Investment holding |
| * | Liven Kingyip (BVI) Limited | British Virgin Islands/ Hong Kong | 1,000 ordinary share of US$1 each | 68% | – | 68% | Investment holding |
| | Liven Kingyip Communication Technology Limited | Hong Kong | 10,000 ordinary share of HK$1 each | 68% | – | 68% | Trading of electronic components |

## 15 INTEREST IN SUBSIDIARIES (continued)

| Name of company | Place of incorporation/ operation | Particulars of issued/registered capital | Proportion of ownership interest: Group's effective interest | Held by the Company | Held by a subsidiary | Principal activities |
|---|---|---|---|---|---|---|
| * Profit Concept Holdings Limited | British Virgin Islands/ Hong Kong | 1 ordinary share of US$1 each | 100% | – | 100% | Investment holding |
| #* Shenzhen Liven Kingyip Communication Technology Limited | The People's Republic of China | HK$500,000 | 68% | – | 68% | Trading of liquid crystal display |
| #* Varitronix Electronics (Shenzhen) Limited | The People's Republic of China | US$2,100,000 | 100% | – | 100% | Manufacture of liquid crystal displays and related products |
| * Varitronix Asia Limited | British Virgin Islands/ Hong Kong | 1 ordinary share of US$1 each | 100% | – | 100% | Investment holding |
| Ample Bonus Limited | Hong Kong | 10,000 ordinary shares of HK$1 each | 100% | – | 100% | Trading of liquid crystal display |
| * Varitronix (Switzerland) GmbH | Switzerland | CHF30,000 | 100% | – | 100% | Marketing and sales consultants |

* *Companies not audited by KPMG. The financial statements of the subsidiaries not audited by KPMG reflect total assets and total turnover constituting approximately 23% (2005: 35%) and 15% (2005: 10%) respectively of the related consolidated totals.*

| # *Name of company* | *Type of legal entity* |
|---|---|
| Varitronix (Heyuan) Co. Ltd. | Sino-foreign co-operative joint venture |
| Varitronix Pengyuan Limited | Sino-foreign equity joint venture |
| Varitronix (Heyuan) Display Technology Limited | Wholly owned foreign enterprise |
| Varitronix Pengyuan Electronics Limited | Sino-foreign equity joint venture |
| Shenzhen Liven Kingyip Communication Technology Limited | Wholly owned foreign enterprise |
| Varitronix Electronics (Shenzhen) Limited | Wholly owned foreign enterprise |

## 16 OTHER NON-CURRENT FINANCIAL ASSETS (AT MARKET VALUE)

| | The Group | |
|---|---|---|
| | **2006** | 2005 |
| | **$'000** | $'000 |
| **Available-for-sale debt securities** | | |
| Listed outside Hong Kong | **23,734** | 22,994 |
| Unlisted | **20,785** | 27,828 |
| | **44,519** | 50,822 |
| **Available-for-sale equity securities** | | |
| Listed in Hong Kong | **29,014** | 134,462 |
| Unlisted | **1** | 1 |
| Unlisted investment funds | **–** | 40 |
| | **29,015** | 134,503 |
| Total | **73,534** | 185,325 |

Movements in available-for-sale securities are as follows:

| | **2006** | 2005 |
|---|---|---|
| | **$'000** | $'000 |
| At 1 January | **185,325** | 60,489 |
| Additions | **12,665** | 321,429 |
| Disposals | **(136,018)** | (3,955) |
| Transfer to investment revaluation reserve | **19,772** | (16,863) |
| Impairment loss | **(8,210)** | (175,775) |
| Total | **73,534** | 185,325 |

The above available-for-sale securities consist of certain long-term investments in companies engaging in OLED business and handset design business and other listed debt and equity securities. Of the additional investments made during the year ended 31 December 2005, an impairment loss of $168,025,000 was made against the carrying amount at 31 December 2005 as the directors reassessed the expected future cashflows to be generated from these investments in view of the uncertain market situation; a further impairment loss of $8,210,000 was made during the year ended 31 December 2006 following a reassessment in 2006.

The carrying amount of the listed investments at 31 December 2005 included an aggregate amount of $75,127,000 relating to investment in listed companies in respect of which a director and major shareholder of the Company is also a director and major shareholder of these invested companies. All of these listed investments were disposed of at a total gain of $38,005,000 during the year ended 31 December 2006.

