China Ocean Shipbuilding Industry Group Limited
中海船舶重工集團有限公司

(Incorporated in Bermuda with limited liability)

(Stock Code: 00651)

Annual Report

2012

Contents

Corporate Information

BOARD OF DIRECTORS

Executive directors:

Mr. Chau On Ta Yuen *(Chairman)*
Mr. Li Ming
(Deputy Chairman & Chief Executive Officer)
Mr. Zhang Shi Hong
Mr. Wang San Long

Independent non-executive directors:

Mr. Hu Bai He
Ms. Xiang Siying
Ms. Xiang Ying

COMPANY SECRETARY

Mr. Ngai Man Wo

AUDITOR

ZHONGLEI (HK) CPA Company Limited
Suites 313-317
3/F., Shui On Centre
6-8 Harbour Road, Wan Chai
Hong Kong

PRINCIPAL BANKERS

China Merchants Bank Co. Ltd.
Bank of Communications Co. Ltd
Chiyu Banking Corporation Ltd.

REGISTERED OFFICE

Clarendon House
2 Church Street
Hamilton HM 11
Bermuda

PRINCIPAL OFFICE

Units 1702-03,17/F
China Merchants Tower
Shun Tak Centre
168-200 Connaught Road Central
Hong Kong

PRINCIPAL SHARE REGISTRAR

HSBC Bank Bermuda Limited
Bank of Bermuda Building
6 Front Street, Hamilton HM11
Bermuda

BRANCH REGISTRAR IN HONG KONG

Tricor Abacus Limited
26th Floor, Tesbury Centre
28 Queen's Road East
Wanchai, Hong Kong

Chairman's Statement

Dear Shareholders,

On behalf of the board of director, I am pleased to present the annual report of China Ocean Shipbuilding Industry Group Limited (the "Company") and its subsidiaries (collectively the "Group") for the year ended 31 December 2012.

The Group recorded an audited consolidated turnover of approximately HK$1,870.30 million for the year ended 31 December 2012 when compared to turnover of approximately HK$1,660.25 million in 2011, an increase of 12.65% and loss attributable to the shareholders of approximately HK$344.10 million for the year ended 31 December 2012 when compared to HK$542.56 million in 2011, an decrease of 36.58%. The decrease in loss was mainly, among others, due to less impairment loss recognised in respect of property, plant and equipment during the year.

The year 2012 was still a very challenging year for the shipbuilding industry. The weak economic fundamentals, euro zone debt crisis, and reduced availability of shipping loans continued to have adversely impact on the shipbuilding market. Many small and medium sized shipbuilders in China had already disappeared since the downturn in the shipbuilding sector starting few years ago and others would follow. In such difficult market conditions, the Group negotiated with the ship-owners to ensure the successful delivery of vessels, continued to take cost control measures and actively seeking new orders. We hoped this will serve us well through the current challenging period.

In conclusion, I would like to thank all shareholders and staff for your continued support and look forward to improving the Group's performance.

CHAU On Ta Yuen
Chairman

28 March 2013

Management Discussion and Analysis

OVERVIEW

The Group is engaged in the production and operation of shipbuilding and securities trading business. During the year under review, the weak economic fundamentals, euro zone debt crisis, and reduced availability of shipping loans continued to have adversely impact on the shipbuilding market. The newbuilding prices remained at a low level after significant decline over the past few years. 2012 proved a very challenging year for the shipyards in China.

The Group had terminated the negotiation to acquire a company engaged in the production of electricity meters and abandoned the combined harvest project.

For the year ended 31 December 2012, the Group recorded a revenue of HK$1,870.30 million (2011: HK$1,660.25 million), an increase of approximately 12.65% over the year 2011 due to the improvement of production efficiency. The Group's gross loss slightly decreased from HK$41.48 million to HK$39.18 million. The Group continued to record a gross loss mainly because the appreciation of Renminbi and the shipbuilding prices still remained at a low level.

The Group recorded HK$12.36 million (2011: HK$16.54 million) of other income and a loss of HK$1.45 million (2011: gain of HK$4.71 million) of other gains and losses for the year ended 31 December 2012. The decrease in other income was mainly due to less interest income on bank deposits whereas the loss of other gains and losses was mainly resulting by the loss on written off of fixed assets.

The Group recorded a gain of HK$52.94 million on settlement of deferred consideration because the aggregated fair value of the convertible and promissory notes issued to settle deferred consideration was less than the carrying amount of the deferred consideration at the settlement date. The Group also recorded a loss of HK$20.95 million (2011: gain of HK$55.65 million) on modification and fair value change of convertible notes payable.

The Group recorded HK$90.62 million impairment loss recognised in respect of fixed assets (2011: HK$415.37 million) for the year ended 31 December 2012 after carrying revaluation of the assets by adopting value in use approach. The distribution and selling expenses cost of HK$1.65 million (2011: HK$1.58 million) in line with the increase of revenue. The administrative expenses of HK$97.13 million (2011: HK$83.42 million) were increased by 16.43%. The increase was mainly due to certain one-off expenses such as additional land tax, impairment of other receivables and costs relating to occupational safety.

The finance costs of the Group increased by 4.43 % to HK$182.10 million from HK$174.37 million. The high level of finance costs mainly due to the banks imposed a tighter credit policy on those in the shipbuilding sector by raising collateral requirements and both interest and non-interest rate charges. In addition, the Group also faced with higher costs on obtaining liquidity from other sources such as micro lending companies and suppliers. Besides, the Group also has HK$420 million notes payable which generated significant imputed interest expenses. The Group recorded HK$23.99 million (2011: HK$105.19 million) of tax credit. The decrease was due to less tax credit is arising from reversal of deferred taxation resulting from less impairment costs.

As at year end date, the trade receivables increased to HK$149.95 million (as at 31 December 2011: nil), primarily due to the increase of delivery of vessels during the year and the Group agreed to extend credit terms to a shipowner reflecting the continuing downtrend in the global shipbuilding industry. The Group has considered the long-term relationship with the shipowner and ensuring successfully delivery of vessels before agreeing to extend credit terms. The directors monitored the trade receivables closely.

To conclude, the loss for the year ended 31 December 2012 was amounting to approximately HK$344.10 million (2011: HK$542.56 million), it was decreased by 36.58% in comparing with year 2011.

SHIPBUILDING BUSINESS

During 2012, the shipbuilding segment was still performing at low level amid a lack of liquidity and new orders, unfavorable payment terms and pricing pressures imposed by the ship-buyers. During the year ended 31 December 2012, the shipbuilding business of the Group generated revenue of approximately HK$1,870.30 million to the Group, representing an increase of approximately 12.65% as compared to approximately HK$1,660.25 million in 2011. The increase in revenue mainly represented an improvement in production efficiency which offsetting the newbuilding prices declined. The shipbuilding business recorded a loss before tax of HK$109.68 million *(before deducting impairment cost recognized in fixed assets and finance costs)* (2011: HK$94.91 million *(before deducting impairment cost recognized in fixed assets and finance costs)*). The increase of loss was mainly due to the appreciation of Renminbi and the decline in shipbuilding market.

During the year, the Group had delivered eleven vessels including three chemical tankers, two multi-purposes vessels and six heavy lift vessels to ship-owners and also signed a contract of constructing four multi-purposes vessels with an option of additional two. As at 31 December 2012, the secured order book comprised seven heavy lift vessels. During the period from the year end date to the date of this report, the Group delivered one heavy lift vessel to a ship owner and secured one multi-purposes vessel with an option of additional one, in addition, the six multi-purposes vessels would become effective if the ship owner could obtain financial support from its banks. Besides, certain new orders which are currently being close negotiated.

TRADING BUSINESS

For the year ended 31 December 2012, the trading business recorded an insignificant loss (2011: HK$0.26 million). The Group discontinued the metal trading business but continued its trading business.

LIQUIDITY AND FINANCIAL RESOURCES

As at 31 December 2012, the Group had bank balances and cash (including pledged bank deposits) of approximately HK$309.30 million (31 December 2011: HK$511.35 million) of which HK$269.45 million (31 December 2011: HK$360.84 million) was pledged; short term borrowings of HK$608.01 million (31 December 2011: HK$538.12 million); long term borrowings of HK$31.08 million (31 December 2011: HK$68.97 million); long term convertible notes payable amounted to approximately HK$278.63 million (31 December 2011: HK$157.14 million) represented the fair value of principal amount of HK$330.00 million (31 December 2011: HK$225.00 million). The gearing ratio defined as non-current liabilities and short term borrowing divided by total shareholders' equity was (1.49) as at 31 December 2012 (31 December 2011: (2.19)).

SEGMENT INFORMATION

The segment information for the Group for the year ended 31 December 2012 is set out in Note 8 to the consolidated financial statements from page 78 to 84.

CHARGES ON GROUP ASSETS

As at 31 December 2012, HK$302.45 million (31 December 2011: HK$393.31 million) of deposits, HK$50.91 million (31 December 2011: HK$156.62 million) of inventories, HK$563.96 million (31 December 2011: HK$399.63 million) of property, plant and equipment, HK$335.14 million (31 December 2011: 341.03 million) of prepaid lease payment and HK$148.23 million (31 December 2011: HK$258.94 million of value-added tax recoverable, were pledged to banks for other borrowings and banking facilities granted by banks to the Group. The pledge on the bank deposits will be released upon the settlement of relevant bills payables.

EXPOSURE TO FLUCTUATIONS IN EXCHANGE RATES AND ANY RELATED HEDGES

The income and expenditure of the Group were denominated in Renminbi, Hong Kong Dollars and United States Dollars. As at 31 December 2012, the Group did not hedge its exposure to foreign exchange risk profile as the Group could not find a suitable tool to manage this exposure. The Board will continue to consider the appropriate hedging measures.

NEW BUSINESS, MATERIAL ACQUISITIONS AND DISPOSALS

There was no new business, material acquisitions and disposals of subsidiaries and associated companies during the year under review.

SUBSEQUENT EVENTS

Significant events after the end of the reporting period are set out in Note 46 to the financial statements on page 132.

LITIGATION

Jiangxi Jiangzhou Union Shipbuilding Co. Ltd (the "Shipyard"), a wholly owned subsidiary of the Company, with Sloman Neptun Schiffahrts-Aktiengesellschaft (the "Sloman") had an arbitration process related to the refund of instalments paid including interests, amounting to approximately US$73 million, on contracts to build three chemical tankers. In November 2011, Sloman and Shipyard have reached new agreements to reinstate all the contracts in arbitration with revised terms. According to the terms of agreements, the vessels in arbitration had been delivered to Sloman in June 2012. After that, the arbitration proceeding with Sloman was fully settled. The Group considered that there was no material adverse financial impact to the results of the Group in 2012.

As at the date of this report, Shipyard has an arbitration proceeding in progress with a ship-buyer, namely Algoma Tankers International Inc. (the "Algoma") over the validity of rescission notices. Algoma sent the rescission notices to the Shipyard on the ground that the Shipyard failed to meet the delivery date in relation to a third-party sister ship. It requested for the refund of instalments paid including interests, amounting to approximately US$40 million, on contracts to build three chemical tankers. The hearing had completed in September 2012 in England. Up to the latest practicable date of preparing this report, the arbitration panel has not yet rendered a decision in this matter but the ruling was expected to be made in 2013.

The outcome of arbitration proceedings is uncertain. If the Shipyard wins the arbitration, the Shipyard may stand to receive a compensation for the loss (including potential gains on the execution of contracts) arising from the cancellation, while if the Shipyard loses the arbitration, the Shipyard may be required to refund of the installments paid for shipbuilding, its related interests and legal fees to Algoma. For the sake of prudence, the Group classified the refund of deposits and its estimated interest under current liabilities in the financial statements. The Group considered that there has already reflected the unfavourable outcomes of the arbitration, if any.