## 17 TRADING SECURITIES (AT MARKET VALUE)

| | The Group | |
|---|---|---|
| | **2006** | 2005 |
| | **$'000** | $'000 |
| **Debt securities** | | |
| Listed outside Hong Kong | **3,940** | 3,955 |
| **Equity securities** | | |
| Listed | | |
| – in Hong Kong | **31,638** | 52,652 |
| – outside Hong Kong | **109,887** | 118,861 |
| | **141,525** | 171,513 |
| Unlisted investment funds | **18,719** | 17,797 |
| | **160,244** | 189,310 |
| Total | **164,184** | 193,265 |

## 18 INVENTORIES

### (a) Inventories in the balance sheet comprise:

| | The Group | |
|---|---|---|
| | **2006** | 2005 |
| | **$'000** | $'000 |
| Raw materials | **167,650** | 119,545 |
| Work in progress | **60,104** | 31,310 |
| Finished goods | **109,383** | 82,782 |
| | **337,137** | 233,637 |

### (b) The analysis of the amount of inventories recognised as an expense is as follows:

| | The Group | |
|---|---|---|
| | **2006** | 2005 |
| | **$'000** | $'000 |
| Carrying amount of inventories sold | **1,381,479** | 1,470,060 |
| Write down of inventories | **12,658** | 8,540 |
| | **1,394,137** | 1,478,600 |

## 19 TRADE AND OTHER RECEIVABLES

Included in trade and other receivables are trade debtors and bills receivable (net of impairment losses for bad and doubtful debts) which are expected to be recovered within one year and have the following ageing analysis as of the balance sheet date:

| | The Group | |
|---|---|---|
| | **2006** | 2005 |
| | **$'000** | $'000 |
| Within 60 days of the invoice issue date | **278,040** | 320,436 |
| 61 to 90 days after the invoice issue date | **47,915** | 33,888 |
| 91 to 120 days after the invoice issue date | **9,114** | 7,350 |
| More than 120 days but less than 12 months after the invoice issue date | **12,049** | 20,143 |
| More than 12 months after the invoice issue date | **1** | 2,506 |
| | **347,119** | 384,323 |

Debts are due within 90 days from the date of the invoice.

Included in trade and other receivables are the following amounts denominated in a currency other than the functional currency of the entity to which they relate:

| | The Group | |
|---|---|---|
| | **2006** | 2005 |
| | **$'000** | $'000 |
| Euros | **EUR 1,277** | EUR 1,108 |
| United States Dollars | **USD 19,642** | USD 17,585 |

## 20 CASH AND CASH EQUIVALENTS

| | The Group | | The Company | |
|---|---|---|---|---|
| | **2006** | 2005 | **2006** | 2005 |
| | **$'000** | $'000 | **$'000** | $'000 |
| Deposits with banks and other financial institutions | **152,607** | 263,279 | **–** | – |
| Cash at bank and in hand | **346,081** | 152,566 | **299** | 316 |
| Cash and cash equivalents in the balance sheet and consolidated cash flow statement | **498,688** | 415,845 | **299** | 316 |

## 20 CASH AND CASH EQUIVALENTS (continued)

Included in cash and cash equivalents are the following amounts denominated in a currency other than the functional currency of the entity to which they relate:

| | The Group | | The Company | |
|---|---|---|---|---|
| | **2006** | 2005 | **2006** | 2005 |
| | **$'000** | $'000 | **$'000** | $'000 |
| Euros | **EUR 3,120** | EUR 6,669 | **EUR –** | EUR – |
| United States Dollars | **USD 22,059** | USD 33,192 | **USD 3** | USD 13 |

## 21 BANK LOANS AND OVERDRAFTS

Unsecured, interest-bearing bank loans and overdrafts are repayable as follows:

| | The Group | |
|---|---|---|
| | **2006** | 2005 |
| | **$'000** | $'000 |
| Within 1 year or on demand | **45,144** | 98,549 |

Included in bank loans and overdrafts are the following amounts denominated in a currency other than the functional currency of the entity to which they relate:

| | The Group | |
|---|---|---|
| | **2006** | 2005 |
| | **$'000** | $'000 |
| Japanese Yen | **JPY 189,644** | JPY 376,976 |

## 22 TRADE AND OTHER PAYABLES

Included in trade and other payables are trade creditors and bills payable with the following ageing analysis as of the balance sheet date:

| | The Group | |
|---|---|---|
| | **2006** | 2005 |
| | **$'000** | $'000 |
| Within 60 days of supplier invoice date | **275,516** | 200,217 |
| 61 to 120 days after supplier invoice date | **36,040** | 32,178 |
| More than 120 days but within 12 months after supplier invoice date | **5,626** | 9,059 |
| | **317,182** | 241,454 |

## 22 TRADE AND OTHER PAYABLES (continued)

Included in trade and other payables are the following amounts denominated in a currency other than the functional currency of the entity to which they relate:

| | The Group | |
|---|---|---|
| | **2006** | 2005 |
| | **$'000** | $'000 |
| United States Dollars | **USD 14,476** | USD 13,445 |
| Renminbi | **RMB 10,638** | RMB 4,615 |
| Japanese Yen | **JPY 495,009** | JPY 435,921 |

## 23 CONVERTIBLE NOTES

| | The Group | |
|---|---|---|
| | **2006** | 2005 |
| | **$'000** | $'000 |
| At 31 December | **–** | 30,109 |

Pursuant to a supplemental note entered into by the issuer, being an indirect wholly-owned subsidiary of the Company and the holders of the convertible notes ("Noteholders") on 25 January 2006, the convertible notes were redeemed at 85% of their face value ($26,520,000) on 27 January 2006. One of the Noteholders is the brother-in-law of an Executive Director of the Company. The other Noteholder is a director of an indirect wholly-owned subsidiary of the Company.

## 24 INCOME TAX IN THE BALANCE SHEET

### (a) Current taxation in the balance sheet represents:

| | The Group | |
|---|---|---|
| | **2006** | 2005 |
| | **$'000** | $'000 |
| Provision for Hong Kong Profits Tax for the year | **14,998** | 22,007 |
| Provisional Profits Tax paid | **(277)** | (354) |
| Balance of Profits Tax recoverable relating to prior years | **(4,537)** | (3,032) |
| Overseas tax | **3,142** | 2,272 |
| | **13,326** | 20,893 |
| Current tax recoverable | **(888)** | (2,483) |
| Current tax payable | **14,214** | 23,376 |
| | **13,326** | 20,893 |

## 24 INCOME TAX IN THE BALANCE SHEET (continued)

### (b) Deferred tax assets and liabilities recognised:

**The Group**

The components of deferred tax (assets)/liabilities recognised in the consolidated balance sheet and the movements during the year are as follows:

| | Depreciation allowances in excess of the related depreciation $'000 | Tax allowances for intangible assets in excess of amortisation $'000 | Provisions $'000 | Others $'000 | Total $'000 |
|---|---|---|---|---|---|
| At 1 January 2005 | 8,891 | 4,734 | (6,902) | (1,346) | 5,377 |
| (Credited)/charged to profit or loss (note 8(a)) | (7,823) | (4,734) | (1,068) | 896 | (12,729) |
| At 31 December 2005 | 1,068 | – | (7,970) | (450) | (7,352) |
| At 1 January 2006 | 1,068 | – | (7,970) | (450) | (7,352) |
| Charged/(credited) to profit or loss (note 8(a)) | 357 | – | 2,278 | – | 2,635 |
| **At 31 December 2006** | **1,425** | **–** | **(5,692)** | **(450)** | **(4,717)** |

| | The Group | |
|---|---|---|
| | **2006 $'000** | 2005 $'000 |
| Net deferred tax assets recognised on the balance sheet | **(4,957)** | (8,725) |
| Net deferred tax liabilities recognised on the balance sheet | **240** | 1,373 |
| | **(4,717)** | (7,352) |

### (c) Deferred tax assets not recognised

In accordance with the accounting policy set out in note 1(o), the Group has not recognised deferred tax assets in respect of cumulative tax losses of $39,565,000 (2005: $19,119,000) as it is not probable that future taxable profits against which the losses can be utilised will be available in the relevant tax jurisdiction and entity. The tax losses do not expire under current tax legislation.

(Expressed in Hong Kong dollars unless otherwise indicated)

## 25 EQUITY SETTLED SHARE-BASED TRANSACTIONS

The Company had a Share Option Scheme for the employees of the Group which was adopted on 6 June 1991, subsequently amended on 8 June 1999 and expired on 5 June 2001. The options under the first Share Option Scheme are exercisable for a period of ten years following the date of grant. A second Share Option Scheme of the Company for the employees of the Group was adopted on 22 June 2001 and terminated on 12 May 2003. The options under the second Share Option Scheme are exercisable for a period of ten years following the date of grant.

A third Share Option Scheme of the Company was adopted on 12 May 2003 as an incentive to the Group's employees and business associates. The directors of the Company are authorised, at their discretion, to invite any employee, director, including executive and non-executive directors, or business associate of any company in the Group, to take up options to subscribe for shares at a price determined by the board and notified to each grantee and which will not be less than the closing price of the shares on the Stock Exchange on the date of offer of the option granted to such grantee or the average of the closing prices of the shares on the Stock Exchange on the five trading days immediately preceding the date of offer of the option granted to such grantee or the nominal value of the shares, whichever is higher.

The maximum number of shares in respect of which options may be granted under the third Share Option Scheme and any other Share Option Schemes of the Company may not exceed 10 percent of the issued share capital of the Company at the date of approval of the third Share Option Scheme. The options under the third Share Option Scheme are exercisable for a period of ten years from the date of grant.