Save as disclosed above, no member of the Group was engaged in any litigation or arbitration or claim of material importance.

HUMAN RESOURCES

The Group had around 1,110 employees as at 31 December 2012. It has been the Group's policy to ensure that the pay levels of its employees are rewarded on a performance related basis within the general framework of the Group's salary and bonus system. The Group has participated in a mandatory provident fund scheme for its employees based in Hong Kong. Shares options may also be granted to eligible persons of the Group.

RELATED PARTY TRANSACTIONS

Significant balances with related parties and related party transactions entered into by the Group during the year ended 31 December 2012 are disclosed in Note 43 to the financial statements on pages 127 and 128.

RETIREMENT SCHEME

The Group's Hong Kong employees participate in a mandatory provident fund scheme. Particulars of this retirement scheme are set out in Note 40 to the financial statements on pages 124 and 125.

CONTINGENT LIABILITIES

Particulars of the Group's contingent liabilities as at 31 December 2012 are set out in Note 41 to the financial statements on pages 125 and 126.

CAPITAL COMMITMENTS

Particulars of the Group's capital commitments as at 31 December 2012 are set out in Note 37 to the financial statements on page 120.

PROSPECTS

The shipbuilding market will continue to suffer from a lack of ordering activities and liquidity. A difficult operating environment is expected to continue in 2013. The Group is expected to witness continued global overcapacity and weakness in the shipbuilding financing market. It is likely that there will be integration of existing capacities in the industry through mergers and acquisitions among the shipbuilders in China. To face this difficult market condition, the Group will continue to strengthen its internal control, enhance efficiency and seeking new orders. The directors expect that a certain amount of new orders will be placed in the coming months but the construction works for new orders would not commence immediately. It seems will have a time gap for the yard to work at its full capacity in mid 2013.

In order to enhance the overall performance of the Group, the Group is actively re-evaluating its existing business operations by examining diversification. The Directors will continue to reinforce the Group's financial position so that the Group will be well placed when the recovery begins.

Report on Corporate Governance

The Group has recognized the importance of transparency and accountability, and the Board believes that shareholders can be benefited from good corporate governance. The Company aims to achieve good standard of corporate governance. The Company has complied with the code provisions as set out in Appendix 14 of the Rules Governing the Listing of Securities ("Listing Rules") on The Stock Exchange of Hong Kong Limited ("Stock Exchange").

The Board of Directors

The Board's primary responsibilities are to formulate the Company's long-term corporate strategy, to oversee the management and to evaluate the performance of the Group.

The Board meets regularly throughout the year to discuss the overall strategy as well as the operation and financial performance of the Group.

When the Board considers any material transaction in which a substantial shareholder or a Director has a conflict of interest, a board meeting is held and Independent Non-executive Directors who have no material interest in the transaction will be present at such board meeting. At the meeting, the Director who has an interest in the transaction is required to abstain from voting.

Every Director shall ensure that he/she can contribute sufficient time and effort to the corporate affairs of the Company once he/she accepts the appointment.

The number of general meetings and Board meetings held during the year ended 31 December 2012 and the Directors' respective attendance record are summerized as follows:

Name	Number of board meetings attended	Numbers of general meetings attended
Executive directors:		
Mr. Chau On Ta Yuen *(Chairman)*	12/12	1/1
Mr. Li Ming *(Deputy Chairman and CEO)*	12/12	1/1
Mr. Zhang Shi Hong	12/12	1/1
Mr. Wang San Long	12/12	1/1
Independent non-executive directors:		
Mr. Hu Bai He	7/12	1/1
Ms. Xiang Siying	7/12	0/1
Ms. Xiang Ying	7/12	1/1

Chairman and Chief Executive Officer

The Board appointed Mr. Chau On Ta Yuen as the Chairman, who is responsible for the leadership and effective running of the Board to achieve its primary responsibilities. With the support of the executive directors, the Chairman seeks to ensure that all directors are properly briefed on issues arising at board meetings and that all directors receive adequate and reliable information on a timely manner. The Chairman also encourages Directors to be fully engaged in the Board's affair and make contribution in performing the Board's functions. The position of Chief Executive Officer is vested with executive responsibilities over the business directions and operational decisions of the management and performance of the Group.

Board Composition

The Board comprises four executive directors and three independent non-executive directors as at the date of this report. The independent non-executive directors constitute over one-third of the Board. In addition, one of the independent non-executive directors possesses appropriate accounting qualifications and financial management expertise. The Directors are considered to have a balance of knowledge and experience appropriate for the requirements of the business of the Group. The independent non-executive directors serve the important function of ensuring and monitoring the basis of an effective corporate governance framework. The Board considers that each independent non-executive director is independent in character and judgment and that they all meet the specific independent criteria as required by the Listing Rules.

Independence of Independent Non-executive Directors

Pursuant to the requirement of the Rule 3.13 of the Listing Rules, the Board confirmed that the Company has received written confirmation from each of all three independent non-executive directors of their independence and considers them to be independent throughout the year.

Terms of appointment of Non-executive Directors

Each of the Independent Non-executive directors is appointed for an initial term of not more than two years commencing from his/her date of appointment and is renewable successively for a term of two years until termination. He/She is subject to retirement by rotation and re-election by shareholders at annual general meeting in accordance with the Bye-laws.

Model Code for Directors' Securities Transaction

The Company has adopted the Model Code for Securities Transactions by Directors of Listed Companies (the "Model Code") set out in Appendix 10 of the Listing Rule regarding Directors' securities transactions. Based on specific enquiry of all the Directors of the Company, the Directors have complied with the required standard as set out in the Model Code for the year ended 31 December 2012.

Nomination Committee

The Company set up a Nomination Committee on 28 March 2012 to ensure that there are fair and transparent procedures for the appointment, re-election and removal of directors to the Board. The Nomination Committee comprises the Chairman of the Board and three independent non-executive directors, namely, Mr. Chau On Ta Yuen, Mr. Hu Bai He, Ms. Xiang Siying and Ms. Xiang Ying. The Chairman of the Nomination Committee is Ms. Xiang Ying. The terms of reference of the Nomination Committee are consistent with the terms set out in the Code. The nomination of directors should take into consideration of the nominee's qualification, experience, ability and potential contributions to the Company.

One meeting was held during the year ended 31 December 2012. All members attended the meeting. The members of the Nomination Committee reviewed the directors' details and access the independence of all independent non-executive directors. They satisfied the structure, size and composition (including the skills, knowledge and experience) of the Board and the independence of independent non-executive directors.

Remuneration Committee

The Company has set up the Remuneration Committee to ensure that there are formal and transparent procedures for setting up policies on the remuneration of the Directors and senior management. The revised terms of reference of the Remuneration Committee were adopted by the Board on 28 March 2012 and were consistent with the terms set out in the Code. The Remuneration Committee comprises three independent non-executive directors, Mr. Hu Bai He, Ms. Xiang Siying and Ms. Xiang Ying and one executive director, Mr. Li Ming. The Chairman of the Remuneration Committee is Ms. Xiang Ying.

One meeting was held during the year ended 31 December 2012. All members attended the meeting. They made recommendation to the Board regarding the Company's remuneration policy and the remuneration package of all directors (excluding his own remunerations) of the Company. No Director was involved in deciding his own remuneration during the year under review.

Audit Committee

The Company established an Audit Committee with reference to "A Guide for the Formation of an Audit Committee" published by the Hong Kong Institute of Certified Public Accountants. The revised terms of the Audit Committee were adopted by the Board on 28 March 2012 and were consistent with the terms set up in the Code.

The Audit Committee comprises three independent non-executive directors, and the chairman of the Audit Committee, Mr. Hu Bai He, possesses a professional accountancy qualification and has substantial experience in accounting and financial matters.

The principal duties of the Audit Committee include the review and supervision of the Group's financial reporting system, financial statements and internal control procedures.

Five meetings were held during the year ended 31 December 2012. The individual attendance of each member is set out below:

Name of member	Number of committee meetings attended
Mr. Hu Bai He	5/5
Ms. Xiang Siying	5/5
Ms. Xiang Ying	5/5

The Group's interim report of the six months to 30 June 2012 and the annual report for the year ended 31 December 2012 had been reviewed by the Audit Committee and recommendation was provided to the Board for approval.

Auditor's Remuneration

For the year ended 31 December 2012, the auditors of the Company received approximately HK$1,000,000 for audit services and HK$180,000 for other services.

Directors' Responsibility for the Financial Statements

The Directors acknowledge their responsibility for preparing the financial statements of the Group in accordance with statutory requirements and applicable accounting standards.

The Directors, having made appropriate enquiries, consider that the Group has adequate resources to continue in operational existence for the foreseeable future and that, for this reason, it is appropriate to adopt the going concern basis in preparing the financial statements.

Corporate Governance function

In order to achieve enhanced corporate governance of the Company, the Board has undertaken constant review of the policies for corporate governance of the Company, the training and continuous professional development of Directors and senior management, the Company's policies and practices on compliance with legal and regulatory requirements. During this year, the Board performed the duties relating to corporate governance matters such as adoption of a whistleblowing policy and appointed external professionals to carry out internal control review.

Directors' training and professional development

Directors are continually updated on the latest development and changes in the Listing Rules, the Code and other regulatory requirements in order to ensure the compliance with the same by the Directors. Directors are also encouraged to participate in professional development courses and seminars to develop and refresh their knowledge and skills. All Directors had provided a record of training they received during the year to the Company. According to the training records provided by the Directors, the training attended by them during the reporting period is summarized as follows:

Directors	Corporate Governance, regulatory development and training on other relevant topics
Mr. Chau On Ta Yuen	✓
Mr. Li Ming	✓
Mr. Zhang Shi Hong	✓
Mr. Wang San Long	✓
Mr. Hu Bai He	✓
Ms. Xiang Siying	✓
Ms. Xiang Ying	✓

Internal Control

The Board is responsible for managing business and operational risks and maintaining a proper and effective system of internal control to safeguard the shareholders' investment and the Group's assets. During the year, the directors appointed external professional to conduct an annual review of the effectiveness of the Group's system of internal control covering financial, operational and compliance controls.

Communication with Shareholders and Shareholders' right

The Company recognizes the importance of good communications with all shareholders and investors. The Company's annual general meeting is a valuable forum for the Board to communicate directly with the shareholders. All shareholders of the Company are given a minimum of 21 days' notice of the date and venue of such annual general meeting. Shareholders are encouraged to attend shareholders' meetings. The Chairman and/or the Directors are available to answer questions on the Group's businesses at the meetings. The Company provides information relating to the Company and its business in its annual and half-yearly report and also disseminates such information electronically through its website at "www.irasia.com/listco/hk/chinaoceanshipbuilding" and the website of the Stock Exchange.

As one of the measures to safeguard shareholders' interests and rights, separate resolutions are proposed at shareholders' meetings on each substantial issue, including the election of individual Directors, for shareholders' consideration and voting. All resolutions put forward at shareholders' meetings will be voted by poll pursuant to the Listing Rules.

Memorandum of Association and Bye-laws of the Company

During the reporting period, no amendment had been made to the Memorandum of Association and Bye-Laws of the Company.

On behalf of the Board

Zhang Shi Hong
Director
28 March 2013

Directors' Report

The directors present their annual report and the audited consolidated financial statements of the Company and its subsidiaries (hereinafter collectively referred to as the "Group") for the year ended 31 December 2012.