### (a) The terms and conditions of the grants that existed during the years are as follows, whereby all options are settled by physical delivery of shares:

| | **Number of options** | **Vesting conditions** | **Contractual life of options** |
|---|---|---|---|
| Options granted to directors: | | | |
| – 30 October 2002 | 1,000,000 | Immediate from the date of grant | 10 years |
| – 21 December 2004 | 300,000 | Immediate from the date of grant | 10 years |
| – 22 July 2005 | 3,000,000 | Immediate from the date of grant | 10 years |
| – 19 December 2005 | 9,000,000 | Immediate from the date of grant | 10 years |

## 25 EQUITY SETTLED SHARE BASED TRANSACTIONS (continued)

(a) The terms and conditions of the grants that existed during the years are as follows, whereby all options are settled by physical delivery of shares: (continued)

| | Number of options | Vesting conditions | Contractual life of options |
|---|---|---|---|
| Options granted to employees: | | | |
| – 9 June 1999 | 357,750 | Immediate from the date of grant | 10 years |
| – 1 June 2000 | 569,000 | Immediate from the date of grant | 10 years |
| – 30 August 2001 | 140,000 | Immediate from the date of grant | 10 years |
| – 13 September 2002 | 153,500 | Immediate from the date of grant | 10 years |
| – 30 October 2002 | 1,000,000 | Immediate from the date of grant | 10 years |
| – 6 October 2003 | 301,500 | Immediate from the date of grant | 10 years |
| – 20 December 2004 | 2,428,000 | Immediate from the date of grant | 10 years |
| – 21 December 2004 | 3,000,000 | Immediate from the date of grant | 10 years |

(Expressed in Hong Kong dollars unless otherwise indicated)

## 25 EQUITY SETTLED SHARE BASED TRANSACTIONS (continued)

### (b) The number and weighted average exercise prices of share options are as follows:

| | **2006** Weighted average exercise price | **2006** Number of options | 2005 Weighted average exercise price | 2005 Number of options |
|---|---|---|---|---|
| Outstanding at the beginning of the year | **$6.445** | **21,250,250** | $6.979 | 18,061,250 |
| Granted during the year | **–** | **–** | $5.948 | 12,000,000 |
| Forfeited during the year | **$7.140** | **(4,726,500)** | $7.633 | (6,555,000) |
| Exercised during the year | **$3.348** | **(22,000)** | $4.623 | (2,256,000) |
| Outstanding at the end of the year | **$6.250** | **16,501,750** | $6.445 | 21,250,250 |
| Exercisable at the end of the year | | **16,501,750** | | 21,250,250 |

The weighted average share price at the date of exercise of shares options exercised during the year was $5.252 (2005: $6.063).

### (c) Fair value of share options and assumptions

The fair value of services received in return for share options granted are measured by reference to the fair value of share options granted. The estimate of the fair value of the services received is measured based on a Black-Scholes. The contractual life of the option is used as in input into this model.

There were no share options granted during 2006.

Fair value of share options and assumptions for share options granted in 2005

| | |
|---|---|
| Fair value at measurement date | 0.948 |
| Share price | 5.88 |
| Exercise price | 5.89 |
| Expected volatility (expressed as weighted average volatility) | 31.9% |
| Option life | 5 years |
| Expected dividends | 6.50% |
| Risk-free interest free (based on Exchange Fund Notes) | 4.02% |

The expected volatility is based on the historic volatility (calculated based on the weighted average remaining life of the share options), adjusted for any expected changes to future volatility due to publicly available information. Expected dividends are based on historical dividends.

Share options were granted under a service condition. This condition has not been taken into account in the grant date fair value measurement of the services received. There were no market conditions associated with the share option grants.

## 26 CAPITAL AND RESERVES

### (a) The Group

| | Attributable to equity shareholders of the Company | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Share capital (note c) $'000 | Share premium (note d(i)) $'000 | Exchange reserve (note d(iii)) $'000 | Fair value revaluation reserve (note d(iv)) $'000 | Capital reserve (note d(v)) $'000 | Other reserves (note d(vi)) $'000 | Retained profits $'000 | Total $'000 | Minority interests $'000 | Total equity $'000 |
| **2005** | | | | | | | | | | |
| At 1 January 2005 | 79,059 | 657,389 | (12,469) | 5,365 | 1,961 | 1,933 | 819,073 | 1,552,311 | 55,908 | 1,608,219 |
| Final dividends approved in respect of the previous year | – | – | – | – | – | – | (88,607) | (88,607) | – | (88,607) |
| Shares issued under share option scheme | 564 | 9,866 | – | – | – | – | – | 10,430 | – | 10,430 |
| Allotment of shares from scrip dividends | 991 | 23,565 | – | – | – | – | – | 24,556 | – | 24,556 |
| Available-for-sale securities: | | | | | | | | | | |
| – changes in fair value | – | – | – | (16,863) | – | – | – | (16,863) | – | (16,863) |
| – transfer to profit or loss on disposal | – | – | – | (70) | – | – | – | (70) | – | (70) |
| Capital contribution by minority interest shareholder | – | – | – | – | – | – | – | – | 2,820 | 2,820 |
| Equity settled share-based transactions | – | – | – | – | 11,373 | – | – | 11,373 | – | 11,373 |
| Transfer to other reserves | – | – | – | – | – | 49 | (49) | – | – | – |
| Interim dividends declared in respect of the current year | – | – | – | – | – | – | (32,120) | (32,120) | – | (32,120) |
| Loss for the year | – | – | – | – | – | – | (178,976) | (178,976) | (25,343) | (204,319) |
| Exchange differences on translation of financial statements of overseas subsidiaries | – | – | 7,111 | – | – | – | – | 7,111 | 407 | 7,518 |
| At 31 December 2005 | 80,614 | 690,820 | (5,358) | (11,568) | 13,334 | 1,982 | 519,321 | 1,289,145 | 33,792 | 1,322,937 |