PRINCIPAL ACTIVITIES

The Company is an investment holding company. The principal activities of its subsidiaries are set out in Note 45 to the consolidated financial statements on page 131.

RESULTS

The results of the Group for the year ended 31 December 2012 are set out in the consolidated statement of comprehensive income on page 28 of the annual report.

DIVIDENDS

The directors do not recommend the payment of a dividend.

RESERVES

Movements in the reserves of the Group during the year are set out on pages 31 and 32 of the annual report.

PROPERTY, PLANT AND EQUIPMENT

Details of movements during the year in property, plant and equipment of the Group are set out in Note 17 to the consolidated financial statements on pages 90 and 91.

SHARE CAPITAL

Details of movements in share capital of the Company during the year are set out in Note 33 to the consolidated financial statements on page 110.

BORROWINGS

Particulars of the Group's borrowings as at 31 December 2012 are set out in Note 30 to the consolidated financial statements from page 104 to 107.

DISTRIBUTABLE RESERVES OF THE COMPANY

The Company did not have any reserves available for distribution (2011: Nil).

Under the Companies Act 1981 of Bermuda (as amended), the balances in a company's contributed surplus and share premium accounts are available for distribution. However, the company cannot declare or pay a dividend, or make a distribution out of contributed surplus and share premium accounts if:

(a) the company is, or would after the payment be, unable to pay its liabilities as they become due; or

(b) the realisable value of the assets of the company would thereby be less than the aggregate of its liabilities and its issued share capital and share premium accounts.

FIVE YEAR FINANCIAL SUMMARY

A summary of the results and of the assets and liabilities of the Group for the last five financial years is set out on page 133 of the annual report.

DIRECTORS

The directors of the Company during the year and up to the date of this report were:

Executive directors:
Mr. Chau On Ta Yuen – *Chairman*
Mr. Li Ming – *Deputy Chairman and Chief Executive Officer*
Mr. Zhang Shi Hong
Mr. Wang San Long

Independent non-executive directors:
Mr. Hu Bai He
Ms. Xiang Siying
Ms. Xiang Ying

In accordance with Clause 87 of the Company's Bye-laws, Mr. Li Ming, Mr. Hu Bai He and Ms. Xiang Ying will retire by rotation and are eligible for re-election at the forthcoming annual general meeting.

All of the remaining directors will continue in office.

BIOGRAPHICAL DETAILS OF DIRECTORS

Brief biographical details of directors as at the date of this report are set out below:

Executive Directors

Mr. Chau On Ta Yuen, aged 65, was appointed as a Director in September 2007 and is the Chairman of the Group. Mr. Chau graduated from Xiamen University majoring in Chinese Language and literature. He is currently an independent non-executive director of Good Fellow Resources Limited, Come Sure Group (Holdings) Limited and Sumpo Food Holdings Limited, the shares of which are listed on the Main Board of the Stock Exchange of Hong Kong Limited (the "Stock Exchange"). From December 2008 to September 2010, Mr. Chau was an independent non-executive director of Buildmore International Limited, the shares of which are listed on the Main Board of the Stock Exchange. From June 2003 to August 2009, Mr. Chau was an independent non-executive director of Everpride Biopharmaceutical Company Limited (now known as Hao Wen Holdings Limited), the shares of which are listed on the Growth Enterprise Market of the Stock Exchange. From March 2000 to November 2006, he was appointed as an executive director and the vice chairman of Everbest Century Holdings Limited (now known as Dynamic Energy Holdings Limited), the shares of which are listed on the Main Board of the Stock Exchange. Mr. Chau is currently a member of the Chinese People Political Consultative Conference of the People's Republic of China and duputy officer of the Social and Legal Affairs Committee of the Chinese People Political Consultative Conference. He is also the vice chairman of Hong Kong Federation of Fujian Associations.

Mr. Li Ming, aged 50, was appointed as a Director in February 2009 and is the Deputy Chairman and Chief Executive Officer of the Group. Mr. Li graduated from Jiangxi Finance Institute (now known as Jiangxi University of Finance & Economics) majoring in planning statistics. Prior to joining the Company, Mr. Li held senior positions in a number of well-known companies in the People's Republic of China and had extensive experience in management and business planning Mr. Li is currently an executive director of Shenzhen Microgate Technology Co. Ltd., the shares of which are listed on the Shenzhen Stock Exchange. During the period from 3 September 2002 to 5 October 2007, he was appointed as a non-executive director of Ningbo Yidong Electronic Company Limited, the shares of which are listed on the Growth Enterprise Market of the Stock Exchange.

Mr. Zhang Shi Hong, aged 44, was appointed as a Director in December 2007. Mr. Zhang has over 16 years of experience in finance, credit management and investment management. He has worked for the head office of the Bank of China for around nine years and was mainly responsible for credit management. He also pursued investment management in various corporations in the People's Republic of China. Mr. Zhang holds a Master's degree in Economics.

Mr. Wang San Long, aged 62, was appointed as a Director in May 2008. Mr. Wang has more than thirty years experience in the field of ship-building. He is a senior engineer and was graduated from ship-building department of Huazhong Gong Xue Yuan (now known as Huazhong University of Science and Technology). Mr. Wang is a member of Changjiang Committee in China Classification Society. He is also a member of teaching guidance committee of ship engineering department in Jiujiang Vocational and Technical College. Mr. Wang is currently the chairman of one of the subsidiary of the Company, namely Jiangxi Jiangzhou Union Shipbuilding Co., Ltd.

Independent Non-Executive Directors

Mr. Hu Bai He, aged 50, appointed as an independent non-executive Director in May 2008. Mr. Hu was graduated from Jiangxi University of Finance & Economics. He is a senior accountant, certified public accountant, certified public valuer and certified tax agent in the People's Republic of China (the "PRC"). He has extensive experience in finance and accounting field. Mr. Hu is currently the general manager of Peking Certified Public Accountants. Before he joined Peking Certified Public Accountants in 1993, he has had over seven years working experience with Ministry of Finance the PRC.

Ms. Xiang Siying, aged 50, was appointed as an independent non-executive Director in May 2008. Ms. Xiang holds an MBA degree from the London Business School. She has extensive experience in all sectors of corporate finance, restructuring and merge and acquisitions practice. Ms. Xiang currently is an executive director of CDH Investments, a leading private equity firm in China. Prior to joining CDH, she had worked for China International Capital Corporation Limited since returning to China in early 2004. Before that Ms. Xiang had long career with International Finance Corporation, the private investment arm of the World Bank Group, in Washington, United States of America.

Ms. Xiang Ying, aged 58, was appointed as an independent non-executive Director in August 2009. Ms. Xiang was graduated and obtained her Bachelor's Degree in Economics from Zhongnan University of Economics and Law. Ms. Xiang is a qualified lawyer and a certified public accountant in the People's Republic of China. She also holds qualifications to act as a senior lecturer in Economic Law. Ms. Xiang has significant experience in the fields of mergers and acquisitions, financial services and risk management. During the period from 31 August 2011 to 25 November 2012, she was appointed as an independent non-executive director of Anxin Trust & Investment Co. Ltd., the shares of which are listed on the Shanghai Stock Exchange. Ms. Xiang is currently an independent director of Guangdong Sky Dragon Ink Group Co. Ltd, the shares of which are listed on Shenzhen Stock Exchange.

DIRECTORS' INTERESTS IN SHARES AND UNDERLYING SHARES

As at 31 December 2012, the interests of the directors in the share capital of the Company or its associated corporations, as defined in Part XV of the SFO and as recorded in the register required to be kept by the Company under Section 352 of the SFO, or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers (the "Model Code") were as follows:

(i) Interest in ordinary shares of the company

Name	Long/Short position	Capacity	Number of ordinary shares held	Approximate percentage of the issued shares held
Li Ming	Long position	Beneficial owner	243,632,500	6.64%
	Long position	Interest of controlled Corporation	31,775,000*	0.87%
	Long position	Beneficial owner and Interest of controlled Corporation	275,407,500	7.51%

* These shares are held by Lead Dragon Limited, a company incorporated in the British Virgin Islands whose entire issued share capital is solely and beneficially owned by Mr. Li Ming.

(ii) Rights to acquire shares in the company

As at 31 December 2012, the directors of the Company had interests in share options to subscribe for shares in the Company granted as follows:

Name of Director	Company/ name of associated corporation	Nature of interest	Number of ordinary shares	Exercise price
Chau On Ta Yuen	Company	Personal interest (Note 1)	4,743,000	HK$5.693
Zhang Shi Hong	Company	Personal interest (Note 1)	1,581,000	HK$5.693
Wang San Long	Company	Personal interest (Note 2)	4,110,600	HK$4.523

Notes:

1. Such number of Shares represents the underlying shares of the options granted on 5 March 2008 under the share option scheme of the Company adopted on 27 May 2002 ("2002 Scheme").

2. Such number of Shares represents the underlying shares of the options granted on 7 May 2008 under the 2002 Scheme.

Save as disclosed in this report, none of the Directors or their associates had any personal, family, corporate or other interests in the equity or debt securities of the Company or any of its associated corporations.

SHARE OPTION SCHEMES

Particulars of the Company's share option schemes adopted on 27 May 2002 (the "2002 Scheme") and on 27 June 2012 (the "2012 Scheme") as at 31 December 2012 are set out in Note 39 to the consolidated financial statements.

DIRECTORS' INTERESTS IN CONTRACTS OF SIGNIFICANCE

Save as the information disclosed in Note 43 to the consolidated financial statements, no contract of significance to which the Company or its subsidiaries was a party and in which a director of the Company had a material interest, whether directly or indirectly, subsisted at the end of the year or at any time during the year.

DIRECTORS' SERVICE CONTRACTS

None of the directors of the Company for re-election at the forthcoming annual general meeting has service contract with the Company or any of its subsidiaries, which is not determinable by the employer within one year without payment of compensation, other than statutory compensations.

SUBSTANTIAL SHAREHOLDERS

As at 31 December 2012, save as disclosed below, no persons, not being a Director or chief executive of the Company, had interests or short positions in the shares and underlying shares of the Company as recorded in the register (the "Register") maintained by the Company pursuant to Section 336 of the SFO. Other than as disclosed below, the Company has not been notified of any other interest or short positions in the shares and underlying shares of the Company as at 31 December 2012.

Name	Long/Short position	Capacity	Number of ordinary shares held	Number of underlying share held	Approximate percentage of the issued shares held at 31 December 2012
Di Yu Fei	Long	Beneficial owner	0	409,090,909	11.15%
Li Jun	Long	Beneficial owner	7,340,297	386,133,333	10.73%
Yang Li	Long	Beneficial owner	150,590,535	204,545,454	9.68%

EMOLUMENT POLICY

The emolument policy of the employee of the Company is set up by the executive directors on the basis of their merit, qualifications and competence.

The emoluments of the directors of the Company are decided by the Board of Directors, having regard to their responsibility to the Company, their qualifications, experiences and past remuneration, the Company's performance and current market situation. The Company has adopted share option schemes as an incentive to directors and eligible employees, details of the schemes are set out in Note 39 to the consolidated financial statements.

PURCHASE, SALE OR REDEMPTION OF THE COMPANY'S LISTED SECURITIES

Neither the Company nor any of its subsidiaries purchased, sold or redeemed any of the Company's listed securities during the year.

MAJOR CUSTOMERS AND SUPPLIERS

The aggregate amount of purchase attributable to the Group's largest supplier and five largest suppliers taken together accounted for 13% and 46%, respectively, of the Group's total purchase for the year.

The aggregate amount of turnover attributable to the Group's largest customer and five largest customers taken together accounted for 96% and 100%, respectively of the Group's total turnover for the year.