## 26 CAPITAL AND RESERVES (continued)

### (a) The Group (continued)

| | Attributable to equity shareholders of the Company | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Share capital (note c) $'000 | Share premium (note d(i)) $'000 | Exchange reserve (note d(iii)) $'000 | Fair value revaluation reserve (note d(iv)) $'000 | Capital reserve (note d(v)) $'000 | Other reserves (note d(vi)) $'000 | Retained profits $'000 | Total $'000 | Minority interests $'000 | Total equity $'000 |
| **2006** | | | | | | | | | | |
| At 1 January 2006 | **80,614** | **690,820** | **(5,358)** | **(11,568)** | **13,334** | **1,982** | **519,321** | **1,289,145** | **33,792** | **1,322,937** |
| Final dividends approved in respect of the previous year | **–** | **–** | **–** | **–** | **–** | **–** | **(90,290)** | **(90,290)** | **–** | **(90,290)** |
| Shares issued under share option scheme | **6** | **68** | **–** | **–** | **–** | **–** | **–** | **74** | **–** | **74** |
| Allotment of shares from scrip dividends | **236** | **4,448** | **–** | **–** | **–** | **–** | **–** | **4,684** | **–** | **4,684** |
| Available-for-sale securities: | | | | | | | | | | |
| – changes in fair value | **–** | **–** | **–** | **19,772** | **–** | **–** | **–** | **19,772** | **–** | **19,772** |
| – transfer to profit or loss on disposal | **–** | **–** | **–** | **(28,909)** | **–** | **–** | **–** | **(28,909)** | **–** | **(28,909)** |
| Capital contribution by minority interest shareholder | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **4,973** | **4,973** |
| Acquisition of minority interests | **–** | **–** | **–** | **–** | **–** | **(30,321)** | **–** | **(30,321)** | **(15,390)** | **(45,711)** |
| Increase in minority interests upon partial disposal of interests in a subsidiary | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **5,807** | **5,807** |
| Redemption of convertible notes | **–** | **–** | **–** | **–** | **(1,961)** | **–** | **1,961** | **–** | **–** | **–** |
| Profit for the year | **–** | **–** | **–** | **–** | **–** | **–** | **173,228** | **173,228** | **(9,884)** | **163,344** |
| Interim dividends declared in respect of the current year | **–** | **–** | **–** | **–** | **–** | **–** | **(29,108)** | **(29,108)** | **–** | **(29,108)** |
| Exchange differences on translation of financial statements of overseas subsidiaries | **–** | **–** | **14,179** | **–** | **–** | **–** | **–** | **14,179** | **318** | **14,497** |
| At 31 December 2006 | **80,856** | **695,336** | **8,821** | **(20,705)** | **11,373** | **(28,339)** | **575,112** | **1,322,454** | **19,616** | **1,342,070** |

## 26 CAPITAL AND RESERVES (continued)

### (b) The Company

| | Share capital (note c) $'000 | Share premium (note d(i)) $'000 | Contributed surplus (note d(ii)) $'000 | Capital reserve (note d(v)) $'000 | Retained profits $'000 | Total $'000 |
|---|---|---|---|---|---|---|
| At 1 January 2005 | 79,059 | 657,389 | 51,636 | – | 157,129 | 945,213 |
| Final dividends approved in respect of the previous year | – | – | – | – | (88,607) | (88,607) |
| Shares issues under share option scheme | 564 | 9,866 | – | – | – | 10,430 |
| Allotment of shares from scrip dividends | 991 | 23,565 | – | – | – | 24,556 |
| Equity settled share-based transaction | – | – | – | 11,373 | – | 11,373 |
| Profit for the year | – | – | – | – | 76,441 | 76,441 |
| Interim dividend declared in respect of the current year | – | – | – | – | (32,120) | (32,120) |
| At 31 December 2005 | 80,614 | 690,820 | 51,636 | 11,373 | 112,843 | 947,286 |