None of the directors, their associates or shareholders of the Company (which to the knowledge of the directors own more than 5% of the Company's issued share capital) has an interest in any of the Group's largest supplier and customer.

PRE-EMPTIVE RIGHTS

There are no provisions for pre-emptive rights under the Company's Bye-laws or the laws of Bermuda, which would oblige the Company to offer new shares on pro-rata basis to existing shareholders.

CORPORATE GOVERNANCE

The Group has recognized the importance of transparency and accountability, and the Board believes that shareholders can be benefited from good corporate governance. The Company aims to achieve good standard of corporate governance. The Company has complied with most of the code provisions as set out in Appendix 14 of the Rules Governing the Listing of Securities ("Listing Rules") on The Stock Exchange of Hong Kong Limited ("Stock Exchange"). Further information on the Company's corporate governance practice is set out in the Corporate Governance Report on pages 9 to 14.

SUFFICIENCY OF PUBLIC FLOAT

Based on the information that is publicly available to the Company and within the knowledge of the Directors, as at the date of this report, there is sufficient public float of not less than 25% of the Company's issued shares as required under the Listing Rules.

AUDITORS

At a board meeting of the Company convened on 17 January 2012, ZHONGLEI (HK) CPA Company Limited was appointed as the auditors of the Company. The financial statements had been audited by ZHONGLEI (HK) CPA Company Limited who will retire and, being eligible, offer themselves for re-appoint. A resolution will be submitted to the annual general meeting to re-appointment Messrs. ZHONGLEI (HK) CPA Company Limited as auditors of the Company.

On behalf of the Board

CHAU On Ta Yuen
Chairman
Hong Kong,
28 March 2013

中磊（香港）會計師事務所有限公司
ZHONGLEI (HK) CPA Company Limited

TO THE MEMBERS OF
CHINA OCEAN SHIPBUILDING INDUSTRY GROUP LIMITED
中海船舶重工集團有限公司
(incorporated in Bermuda with limited liability)

We have audited the consolidated financial statements of China Ocean Shipbuilding Industry Group Limited (the "Company") and its subsidiaries (collectively referred to as the "Group") set out on pages 28 to 132, which comprise the consolidated statement of financial position as at 31 December 2012, and the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

DIRECTORS' RESPONSIBILITY FOR THE CONSOLIDATED FINANCIAL STATEMENTS

The directors of the Company (the "Directors") are responsible for the preparation of consolidated financial statements that give a true and fair view in accordance with Hong Kong Financial Reporting Standards issued by the Hong Kong Institute of Certified Public Accountants and the disclosure requirements of the Hong Kong Companies Ordinance, and for such internal control as the directors determine is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

AUDITOR'S RESPONSIBILITY

Our responsibility is to express an opinion on these consolidated financial statements based on our audit and to report our opinion solely to you, as a body, in accordance with Section 90 of the Bermuda Companies Act, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report. Except as described in the Basis for Disclaimer of Opinion paragraphs, we conducted our audit in accordance with Hong Kong Standards on Auditing issued by the Hong Kong Institute of Certified Public Accountants. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

However, because of the matters described in the Basis for Disclaimer of Opinion paragraphs, we were not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

BASIS FOR DISCLAIMER OF OPINION

(a) Limitation of scope on prior year's scope limitation affecting comparative figures and related disclosures

As explained in our report dated 30 March 2012 on the Group's consolidated financial statements for the year ended 31 December 2011, we were not provided with sufficient evidence to enable us to assess as to whether the impairment loss recognised in respect of property, plant and equipment and prepaid lease payments included in the consolidated statement of comprehensive income of the Group for the year ended 31 December 2011 were free from material misstatements. We qualified our opinion on the Group's consolidated financial statements for the year ended 31 December 2011 in respect of this scope limitation accordingly.

Any adjustments that might have been found necessary in respect of the above would have had a consequential impact on the Group's results for the year ended 31 December 2011 and the related disclosures made in the consolidated financial statements.

(b) Limitation of scope on the impairment assessment of trade receivables

As disclosed in Note 22(a) to the consolidated financial statements, included in the Group's trade receivables, net of allowance for doubtful debts, of approximately HK$149,950,000 (equivalent to USD19,000,000) as at 31 December 2012 was due from a ship buyer, an independent third party of the Group, in relation to the final payment for the acquisition of seven vessels from the Group. During the year ended 31 December 2012, the revenue derived from this ship buyer was approximately HK$1,771,718,000. The Directors are of the view that the Group is able to recover the outstanding balance due from that ship buyer, and therefore no impairment had been provided on such balance. However, we were unable to obtain sufficient appropriate audit evidence we consider necessary in order to assess whether such receivable could be recovered in full or to determine the amount of impairment, if any. There were no practical alternative audit procedures that we could perform to satisfy ourselves as to any impairment loss had been occurred against this receivable as at 31 December 2012.

Any adjustments to the amount of the above trade receivables found to be necessary would affect the Group's net liabilities as at 31 December 2012 and the Group's loss for the year then ended and related note disclosures to the consolidated financial statements.

(c) Material fundamental uncertainties relating to going concern basis

As set out in the consolidated statement of comprehensive income, the Group incurred gross loss and loss for the year attributable to owners of the Company of approximately HK$39,179,000 and HK$344,101,000 respectively, for the year ended 31 December 2012. Besides, as set out in Note 2 to the consolidated financial statements, in addition to a number of operational issues, the Group's current liabilities exceeded its current assets by approximately HK$1,328,972,000 and the Group had net liabilities of approximately HK$723,074,000 as at 31 December 2012.

As set out in Note 2 to the consolidated financial statements, the Directors have been implementing various operating and financing measures to improve the Group's operating and financial position. The validity of the going concern assumption on which the consolidated financial statements are prepared is dependent on the favourable outcomes of those operating and financing measures being implemented by the Directors. The consolidated financial statements have been prepared on the assumption that the Group will continue as a going concern and therefore do not include any adjustments relating to the realisation and reclassification of non-current assets and non-current liabilities that may be necessary if the Group is unable to continue as a going concern.

Should the going concern assumption be inappropriate, adjustments may have to be made to reflect the situation that assets may need to be realised at other than the amounts at which they are currently recorded in the consolidated statement of financial position. In addition, the Group may have to provide for further liabilities that might arise, and to reclassify non-current assets and non-current liabilities as current assets and current liabilities respectively.

Due to the potential interaction of the above material uncertainties and their possible cumulative effect on the consolidated financial statements, we have not been able to form an opinion on the consolidated financial statements.

DISCLAIMER OF OPINION

Because of the significance of the matters described in the Basis for Disclaimer of Opinion paragraphs, we have not been able to form an opinion on the consolidated financial statements for the year ended 31 December 2012. In all other respects, in our opinion, the consolidated financial statements have been properly prepared in accordance with the disclosure requirements of the Hong Kong Companies Ordinance.

ZHONGLEI (HK) CPA Company Limited
Certified Public Accountants (Practising)
Chan Mei Mei
Practising Certificate Number: P05256

Suites 313-317, 3/F., Shui On Centre
6-8 Harbour Road
Wan Chai
Hong Kong

28 March 2013

Consolidated Statement of Comprehensive Income

For the year ended 31 December 2012

	Notes	2012 HK$'000	2011 HK$'000 (Restated)
Revenue	8	**1,870,304**	1,660,254
Cost of sales		**(1,909,483)**	(1,701,733)
Gross loss		**(39,179)**	(41,479)
Other income	9	**12,362**	16,538
Other gains and losses	10	**(1,448)**	4,708
Change in fair value of investments held for trading		**(320)**	(1,188)
Impairment loss recognised in respect of property, plant and equipment	17	**(90,617)**	(415,365)
Selling and distribution expenses		**(1,651)**	(1,580)
Administrative expenses		**(97,128)**	(83,419)
Gain on settlement of deferred consideration	32	**52,936**	–
Gain on modification of convertible notes payable	34	**–**	4,262
(Loss) gain on fair value change of convertible notes payable	34	**(20,949)**	51,389
Loss on extinguishment of convertible notes payable	34	**–**	(7,241)
Finance costs	11	**(182,100)**	(174,370)
Loss before tax	12	**(368,094)**	(647,745)
Income tax credit	13	**23,993**	105,186
Loss for the year attributable to owners of the Company		**(344,101)**	(542,559)
Exchange differences arising on translation		**(4,550)**	2,288
Total comprehensive expenses for the year attributable to owners of the Company		**(348,651)**	(540,271)
Loss per share			
– Basic and diluted	16	**(HK$0.09)**	(HK$0.15)

Consolidated Statement of Financial Position

At 31 December 2012

	Notes	2012 HK$'000	2011 HK$'000
NON-CURRENT ASSETS			
Property, plant and equipment	17	**577,546**	683,525
Deposit paid for acquisition of property, plant and equipment		**–**	3,136
Prepaid lease payments – non-current portion	18	**333,226**	339,192
Trade receivables – non-current portion	22	**134,200**	–
Intangible assets	19	**–**	–
Pledged deposits for other borrowings	20	**33,000**	32,472
		1,077,972	1,058,325
CURRENT ASSETS			
Inventories	21	**122,018**	180,369
Trade receivables – current portion	22	**15,750**	–
Bills and other receivables	22	**322,780**	577,482
Prepayment for purchase of raw materials	22	**324,397**	818,869
Prepaid lease payments – current portion	18	**1,910**	1,842
Amounts due from customers for contract work	27	**–**	12,880
Tax recoverable		**5,506**	5,418
Investments held for trading	23	**2,430**	2,750
Available-for-sale investments	24	**6,250**	–
Pledged bank deposits	25	**269,447**	360,841
Bank balances and cash	25	**39,854**	150,506
		1,110,342	2,110,957

Consolidated Statement of Financial Position (Continued)

At 31 December 2012

	Notes	2012 HK$'000	2011 HK$'000
CURRENT LIABILITIES			
Trade, bills and other payables	26	**1,160,722**	1,459,753
Amounts due to customers for contract work	27	**580,961**	957,515
Amounts due to related parties	28	**53,285**	31,588
Amount due to a director	29	**812**	615
Borrowings – due within one year	30	**608,004**	538,117
Provision for warranty	31	**35,530**	25,366
Deferred consideration	32	**–**	217,268
		2,439,314	3,230,222
NET CURRENT LIABILITIES		**(1,328,972)**	(1,119,265)
TOTAL ASSETS LESS CURRENT LIABILITIES		**(251,000)**	(60,940)
CAPITAL AND RESERVES			
Share capital	33	**183,400**	183,400
Reserves		**(906,474)**	(584,795)
		(723,074)	(401,395)
NON-CURRENT LIABILITIES			
Borrowings – due after one year	30	**31,080**	68,972
Convertible notes payable	34	**278,632**	157,135
Promissory notes payable	35	**68,713**	–
Deferred tax liabilities	36	**93,649**	114,348
		472,074	340,455
		(251,000)	(60,940)

The consolidated financial statements on pages 28 to 132 were approved and authorised for issue by the board of directors on 28 March 2013 and are signed on its behalf by:

CHAU On Ta Yuen
Director

ZHANG Shi Hong
Director

Consolidated Statement of Changes in Equity

For the year ended 31 December 2012

	Share capital HK$'000 (Note 33)	Share premium HK$'000	Contributed surplus HK$'000 (Note a)	Statutory reserve HK$'000 (Note b)	Translation reserve HK$'000	Share option reserve HK$'000	Convertible notes reserve HK$'000 (Note 34)	Accumulated losses HK$'000	Total HK$'000
At 1 January 2011	112,762	152,321	3,368,411	20,390	96,370	43,693	–	(3,902,302)	(108,355)
Loss for the year	–	–	–	–	–	–	–	(542,559)	(542,559)
Exchange differences arising on translation	–	–	–	–	2,288	–	–	–	2,288
Total comprehensive income (expenses) for the year	–	–	–	–	2,288	–	–	(542,559)	(540,271)
Issue of shares upon conversion of convertible notes	70,638	176,593	–	–	–	–	–	–	247,231
Transfer	–	–	–	14,434	–	–	–	(14,434)	–
At 31 December 2011	183,400	328,914	3,368,411	34,824	98,658	43,693	–	(4,459,295)	(401,395)
Loss for the year	–	–	–	–	–	–	–	(344,101)	(344,101)
Exchange differences arising on translation	–	–	–	–	(4,550)	–	–	–	(4,550)
Total comprehensive expenses for the year	–	–	–	–	(4,550)	–	–	(344,101)	(348,651)
Recognition of equity component of convertible notes payable	–	–	–	–	–	–	26,972	–	26,972
At 31 December 2012	**183,400**	**328,914**	**3,368,411**	**34,824**	**94,108**	**43,693**	**26,972**	**(4,803,396)**	**(723,074)**

Notes:

(a) Contributed surplus of the Company comprises:

(i) Pursuant to a group reorganisation in 2001, the then issued share capital of HK$469,869,000 representing 4,698,693,818 shares with a par value of HK$0.10 each were cancelled to the extent of HK$0.09 on each issued share. The cancelled portion of HK$0.09 each amounting to approximately HK$422,882,000 was transferred to contributed surplus.