| | **Share capital** (note c) $'000 | **Share premium** (note d(i)) $'000 | **Contributed surplus** (note d(ii)) $'000 | **Capital reserve** (note d(v)) $'000 | **Retained profits** $'000 | **Total** $'000 |
|---|---|---|---|---|---|---|
| At 1 January 2006 | **80,614** | **690,820** | **51,636** | **11,373** | **112,843** | **947,286** |
| Final dividends approved in respect of the previous year | **–** | **–** | **–** | **–** | **(90,290)** | **(90,290)** |
| Shares issues under share option scheme | **6** | **68** | **–** | **–** | **–** | **74** |
| Allotment of shares from scrip dividends | **236** | **4,448** | **–** | **–** | **–** | **4,684** |
| Profit for the year | **–** | **–** | **–** | **–** | **45,610** | **45,610** |
| Interim dividend declared in respect of the current year | **–** | **–** | **–** | **–** | **(29,108)** | **(29,108)** |
| At 31 December 2006 | **80,856** | **695,336** | **51,636** | **11,373** | **39,055** | **878,256** |

## 26 CAPITAL AND RESERVES (continued)

### (c) Share capital

(i) Authorised and issued share capital

| | 2006 | | 2005 | |
|---|---|---|---|---|
| | **No. of shares '000** | **Amount $'000** | No. of shares '000 | Amount $'000 |
| **Authorised:** | | | | |
| Ordinary shares of $0.25 each | **400,000** | **100,000** | 400,000 | 100,000 |
| **Issued and fully paid:** | | | | |
| At 1 January | **322,455** | **80,614** | 316,235 | 79,059 |
| Shares issued under share option scheme | **22** | **6** | 2,256 | 564 |
| Allotment of shares from scrip dividends | **945** | **236** | 3,964 | 991 |
| At 31 December | **323,422** | **80,856** | 322,455 | 80,614 |

(ii) Terms of unexpired and unexercised share options at balance sheet date

| Exercise period | Exercise price | **2006 Number** | 2005 Number |
|---|---|---|---|
| 9 July 1999 to 8 July 2009 | HK$ 10.900 | **166,750** | 357,750 |
| 1 July 2000 to 30 June 2010 | HK$ 11.300 | **371,000** | 569,000 |
| 30 August 2001 to 29 August 2011 | HK$ 3.060 | **121,500** | 140,000 |
| 13 September 2002 to 12 September 2012 | HK$ 3.905 | **137,000** | 153,500 |
| 31 October 2002 to 30 October 2012 | HK$ 4.605 | **1,000,000** | 2,000,000 |
| 6 October 2003 to 5 October 2013 | HK$ 7.350 | **239,500** | 301,500 |
| 20 December 2004 to 19 December 2014 | HK$ 7.500 | **2,166,000** | 2,428,500 |
| 21 December 2004 to 20 December 2014 | HK$ 7.450 | **300,000** | 3,300,000 |
| 22 July 2005 to 21 July 2015 | HK$ 6.600 | **3,000,000** | 3,000,000 |
| 19 December 2005 to 18 December 2015 | HK$ 5.730 | **9,000,000** | 9,000,000 |
| | | **16,501,750** | 21,250,250 |

Each option entitles the holder to subscribe for one ordinary share in the Company. Further details of these options are set out in note 25 to the financial statements.

(iii) Shares issued under share option scheme

Shares issued under the share option scheme during the year were exercised to subscribe for 22,000 (2005: 2,256,000) ordinary shares in the Company at a consideration of $74,000 (2005: $10,430,000) of which $5,500 (2005: $564,000) was credited to share capital and the balance of $68,500 (2005: $9,866,000) was credited to the share premium account.

## 26 CAPITAL AND RESERVES (continued)

### (d) Nature and purpose of reserves

(i) Share premium

The application of the share premium account is governed by sections 150 and 157 of the Company's Articles of Association and the Companies Act 1981 of Bermuda.

(ii) Contributed surplus

The excess value of the shares of the subsidiaries acquired pursuant to the Group reorganisation scheme in 1991 over the nominal value of the new shares of the Company issued in exchange is credited to the contributed surplus account. Under the Companies Act 1981 of Bermuda (as amended) and the Bye-laws of the Company, the contributed surplus is distributable to shareholders. However, the directors have no current intention to distribute this surplus.

(iii) Exchange reserve

The exchange reserve comprises all foreign exchange differences arising from the translation of the financial statements of foreign operations. The reserve is dealt with in accordance with the accounting policies set out in note 1(q).

(iv) Fair value revaluation reserve

The fair value revaluation reserve comprises the cumulative net change in the fair value of available-for-sale securities held at the balance sheet date and is dealt with in accordance with the accounting policies in notes 1(d) and (g).

(v) Capital reserve

The capital reserve at 31 December 2006 comprises the fair value of the actual or estimated number of unexercised share options granted to employees of the Company recognised in accordance with the accounting policy adopted for share based payments in note 1(m).

The capital reserve at 31 December 2005 also included the value of the unexercised equity component of convertible notes issued by the Company recognised in accordance with the accounting policy adopted for convertible notes in note 1(p), which was released to retained profits upon redemption during the year ended 31 December 2006.