(ii) Pursuant to a special resolution passed at a special general meeting on 8 July 2005:

(1) Every twenty shares of HK$0.01 each in the then issued, representing 8,860,906,389 shares, and unissued ordinary share capital of the Company was consolidated into one consolidated share of HK$0.20 each (the "2005 Consolidated Share"); and

(2) Every issued 2005 Consolidated Share, representing 443,045,319 shares having a par value of HK$0.20 each, of the Company was reduced in nominal amount by cancelling HK$0.19 of the capital paid up on each issued 2005 Consolidated Share and by reducing the nominal amount of each authorised but unissued 2005 Consolidated Share from HK$0.20 to HK$0.01 each.

The reduced portion of HK$0.19 each for the 443,045,319 2005 Consolidated Shares amounting to approximately HK$84,179,000 was transferred to contributed surplus.

(iii) Pursuant to a special resolution passed at a special general meeting on 3 March 2006:

(1) Every five shares of HK$0.01 each in the then issued, representing 2,658,226,595 shares, and unissued ordinary share capital of the Company was consolidated into one consolidated share of HK$0.05 each (the "2006 Consolidated Share"); and

(2) Every issued 2006 Consolidated Share, representing 531,645,319 shares having a par value of HK$0.05 each, of the Company was reduced in nominal amount by cancelling HK$0.04 of the capital paid up on each issued 2006 Consolidated Share and by reducing the nominal amount of each authorised but unissued 2006 Consolidated Share from HK$0.05 to HK$0.01 each.

The reduced portion of HK$0.04 each for the 531,645,319 2006 Consolidated Shares amounting to approximately HK$21,266,000 was transferred to contributed surplus.

(iv) Pursuant to a special resolution passed at a special general meeting held on 16 August 2010, the share premium of the Company was reduced by approximately HK$2,840,084,000 with the same amount transferred to contributed surplus.

(b) According to the relevant laws in the People's Republic of China (the "PRC"), the wholly foreign-owned enterprises in the PRC are required to transfer 10% of their net profit before taxation, as determined under the relevant accounting principles and financial regulations applicable to companies established in the PRC, to statutory reserve until the statutory reserve balance reaches 50% of their registered capital. The transfer to this statutory reserve must be made before the distribution of dividend to equity owners. Statutory reserve can be used to offset previous years' losses, if any, and is non-distributable other than upon liquidation.

Consolidated Statement of Cash Flows

For the year ended 31 December 2012

	2012 HK$'000	2011 HK$'000 (Restated)
OPERATING ACTIVITIES		
Loss before tax	**(368,094)**	(647,745)
Adjustments for:		
Depreciation of property, plant and equipment	**58,897**	66,888
Change in fair value of investments held for trading	**320**	1,188
Gain on settlement of deferred consideration	**(52,936)**	–
Loss (gain) on fair value change of convertible notes payable	**20,949**	(51,389)
Gain on modification of convertible notes payable	**–**	(4,262)
Loss on extinguishment of convertible notes payable	**–**	7,241
Written-off of property, plant and equipment	**7,001**	–
Gain on disposal of property, plant and equipment	**–**	(200)
Interest income	**(3,986)**	(8,908)
Finance costs	**182,100**	174,370
Amortisation of prepaid lease payments	**7,234**	7,167
Impairment loss recognised in respect of property, plant and equipment	**90,617**	415,365
Impairment loss recognised in respect of trade receivables	**794**	–
Impairment loss recognised in respect of other receivables	**1,090**	–
Operating cash flows before movements in working capital	**(56,014)**	(40,285)
Decrease in inventories	**55,418**	150,340
Increase in trade receivables	**(150,744)**	–
Decrease (increase) in bills and other receivables	**241,546**	(169,957)
Decrease (increase) in prepayment for purchase of raw materials	**481,157**	(118,406)
Decrease (increase) in amounts due from customers for contract work	**12,671**	(12,880)
Increase in amounts due to related parties	**22,211**	16,669
Increase in amount due to a director	**207**	615
(Decrease) increase in trade, bills and other payables	**(275,295)**	309,601
Increase (decrease) in provision for warranty	**9,751**	(10,282)
(Decrease) increase in amounts due to customers for contract work	**(360,985)**	136,786

Consolidated Statement of Cash Flows (Continued)

For the year ended 31 December 2012

	2012 HK$'000	2011 HK$'000 (Restated)
Cash (used in) generated from operations	**(20,077)**	262,201
Tax paid	**–**	(526)
Interest received	**3,986**	8,908
NET CASH (USED IN) FROM OPERATING ACTIVITIES	**(16,091)**	270,583
INVESTING ACTIVITIES		
Purchase of property, plant and equipment	**(33,147)**	(19,971)
Purchase of available-for-sale investments	**(6,250)**	–
Decrease in pledged bank deposits	**91,394**	28,762
Proceeds on disposal of property, plant and equipment	**–**	325
NET CASH FROM INVESTING ACTIVITIES	**51,997**	9,116
FINANCING ACTIVITIES		
Borrowings raised	**636,985**	753,116
Repayment of borrowings	**(623,667)**	(892,631)
Repayment for deferred consideration	**(10,000)**	–
Interest paid	**(125,383)**	(107,148)
NET CASH USED IN FINANCING ACTIVITIES	**(122,065)**	(246,663)
NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	**(86,159)**	33,036
CASH AND CASH EQUIVALENTS AT 1 JANUARY	**150,506**	142,608
Effect of foreign exchange rate changes	**(24,493)**	(25,138)
CASH AND CASH EQUIVALENTS AT 31 DECEMBER, represented by bank balances and cash	**39,854**	150,506

1. GENERAL

China Ocean Shipbuilding Industry Group Limited (the "Company") is incorporated in Bermuda as an exempted company with limited liability under the Companies Act of Bermuda. The Company's shares are listed on The Stock Exchange of Hong Kong Limited (the "Stock Exchange"). The addresses of the registered office and principal place of business of the Company are disclosed in the corporate information section to this annual report.

The Company is an investment holding company. The principal activities of its subsidiaries are set out in Note 45.

The functional currency of the Company and its subsidiaries (hereinafter collectively known as the "Group") was Renminbi ("RMB"). The consolidated financial statements are presented in Hong Kong dollars ("HK$") for the convenience of the shareholders as the Company is listed in Hong Kong.

2. BASIS OF PREPARATION OF THE CONSOLIDATED FINANCIAL STATEMENTS

In preparing the consolidated financial statements, the directors of the Company (the "Directors") have given consideration to the future liquidity of the Group.

The Group incurred a consolidated loss of approximately HK$344,101,000 for the year ended 31 December 2012 and, as 31 December 2012, the Group had net current liabilities and net liabilities of approximately HK$1,328,972,000 and HK$723,074,000 respectively. In addition, the Group has an arbitration proceeding in progress with one vessel owner over the validity of three rescission notices, which, if the arbitration result is unfavourable to the Group, could result in the Group refund of principal payments and interests for the principal payments calculated in accordance with the relevant shipbuilding contract up to the settlement date. At 31 December 2012, the principal payment and the interests accrued up to 31 December 2012 of approximately HK$372,338,000 (2011: HK$366,381,000) in aggregate, were recorded as "Trade, bills and other payables" in the consolidated statement of financial position (Note 26).

2. BASIS OF PREPARATION OF THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

In order to improve the Group's operating and financial position, the Directors have been implementing various operating and financing measures as follows:

a) The Group has engaged legal counsels to defend the Group for the vessel rescission notices;

b) The Group has been actively pursuing new customers so as to enlarge its customer base and new sales orders. At the same time, the Group has improved its production efficiency and tightened cost control so as to reduce unnecessary expenditure. With all these measures, the Group is expecting to improve its performance;

c) The Group is in negotiation with banks to allow revolving of loans upon their due dates when the same renewal conditions entitling the past renewal are met;

d) The Group is in negotiation with financial institutions such as financial leasing company to obtain new borrowings;

e) The Group is seeking assistance from local government;

f) The balance due from a ship buyer is expected to be recovered; and

g) The Group is in negotiation with its creditors to extend payment due date.

The Directors are of the opinion that, taking into account the measures as above, the Group will have sufficient working capital to meet its financial obligations as they fall due in the next twelve months from this consolidated financial statements were authorised to issue.

2. BASIS OF PREPARATION OF THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Accordingly, the consolidated financial statements have been prepared on a going concern basis. However, the eventual outcome is uncertain, should the going concern assumption be inappropriate, adjustments may have to be made to reflect the situation that assets may need to be realised at other than the amounts at which they are currently recorded in the consolidated statement of financial position. In addition, the Group may have to provide for further liabilities that might arise, and to reclassify non-current assets and non-current liabilities as current assets and current liabilities respectively.

3. APPLICATION OF NEW AND REVISED HONG KONG FINANCIAL REPORTING STANDARDS ("HKFRSs") AND HONG KONG ACCOUNTING STANDARDS ("HKASs")

In the current year, the Group has applied the following new and revised HKFRSs and HKASs issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA").

Amendments to HKFRS 1	*Severe Hyperinflation and Removal of Fixed Dates for First-time Adopters*
Amendments to HKAS 12	*Deferred Tax: Recovery of Underlying Asset*
Amendments to HKFRS 7	*Financial Instruments: Disclosures – Transfers of Financial Assets*

The application of the new and revised to HKFRSs and HKASs in the current year has had no material impact on the Group's financial performance and positions for the current and prior years and/or on the disclosures set out in these consolidated financial statements.