(vi) Other reserves

Other reserves comprise statutory reserves required in respect of the PRC incorporated subsidiaries.

(vii) Distributability of reserves

At 31 December 2006, the aggregate amount of reserves available for distribution to shareholders of the Company was $90,691,000 (2005: $164,479,000).

## 27 SEGMENT REPORTING

Segment information is presented in respect of the Group's business and geographical segments. Business segment information is chosen as the primary reporting format because this is more relevant to the Group's internal financial reporting.

### Business segment

As all of the Group's turnover and profits were derived from the design, manufacture and sale of liquid crystal displays and related products, accordingly no separate business segment analysis is presented for the Group.

### Geographical segments

In presenting information on the basis of geographical segments, segment revenue is based on the geographical locations of customers. Segment assets and capital expenditure are based on the geographical location of the assets.

| | Hong Kong and PRC | | Rest of Asia | | Europe | | North America | | Others | | Total | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | **2006** | 2005 | **2006** | 2005 | **2006** | 2005 | **2006** | 2005 | **2006** | 2005 | **2006** | 2005 |
| | **$'000** | $'000 | **$'000** | $'000 | **$'000** | $'000 | **$'000** | $'000 | **$'000** | $'000 | **$'000** | $'000 |
| Revenue from external customers | **743,609** | 828,255 | **260,653** | 371,894 | **703,303** | 635,913 | **109,667** | 88,387 | **49,843** | 55,358 | **1,867,075** | 1,979,807 |
| Segment assets | **1,407,648** | 1,396,501 | **158,372** | 197,680 | **152,091** | 114,469 | **155,748** | 100,496 | | | | |
| Capital expenditure incurred during the year | **49,753** | 112,344 | **5** | 850 | **812** | 1,950 | **37** | 18 | | | | |

Revenue from external customers located in Europe is analysed as follows:

| | **2006** | 2005 |
|---|---|---|
| | **$'000** | $'000 |
| France | **176,939** | 160,775 |
| United Kingdom | **118,023** | 116,737 |
| Germany | **156,069** | 131,500 |
| Other European countries | **252,272** | 226,901 |
| | **703,303** | 635,913 |

There is no major disparity in the ratios between turnover and profit in relation to the above geographical locations, hence no analysis is given of the profit contributions from the above geographical locations.

## 28 ACQUISITION OF ADDITIONAL EQUITY INTERESTS IN SUBSIDIARIES

### (a) Acquisition of additional equity interest in Varitronix Pengyuan Limited ("Varitronix Pengyuan")

On 22 March 2006, pursuant to the agreement with Tsinghua Holdings Corporation ("Tsinghua Holdings") signed on 8 November 2005, Varitronix Marketing acquired 49% equity interest in Varitronix Pengyuan, a then sino-foreign equity joint venture enterprise which was owned as to 51% by Varitronix Marketing and as to 49% by Tsinghua Holdings, at a total consideration of RMB40,000,000. As a result, the Group's equity interest in Varitronix Pengyuan increased from 51% to 100% effective on the same date. The premium on acquisition of minority interests of Varitronix Pengyuan amounting to $26,775,000 has been recognised directly in shareholders' equity. As further described in note 28(b), the Group's effective equity interest in Varitronix Pengyuan decreased from 100% to 90% on 19 July 2006 as a result of the transfer of the Group's 10% equity interest in Great Boom, the immediate holding company of Varitronix Pengyuan, to Harvest King.

### (b) Acquisition of additional equity interest in Varitronix Pengyuan Electronics

On 19 July 2006, pursuant to the agreement with Harvest King signed on 8 November 2005, the Company transferred, through Varitronix BVI, to Harvest King a 10% interest in the share capital of Great Boom, and Harvest King transferred to Varitronix Marketing its entire 20% equity interest in Varitronix Pengyuan Electronics on the same date. As a result, the Group's equity interest in Varitronix Pengyuan Electronics increased from 80% to 90% effective on the same date. The premium on acquisition of minority interests of Varitronix Pengyuan Electronics amounting to $3,546,000 has been recognised directly in shareholders' equity.

## 29 FINANCIAL INSTRUMENTS

Exposure to credit, liquidity and interest rate risks arises in the normal course of the Group's business. These risks are limited by the Group's financial management policies and practices described below.

### (a) Credit risk

The Group's credit risk is primarily attributable to accounts receivable and other receivables. Management has a credit policy in place and exposures to these credit risks are monitored on an ongoing basis.

Credit evaluations are performed on all customers requiring credit over a certain amount. Customers are generally granted credit terms of 30 - 90 days. Normally, the Group does not obtain collateral from customers.

Bank deposits and cash at bank are placed with reputable banks.

At the balance sheet date, the Group has a certain concentration of credit risk as 16% (2005: 28%) of the total accounts receivable and other receivables was due from the Group's five largest customers.