3. APPLICATION OF NEW AND REVISED HONG KONG FINANCIAL REPORTING STANDARDS ("HKFRSs") AND HONG KONG ACCOUNTING STANDARDS ("HKASs") (Continued)

New and revised HKFRSs and HKASs issued but not yet effective

The Group has not early applied the following new and revised HKFRSs and HKASs that have been issued but are not yet effective:

Amendments to HKFRSs	Annual Improvements to HKFRSs 2009 – 2011 Cycle[1]
Amendments to HKFRS 1	Government Loans[1]
Amendments to HKFRS 7	Disclosures – Offsetting Financial Assets and Financial Liabilities[1]
Amendments to HKFRS 9 and HKFRS 7	Mandatory Effective Date of HKFRS 9 and Transition Disclosures[3]
Amendments to HKFRS 10, HKFRS 11 and HKFRS 12	Consolidated Financial Statements, Joint Arrangements and Disclosure of Interests in Other Entities: Transition Guidance[1]
Amendments to HKFRS 10, HKFRS 12 and HKAS 27 (2011)	Investment Entities[2]
HKFRS 9	Financial Instruments[3]
HKFRS 10	Consolidated Financial Statements[1]
HKFRS 11	Joint Arrangements[1]
HKFRS 12	Disclosure of Interests in Other Entities[1]
HKFRS 13	Fair Value Measurement[1]
HKAS 19 (as revised in 2011)	Employee Benefits[1]
HKAS 27 (as revised in 2011)	Separate Financial Statements[1]
HKAS 28 (as revised in 2011)	Investments in Associates and Joint Ventures[1]
Amendments to HKAS 1	Presentation of Items of Other Comprehensive Income[4]
Amendments to HKAS 32	Offsetting Financial Assets and Financial Liabilities[2]
HK(IFRIC*) – Interpretation 20	Stripping Costs in the Production Phase of a Surface Mine[1]

1 Effective for annual periods beginning on or after 1 January 2013.
2 Effective for annual periods beginning on or after 1 January 2014.
3 Effective for annual periods beginning on or after 1 January 2015.
4 Effective for annual periods beginning on or after 1 July 2012.
* *IFRIC represents the International Financial Reporting Interpretation Committee*

3. APPLICATION OF NEW AND REVISED HONG KONG FINANCIAL REPORTING STANDARDS ("HKFRSs") AND HONG KONG ACCOUNTING STANDARDS ("HKASs") (Continued)

Annual Improvements to HKFRSs 2009 – 2011 Cycle issued in June 2012

The *Annual Improvements to HKFRSs 2009 – 2011 Cycle* include a number of amendments to various HKFRSs. The amendments are effective for annual periods beginning on or after 1 January 2013. Amendments to HKFRSs include the amendments to HKAS 16 *Property, Plant and Equipment* and the amendments to HKAS 32 *Financial Instruments: Presentation*.

The amendments to HKAS 16 clarify that spare parts, stand-by equipment and servicing equipment should be classified as property, plant and equipment when they meet the definition of property, plant and equipment in HKAS 16 and as inventory otherwise. The Directors do not anticipate that the application of the amendments will have a material effect on the Group's consolidated financial statements.

The amendments to HKAS 32 clarify that income tax on distributions to holders of an equity instrument and transaction costs of an equity transaction should be accounted for in accordance with HKAS 12 *Income Taxes*. The Directors anticipate that the amendments to HKAS 32 will have no effect on the Group's consolidated financial statements.

Amendments to HKAS 32 Offsetting Financial Assets and Financial Liabilities and amendments to HKFRS 7 Disclosures – Offsetting Financial Assets and Financial Liabilities

The amendments to HKAS 32 clarify existing application issues relating to the offset of financial assets and financial liabilities requirements. Specifically, the amendments clarify the meaning of "currently has a legally enforceable right of set-off" and "simultaneous realisation and settlement".

The amendments to HKFRS 7 require entities to disclose information about rights of offset and related arrangements (such as collateral posting requirements) for financial instruments under an enforceable master netting agreement or similar arrangement.

3. APPLICATION OF NEW AND REVISED HONG KONG FINANCIAL REPORTING STANDARDS ("HKFRSs") AND HONG KONG ACCOUNTING STANDARDS ("HKASs") (Continued)

Amendments to HKAS 32 Offsetting Financial Assets and Financial Liabilities and amendments to HKFRS 7 Disclosures – Offsetting Financial Assets and Financial Liabilities (Continued)

The amendments to HKFRS 7 are effective for annual periods beginning on or after 1 January 2013 and interim periods within those annual periods. The disclosures should also be provided retrospectively for all comparative periods. However, the amendments to HKAS 32 are not effective until annual periods beginning on or after 1 January 2014, with retrospective application required.

The Directors anticipate that the application of these amendments to HKAS 32 and HKFRS 7 may result in more disclosures being made with regard to offsetting financial assets and financial liabilities in the future.

New and revised standards on consolidation, joint arrangements, associates and disclosures

In June 2011, a package of five standards on consolidation, joint arrangements, associates and disclosures was issued, including HKFRS 10, HKFRS 11, HKFRS 12, HKAS 27 (as revised in 2011) and HKAS 28 (as revised in 2011).

Key requirements of these five standards are described below.

HKFRS 10 replaces the parts of HKAS 27 *Consolidated and Separate Financial Statements* that deal with consolidated financial statements. HK (SIC)-Int 12 Consolidation – Special Purpose Entities will be withdrawn upon the effective date of HKFRS 10. Under HKFRS 10, there is only one basis for consolidation, that is, control. In addition, HKFRS 10 includes a new definition of control that contains three elements: (a) power over an investee, (b) exposure, or rights, to variable returns from its involvement with the investee, and (c) the ability to use its power over the investee to affect the amount of the investor's returns. Extensive guidance has been added in HKFRS 10 to deal with complex scenarios.

3. APPLICATION OF NEW AND REVISED HONG KONG FINANCIAL REPORTING STANDARDS ("HKFRSs") AND HONG KONG ACCOUNTING STANDARDS ("HKASs") (Continued)

New and revised standards on consolidation, joint arrangements, associates and disclosures (Continued)

HKFRS 11 replaces HKAS 31 *Interests in Joint Ventures*. HKFRS 11 deals with how a joint arrangement of which two or more parties have joint control should be classified. HK (SIC) – Int 13 *Jointly Controlled Entities – Non-monetary Contributions by Venturers* will be withdrawn upon the effective date of HKFRS 11. Under HKFRS 11, joint arrangements are classified as joint operations or joint ventures, depending on the rights and obligations of the parties to the arrangements. In contrast, under HKAS 31, there are three types of joint arrangements: jointly controlled entities, jointly controlled assets and jointly controlled operations. In addition, joint ventures under HKFRS 11 are required to be accounted for using the equity method of accounting, whereas jointly controlled entities under HKAS 31 can be accounted for using the equity method of accounting or proportionate consolidation.

HKFRS 12 is a disclosure standard and is applicable to entities that have interests in subsidiaries, joint arrangements, associates and/or unconsolidated structured entities. In general, the disclosure requirements in HKFRS 12 are more extensive than those in the current standards.

In July 2012, the amendments to HKFRS 10, HKFRS 11 and HKFRS 12 were issued to clarify certain transitional guidance on the application of these five HKFRSs for the first time.

These five standards, together with the amendments relating to the transitional guidance, are effective for annual periods beginning on or after 1 January 2013 with earlier application permitted provided that all of these standards are applied at the same time.

The Directors anticipate that the application of these five standards would not have a significant impact on amounts reported in the consolidated financial statements.

3. APPLICATION OF NEW AND REVISED HONG KONG FINANCIAL REPORTING STANDARDS ("HKFRSs") AND HONG KONG ACCOUNTING STANDARDS ("HKASs") (Continued)

Amendments to HKFRS 10, HKFRS 12 and HKAS 27 Investment Entities

The amendments to HKFRS 10 introduce an exception to consolidating subsidiaries for an investment entity, except where the subsidiaries provide services that relate to the investment entity's investment activities. Under the amendments to HKFRS 10, an investment entity is required to measure its interests in subsidiaries at fair value through profit or loss.

To qualify as an investment entity, certain criteria have to be met. Specifically, an entity is required to:

- obtain funds from one or more investors for the purpose of providing them with professional investment management services;
- commit to its investor(s) that its business purpose is to invest funds solely for returns from capital appreciation, investment income, or both; and
- measure and evaluate performance of substantially all of its investments on a fair value basis.

Consequential amendments to HKFRS 12 and HKAS 27 have been made to introduce new disclosure requirements for investment entities.

The amendments to HKFRS 10, HKFRS 12 and HKAS 27 are effective for annual periods beginning on or after 1 January 2014, with early application permitted. The Directors anticipate that the application of the amendments will have no effect on the Group as the Company is not an investment entity.

3. APPLICATION OF NEW AND REVISED HONG KONG FINANCIAL REPORTING STANDARDS ("HKFRSs") AND HONG KONG ACCOUNTING STANDARDS ("HKASs") (Continued)

HKFRS 9 Financial Instruments

HKFRS 9 issued in 2009 introduces new requirements for the classification and measurement of financial assets. HKFRS 9 amended in 2010 includes the requirements for the classification and measurement of financial liabilities and for derecognition.

Key requirements of HKFRS 9 are described as follows:

- HKFRS 9 requires all recognised financial assets that are within the scope of HKAS 39 *Financial Instruments: Recognition and Measurement* are subsequently measured at amortised cost or fair value. Specifically, debt investments that are held within a business model whose objective is to collect the contractual cash flows, and that have contractual cash flows that are solely payments of principal and interest on the principal outstanding are generally measured at amortised cost at the end of subsequent accounting periods. All other debt investments and equity investments are measured at their fair values at the end of subsequent reporting periods. In addition, under HKFRS 9, entities may make an irrevocable election to present subsequent changes in the fair value of an equity investment (that is not held for trading) in other comprehensive income, with only dividend income generally recognised in profit or loss.

- With regard to the measurement of financial liabilities designated as at fair value through profit or loss, HKFRS 9 requires that the amount of change in the fair value of the financial liability that is attributable to changes in the credit risk of that liability is presented in other comprehensive income, unless the recognition of the effects of changes in the liability's credit risk in other comprehensive income would create or enlarge an accounting mismatch in profit or loss. Changes in fair value of financial liabilities attributable to changes in the financial liabilities' credit risk are not subsequently reclassified to profit or loss. Under HKAS 39, the entire amount of the change in the fair value of the financial liability designated as fair value through profit or loss was presented in profit or loss.

HKFRS 9 is effective for annual periods beginning on or after 1 January 2015, with earlier application permitted.

3. APPLICATION OF NEW AND REVISED HONG KONG FINANCIAL REPORTING STANDARDS ("HKFRSs") AND HONG KONG ACCOUNTING STANDARDS ("HKASs") (Continued)

HKFRS 9 Financial Instruments (Continued)

The Directors anticipate that the adoption of HKFRS 9 in the future may not have significant impact on amounts reported in respect of the Group's financial assets and financial liabilities. Regarding the Group's financial assets and financial liabilities, it is not practicable to provide a reasonable estimate of that effect until a detailed review has been completed.

HKFRS 13 Fair Value Measurement

HKFRS 13 establishes a single source of guidance for fair value measurements and disclosures about fair value measurements. The standard defines fair value, establishes a framework for measuring fair value, and requires disclosures about fair value measurements. The scope of HKFRS 13 is broad; it applies to both financial instrument items and non-financial instrument items for which other HKFRSs require or permit fair value measurements and disclosures about fair value measurements, except in specified circumstances. In general, the disclosure requirements in HKFRS 13 are more extensive than those in the current standards. For example, quantitative and qualitative disclosures based on the three-level fair value hierarchy currently required for financial instruments only under HKFRS 7 *Financial Instruments: Disclosures* will be extended by HKFRS 13 to cover all assets and liabilities within its scope.

HKFRS 13 is effective for annual periods beginning on or after 1 January 2013, with earlier application permitted. The Directors anticipate that the application of the new standard may affect certain amounts reported in the consolidated financial statements and result in more extensive disclosures in the consolidated financial statements.