The maximum exposure to credit risk is represented by the carrying amount of accounts receivable and other receivables in the balance sheet.

## 29 FINANCIAL INSTRUMENTS (continued)

### (b) Liquidity risk

The Group's policy is to regularly monitor current and expected liquidity requirements and its compliance with lending covenants, to ensure that it maintains sufficient reserves of cash and adequate committed lines of funding from major financial institutions to meet its liquidity requirements in the short and longer term. The Company also monitors closely the cash flows of its subsidiaries. Generally, the Company's subsidiaries are required to obtain the Company's approval for activities such as investment of surplus cash, raising of loans and settlement of suppliers' invoices beyond certain limits.

### (c) Interest rate risk

Bank deposits and cash, and bank loans are the major types of the Group's financial instruments subject to interest rate risk. All financial instruments of the Group would be repriced before maturity.

The bank deposits and cash comprise mainly bank deposits with fixed interest rates ranging from 2.50% to 4.81% per annum and the maturity dates of these bank deposits are within 1 year.

The bank loans bear interest at 0.50% per annum over the 7-day HIBOR and are repayable within 1 year. Other details of the bank loans are set out in note 21.

### (d) Foreign currency risk

Forecast transactions

The Group is exposed to foreign currency risk primarily through sales and purchases that are denominated in a currency other than the functional currency of the operations to which they relate. The currencies giving rise to this risk are primarily Euros, United States dollars, Japanese Yen and Renminbi.

### (e) Fair values

No disclosure of fair value is required as all the Group's financial instruments are carried at amounts not materially different from their fair values as at 31 December 2006.

## 30 COMMITMENTS

### (a) Capital commitments representing purchase of property, plant and equipment not provided for in the financial statements were as follows:

| | The Group | |
|---|---|---|
| | **2006** | 2005 |
| | **$'000** | $'000 |
| Contracted for | **9,663** | 1,989 |

### (b) Other commitments

At 31 December 2006 in addition to the above, the Group had commitments to contribute capital of $Nil (2005: $38,400,000) for the acquisition of all the remaining interest, not held by the Group, in a non-wholly owned subsidiary in the PRC.

## 30 COMMITMENTS (continued)

(c) At 31 December 2006, the total future minimum lease payments under non-cancellable operating leases for properties are payable as follows:

| | 2006 $'000 | 2005 $'000 |
|---|---|---|
| Within 1 year | **4,728** | 3,836 |
| After 1 year but within 5 years | **4,351** | 2,685 |
| | **9,079** | 6,521 |

## 31 CONTINGENT LIABILITIES

### Financial guarantees issued

As at the balance sheet date, the Company has issued guarantees to banks in respect of a banking facility granted to certain subsidiaries.

As at the balance sheet date, the directors do not consider it probable that a claim will be made against the company under any of the guarantees. The maximum liability of the Company at the balance sheet date under the guarantees issued and the facility drawn down by the subsidiaries was $50,692,000 (2005: $99,992,000).

## 32 MATERIAL RELATED PARTY TRANSACTIONS

In addition to the transactions and balances disclosed elsewhere in these financial statements, the Group entered into the following material related party transactions.

### Key management personnel remuneration

Remuneration for key management personnel, including amounts paid to the Company's directors is disclosed in note 6 and certain of the highest paid employees is disclosed in note 7.

## 33 SUBSEQUENT EVENT

On 29 December 2006, the Standing Committee of the Tenth National People's Congress ("NPC") passed a resolution to submit the draft corporate income tax law to the Tenth NPC plenary session for voting. According to the income tax law that was passed by NPC on 16 March 2007, the PRC corporate income tax rate will be revised to 25% with effect from 1 January 2008. Since implementation measures on transitional policy of preferential tax rate granted according to current tax law and administrative regulations is not yet announced, the financial impact of the new tax law cannot be reasonably estimated at this stage.

## 34 POSSIBLE IMPACT OF AMENDMENTS, NEW STANDARDS AND INTERPRETATIONS ISSUED BUT NOT YET EFFECTIVE FOR THE ANNUAL ACCOUNTING PERIOD ENDED 31 DECEMBER 2006

Up to the date of issue of these financial statements, the HKICPA has issued the number of amendments, new standards and interpretations which are not yet effective for the accounting period ended 31 December 2006 and which have not been adopted in these financial statements.

The Group is in the process of making an assessment of what the impact of these amendments, new standards and new interpretations is expected to be in the period of initial application. So far it has concluded that the adoption of them is unlikely to have a significant impact on the Group's results of operations and financial position.

In addition, the following developments may result in new or amended disclosures in the financial statements:

| | | **Effective for accounting periods beginning on or after** |
|---|---|---|
| HKFRS 7 | Financial instruments: disclosures | 1 January 2007 |
| Amendment to HKAS 1 | Presentation of financial statements: capital disclosures | 1 January 2007 |