Amendments to HKAS 1 Presentation of Items of Other Comprehensive Income

The amendments to HKAS 1 *Presentation of Items of Other Comprehensive Income* introduce new terminology for the statement of comprehensive income and income statement. Under the amendments to HKAS 1, a "statement of comprehensive income" is renamed as a "statement of profit or loss and other comprehensive income" and an "income statement" is renamed as a "statement of profit or loss". The amendments to HKAS 1 retain the option to present profit or loss and other comprehensive income in either a single statement or in two separate but consecutive statements. However, the amendments to HKAS 1 require items of other comprehensive income to be grouped into two categories: (a) items that will not be reclassified subsequently to profit or loss; and (b) items that may be reclassified subsequently to profit or loss when specific conditions are met. Income tax on items of other comprehensive income is required to be allocated on the same basis – the amendments do not change the option to present items of other comprehensive income either before tax or net of tax.

3. APPLICATION OF NEW AND REVISED HONG KONG FINANCIAL REPORTING STANDARDS ("HKFRSs") AND HONG KONG ACCOUNTING STANDARDS ("HKASs") (Continued)

Amendments to HKAS 1 Presentation of Items of Other Comprehensive Income (Continued)

The amendments to HKAS 1 are effective for annual periods beginning on or after 1 July 2012. The presentation of items of other comprehensive income will be modified accordingly when the amendments are applied in future accounting periods.

4. SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements have been prepared in accordance with HKFRSs issued by the HKICPA. In addition, the consolidated financial statements include applicable disclosures required by the Rules Governing the Listing of Securities on Stock Exchange (the "Listing Rules") and by the Hong Kong Companies Ordinance.

The consolidated financial statements have been prepared on the historical cost basis except for certain financial instruments that are measured at fair values. Historical cost is generally based on the fair value of the consideration given in exchange for goods.

The principal accounting policies are set out below:

Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and entities controlled by the Company (its subsidiaries). Control is achieved where the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities.

Income and expenses of subsidiaries acquired or disposed of during the year are included in the consolidated statement of comprehensive income from the effective date of acquisition and up to the effective date of disposal, as appropriate.

Where necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies into line with those used by other members of the Group.

All intra-group transactions, balances, income and expenses are eliminated in full on consolidation.

4. SIGNIFICANT ACCOUNTING POLICIES (Continued)

Revenue recognition

Revenue is measured at the fair value of the consideration received or receivable and represents amounts receivable for goods sold and service rendered (for shipbuilding, see below "construction contracts" for details) in the normal course of business, net of discounts and sales related taxes.

Revenue from shipbuilding represents income arising on shipbuilding construction contracts for the year.

Revenue from a contract to provide services is recognised by reference to the stage of completion of the contract. The stage of completion of the contract is determined as follows:

– Servicing fees are recognised by reference to the proportion of the total cost of providing the service; and

– Revenue from time and material contracts is recognised at the contractual rates as labour hours and direct expenses are incurred.

Revenue from sales of goods is recognised when the goods are delivered and title has passed, at which time all the following conditions are satisfied;

– the Group has transferred to the buyer the significant risks and rewards of ownership of the goods;

– the Group retains neither continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold;

– the amount of revenue can be measured reliably;

– it is probable that the economic benefits associated with the transaction will flow to the Group; and

– the costs incurred or to be incurred in respect of the transaction can be measured reliably.

4. SIGNIFICANT ACCOUNTING POLICIES (Continued)

Revenue recognition (Continued)

Interest income from a financial asset is recognised when it is probable that the economic benefits will flow to the Group and the amount of income can be measure reliably. Interest income is accrued on a time basis, by reference to principal outstanding and at the effective interest rate applicable, which is the rate that exactly discounts the estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount on initial recognition.

Dividend income from investments is recognised when the shareholders' rights to receive payment have been established (provided that it is probable that the economic benefits will flow to the Group and the amount of revenue can be measured reliably).

Property, plant and equipment

Property, plant and equipment including buildings held for use in the production or supply of goods or services, or for administrative purposes (other than construction in progress) are stated in the consolidated statement of financial position at cost less subsequent accumulated depreciation and accumulated impairment losses, if any.

Depreciation is recognised so as to write-off the cost of items of property, plant and equipment other than construction in progress less their residual values over their estimated useful lives, using the straight-line method. The estimated useful lives, residual values and depreciation method are reviewed at the end of each reporting period, with the effect of any changes in estimate accounted for on a prospective basis.

Properties in the course of construction for production, supply or administrative purposes are carried at cost, less any recognised accumulated impairment loss. Costs include professional fees and, for qualifying assets, borrowing costs capitalised in accordance with the Group's accounting policy. Such properties are classified to the appropriate categories of property, plant and equipment when completed and ready for intended use. Depreciation of these assets, on the same basis as other property assets, commences when the assets are ready for their intended use.

4. SIGNIFICANT ACCOUNTING POLICIES (Continued)

Property, plant and equipment (Continued)

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on the disposal or retirement of an item of property, plant and equipment is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognised in profit or loss.

Prepaid lease payments

Prepaid lease payments are up-front payments to acquire leasehold land interests. The prepaid lease payments are stated at cost and are charged to the consolidated statement of comprehensive income over the period of the lease on a straight-line basis.

Provisions

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that the Group will be required to settle that obligation, and a reliable estimate can be made of the amount of the obligation. Provisions are measured at the best estimate of the consideration required to settle the present obligation at the end of the reporting period, taking into account the risks and uncertainties surrounding the obligation. Where a provision is measured using the cash flows estimated to settle the present obligation, its carrying amount is the present value of those cash flows (where the effect of the time value of money is material).

When some or all of the economic benefits required to settle a provision are expected to be recovered from a third party, a receivable is recognised as an asset if it is virtually certain that reimbursement will be received and the amount of the receivable can be measured reliably.

4. SIGNIFICANT ACCOUNTING POLICIES (Continued)

Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, which are assets that necessarily take a substantial period of time to get ready for their intended use or sale, are added to the cost of those assets until such time as the assets are substantially ready for their intended use or sale.

All other borrowing costs are recognised in profit or loss in the period in which they are incurred.

Construction contracts

Where the outcome of a construction contract for shipbuilding can be estimated reliably, revenue and costs are recognised by reference to the stage of completion of the contract activity at the end of the reporting period, as determined by reference to the standard hours incurred up to the end of the reporting period as a percentage of total estimated standard hours for each contract. Variations in contract work, claims and incentive payments are included to the extent that the amount can be measured reliably and its receipt is considered probable.

Where contract costs incurred to date plus recognised profits less recognised losses exceed progress billings, the surplus is shown as amounts due from customers for contract work. For contracts where progress billings exceed contract costs incurred to date plus recognised profits less recognised losses, the surplus is shown as amounts due to customers for contract work. Amounts received before the related work is performed are included in the consolidated statement of financial position, as a liability, as advances received. Amounts billed for work performed but not yet paid by the customer are included in the consolidated statement of financial position under trade receivables.

4. SIGNIFICANT ACCOUNTING POLICIES (Continued)

Financial instruments

Financial assets and financial liabilities are recognised in the consolidated statement of financial position when a group entity becomes a party to the contractual provisions of the instrument.

Financial assets and financial liabilities are initially measured at fair value. Transaction costs that are directly attributable to the acquisition or issue of financial assets and financial liabilities (other than financial assets or financial liabilities at fair value through profit or loss) are added to or deducted from the fair value of the financial assets or financial liabilities, as appropriate, on initial recognition. Transaction costs directly attributable to the acquisition of financial assets or financial liabilities at fair value through profit or loss are recognised immediately in profit or loss.

Financial assets

The Group's financial assets are classified into one of the three categories, including financial assets at fair value through profit or loss ("FVTPL"), loans and receivables and available-for-sale ("AFS") financial assets. The classification depends on the nature and purpose of the financial assets and is determined at the time of initial recognition. All regular way purchases or sales of financial assets are recognised and derecognised on a trade date basis. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the time frame established by regulation or convention in the marketplace.

Effective interest method

The effective interest method is a method of calculating the amortised cost of a debt instrument and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts (including all fees and points paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the debt instrument, or, where appropriate, a shorter period, to the net carrying amount on initial recognition.

Interest income is recognised on an effective interest basis for debt instruments other than those financial assets classified as at FVTPL, of which interest income is included in net gains or losses.

4. SIGNIFICANT ACCOUNTING POLICIES (Continued)

Financial instruments (Continued)

Financial assets *(Continued)*

Financial assets at fair value through profit or loss

Financial assets at FVTPL of the Group represents financial assets held for trading.

A financial asset is classified as held for trading if:

- it has been acquired principally for the purpose of selling in the near future; or
- it is a part of a portfolio of identified financial instruments that the Group manages together and has a recent actual pattern of short-term profit-taking; or
- it is a derivative that is not designated and effective as a hedging instrument.

Financial assets at FVTPL are measured at fair value, with changes in fair value arising from remeasurement recognised directly in profit or loss in the period in which they arise. The net gain or loss recognised in profit or loss excludes any dividend or interest earned on the financial assets and is included in the "change in fair value of investments held for trading" line item in the consolidated statement of comprehensive income. Fair value is determined in the manner described in Note 23 to the consolidated financial statements.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Subsequent to initial recognition, loans and receivables (including pledged deposits for other borrowings, trade receivables, bills and other receivables, pledged bank deposits and bank balances and cash) are measured at amortised cost using the effective interest method, less any identified accumulated impairment losses (see accounting policy on impairment loss of financial assets below).

AFS financial assets

AFS financial assets are non-derivatives that are either designated or not classified as financial assets at FVTPL, loans and receivables or held-to-maturity investments. The Group designated unlisted equity investments as AFS financial assets on initial recognition of those items.

Dividend on AFS equity instruments are recognised in profit or loss when the Group's right to receive the dividends is established.

4. SIGNIFICANT ACCOUNTING POLICIES (Continued)

Financial instruments (Continued)

***Financial assets** (Continued)*

AFS financial assets (Continued)

AFS equity investments that do not have a quoted market price in an active market and whose fair value cannot be reliably measured and derivatives that are linked to and must be settled by delivery of such unquoted equity investments are measured at cost less any identified accumulated impairment losses at the end of each reporting period (see the accounting policy in respect of impairment loss on financial assets below).

Impairment loss of financial assets

Financial assets, other than those at FVTPL, are assessed for indicators of impairment at the end of the reporting period. Financial assets are considered to be impaired where there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the financial assets have been affected.

For an AFS equity investment, a significant or prolonged decline in the fair value of that investment below its cost is considered to be objective evidence of impairment.

For all other financial assets, objective evidence of impairment could include:

- significant financial difficulty of the issuer or counterparty; or
- breach of contract, such as default or delinquency in interest or principal payments; or
- it becoming probable that the borrower will enter bankruptcy or financial re-organisation; or
- disappearance of an active market for that financial asset because of financial difficulties.

For certain categories of financial assets, such as trade and other receivables, assets that are assessed not to be impaired individually are, in addition, assessed for impairment on a collective basis. Objective evidence of impairment for a portfolio of receivables could include the Group's past experience of collecting payments, observable changes in national or local economic conditions that correlate with default on receivables.

4. SIGNIFICANT ACCOUNTING POLICIES (Continued)

Financial instruments (Continued)

***Impairment loss of financial assets** (Continued)*

For financial assets carried at amortised cost, the amount of the impairment loss recognised is the difference between the asset's carrying amount and the present value of the estimated future cash flows discounted at the financial asset's original effective interest rate.

For financial assets carried at cost, the amount of impairment loss is measured as the difference between the asset's carrying amount and the present value of the estimated future cash flows discounted at the current market rate of return for a similar financial asset. Such impairment loss will not be reversed in subsequent periods.

The carrying amount of the financial asset is reduced by the impairment loss directly for all financial assets with the exception of trade and other receivables, where the carrying amount is reduced through the use of an allowance account. Changes in the carrying amount of the allowance account are recognised in profit or loss. When a trade and other receivable is considered uncollectible, it is written-off against the allowance account. Subsequent recoveries of amounts previously written-off are credited to profit or loss.

When an AFS financial asset is considered to be impaired, cumulative gains or losses previously recognised in other comprehensive income are reclassified to profit or loss in the period in which the impairment takes place.

For financial assets measured at amortised cost, if, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment losses was recognised, the previously recognised impairment loss is reversed through profit or loss to the extent that the carrying amount of the asset at the date the impairment is reversed does not exceed what the amortised cost would have been had the impairment not been recognised.

4. SIGNIFICANT ACCOUNTING POLICIES (Continued)

Financial instruments (Continued)

Impairment loss of financial assets *(Continued)*

Impairment losses on AFS equity investments will not be reversed through profit or loss. Any increase in fair value subsequent to an impairment loss is recognised directly in other comprehensive income and accumulated in investment revaluation reserve. For AFS debt investments, impairment losses are subsequently reversed through profit or loss if an increase in the fair value of the investment can be objectively related to an event occurring after the recognition of the impairment loss.

Financial liabilities and equity instruments

Debt and equity instruments issued by a group entity are classified as either financial liabilities or as equity in accordance with the substance of the contractual arrangements and the definitions of a financial liability and an equity instrument.

Equity instruments

An equity instrument is any contract that evidences a residual interest in the assets of the Group after deducting all of its liabilities. Equity instruments issued by the Group are recognised at the proceeds received, net of direct issue costs.

Effective interest method

The effective interest method is a method of calculating the amortised cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments (including all fees and points paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the financial liability, or, where appropriate, a shorter period, to the net carrying amount on initial recognition.

Interest expense is recognised on an effective interest basis.

4. SIGNIFICANT ACCOUNTING POLICIES (Continued)

Financial instruments (Continued)

***Financial liabilities and equity instruments** (Continued)*

Convertible notes contains liability and equity components

Convertible notes issued by the Group that contain both the liability and conversion option components are classified separately into respective items on initial recognition in accordance with the substance of the contractual arrangements and the definitions of a financial liability and an equity instrument. Conversion option that will be settled by the exchange of a fixed amount of cash or another financial asset for a fixed number of the Company's own equity instruments is classified as an equity instrument.

On initial recognition, the fair value of the liability component is determined using the prevailing market interest of similar non-convertible debts. The difference between the gross proceeds of the issue of the convertible notes and the fair value assigned to the liability component, representing the conversion option for the holder to convert the notes into equity, is included in equity (convertible notes reserve).

In subsequent periods, the liability component of the convertible notes is carried at amortised cost using the effective interest method. The equity component, representing the option to convert the liability component into ordinary shares of the Company, will remain in convertible notes reserve until the embedded option is exercised (in which case the balance stated in convertible notes reserve will be transferred to share premium). Where the option remains unexercised at the expiry date, the balance stated in convertible notes reserve will be released to the accumulated losses. No gain or loss is recognised in profit or loss upon conversion or expiration of the option.

Transaction costs that relate to the issue of the convertible notes are allocated to the liability and equity components in proportion to the allocation of the gross proceeds. Transaction costs relating to the equity component are charged directly to equity. Transaction costs relating to the liability component are included in the carrying amount of the liability portion and amortised over the period of the convertible notes using the effective interest method.

4. SIGNIFICANT ACCOUNTING POLICIES (Continued)

Financial instruments (Continued)

***Financial liabilities and equity instruments** (Continued)*

Convertible notes contains liability components and conversion option derivative

Convertible notes issued by the Group that contain both liability and conversion option components are classified separately into respective items on initial recognition. Conversion option that will be settled other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of the Company's own equity instruments is a conversion option derivative. At the date of issue, both the liability and conversion option components are recognised at fair value.

In subsequent periods, the liability component of the convertible notes is carried at amortised cost using the effective interest method. The conversion option derivative together with other embedded derivates are measured at fair value with changes in fair value recognised in profit or loss.

Transaction costs that relate to the issue of the convertible notes are allocated to the liability and derivative components in proportion to their relative fair values. Transaction costs relating to the derivative components are charged to profit or loss immediately. Transaction costs relating to the liability component are included in the carrying amount of the liability portion and amortised over the period of the convertible notes using the effective interest method.

Other financial liabilities

Other financial liabilities of the Group include trade, bills and other payables, borrowings, amounts due to related parties, amount due to a director, deferred consideration, and promissory notes payable which are subsequently measured at amortised cost, using the effective interest method.

4. SIGNIFICANT ACCOUNTING POLICIES (Continued)

Financial instruments (Continued)

Derecognition

The Group derecognises a financial asset only when the contractual rights to the cash flows from the asset expired, or when it transfers the financial asset and substantially all the risks and rewards of ownership of the asset to another entity. If the Group neither transfers nor retains substantially all the risks and rewards of ownership and continues to control the transferred asset, the Group continues to recognise the asset to the extent of its continuing involvement and recognises an associated liability. If the Group retains substantially all the risks and rewards of ownership of a transferred financial asset, the Group continues to recognise the financial asset and also recognises a collateralised borrowing for the proceeds received.

On derecognition of a financial asset in its entirety, the difference between the asset's carrying amount and the sum of the consideration received and receivable and the cumulative gain or loss that had been recognised in other comprehensive income and accumulated in equity is recognised in profit or loss.

On derecognition of a financial asset other than in its entirety, the Group allocates the previous carrying amount of the financial asset between the part it continues to recognise, and the part it no longer recognises on the basis of the relative fair values of those parts on the date of the transfer. The difference between the carrying amount allocated to the part that is no longer recognised and the sum of the consideration received for the part no longer recognised and any cumulative gain or loss allocated to it that had been recognised in other comprehensive income is recognised in profit or loss. A cumulative gain or loss that had been recognised in other comprehensive income is allocated between the part that continues to be recognised and the part that is no longer recognised on the basis of the relative fair values of those parts.

The Group derecognises financial liabilities when, and only when, the Group's obligations are discharged, cancelled or expired. The difference between the carrying amount of the financial liability derecognised and the consideration paid and payable is recognised in profit or loss.

4. SIGNIFICANT ACCOUNTING POLICIES (Continued)

Impairment losses on tangible and intangible assets

At the end of the reporting period, the Group reviews the carrying amounts of its tangible and intangible assets with finite useful lives to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss, if any. When it is not possible to estimate the recoverable amount of an individual asset, the Group estimates the recoverable amount of the cash-generating unit to which the asset belongs. When a reasonable and consistent basis of allocation can be identified, corporate assets are also allocated to individual cash-generating units, or otherwise they are allocated to the smallest group of cash-generating units for which a reasonable and consistent allocation basis can be identified.

Intangible assets with indefinite useful lives and intangible assets not yet available for use are tested for impairment at least annually, and whenever there is an indication that they may be impaired.

Recoverable amount is the higher of fair value less costs to sell 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 the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted.

If the recoverable amount of an asset (or a cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (or a cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognised immediately in profit or loss.

Where an impairment loss subsequently reverses, the carrying amount of the asset (or cash-generating unit) is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset (or a cash-generating unit) in prior years. A reversal of an impairment loss is recognised as income immediately in profit or loss.

4. SIGNIFICANT ACCOUNTING POLICIES (Continued)

Taxation

Income tax expense represents the sum of the tax currently payable and deferred tax.

The tax currently payable is based on taxable profit for the year. Taxable profit differs from "profit before tax" as reported in the consolidated statement of comprehensive income because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The Group's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the end of the reporting period.

Deferred tax is recognised on temporary differences between the carrying amounts of assets and liabilities in the consolidated financial statements and the corresponding tax base used in the computation of taxable profit. Deferred tax liabilities are generally recognised for all taxable temporary differences. Deferred tax assets are generally recognised for all deductible temporary difference to the extent that it is probable that taxable profits will be available against which those deductible temporary differences can be utilised. Such assets and liabilities are not recognised if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

Deferred tax liabilities are recognised for taxable temporary differences associated with investments in subsidiaries, except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future. Deferred tax assets arising from deductible temporary differences associated with such investments and interests are only recognised to the extent that it is probable that there will be sufficient taxable profits against which to utilise the benefits of the temporary differences and they are expected to reverse in the foreseeable future.

The carrying amount of deferred tax assets is reviewed at the end of each reporting period and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the period in which the liability is settled or the asset is realised, based on tax rate (and tax laws) that have been enacted or substantively enacted by the end of the reporting period.

4. SIGNIFICANT ACCOUNTING POLICIES (Continued)

Taxation (Continued)

The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the Group expects, at the end of the reporting period, to recover or settle the carrying amount of its assets and liabilities.

Current and deferred tax is recognised into profit or loss, except when they relate to items that are recognised in other comprehensive income or directly in equity, in which case, the current and deferred tax are also recognised in other comprehensive income or directly in equity respectively.

When current tax or deferred tax arises from the initial accounting for a business combination, the tax effect is included in the accounting for the business combination.

Foreign currencies

In preparing the financial statements of each individual group entity, transactions in currencies other than the functional currency of that entity (foreign currencies) are recorded in the respective functional currency (i.e. the currency of the primary economic environment in which the entity operates) at the rates of exchanges prevailing on the dates of the transactions. At the end of the reporting period, monetary items denominated in foreign currencies are retranslated at the rates prevailing at that date. Non-monetary items carried at fair value that are denominated in foreign currencies are retranslated at the rates prevailing on the date when the fair value was determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.

Exchange differences arising on the settlement of monetary items, and on the retranslation of monetary items, are recognised in profit or loss in the period in which they arise. Exchange differences arising on the retranslation of non-monetary items carried at fair value are included in profit or loss for the period.

For the purposes of presenting the consolidated financial statements, the assets and liabilities of the Group's foreign operations are translated into the presentation currency of the Group (i.e. Hong Kong dollars) using exchange rates prevailing at the end of each reporting period. Income and expenses items are translated at the average exchange rates for the year, unless exchange rates fluctuate significantly during the year, in which case, the exchange rates prevailing at the dates of the transactions are used. Exchange differences arising, if any, are recognised in other comprehensive income and accumulated in equity under the heading of translation reserve.

4. SIGNIFICANT ACCOUNTING POLICIES (Continued)

Foreign currencies (Continued)

On the disposal of a foreign operation (i.e. a disposal of the Group's entire interest in a foreign operation, or a disposal involving loss of control over a subsidiary that includes a foreign operation), all of the exchange differences accumulated in equity in respect of that operation attributable to the owners of the Company are reclassified to profit or loss.

Inventories

Inventories are stated at the lower of cost and net realisable value. Costs of inventories are calculated using the weighted average method.

Leasing

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

The Group as lessee

Operating lease payments are recognised as an expense on a straight-line basis over the lease term, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed. Contingent rentals arising under operating leases are recognised as an expense in the period in which they are incurred.

In the event that lease incentives are received to enter into operating leases, such incentives are recognised as a liability. The aggregate benefit of incentives is recognised as a reduction of rental expense on a straight-line basis, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed.

Retirement benefits costs

Payments to the Mandatory Provident Fund Scheme ("MPF") and state-managed retirement benefit schemes are recognised as an expense when employees have rendered service entitling them to the contributions.

Intangible assets acquired in a business combination

Intangible assets acquired in a business combination are identified and recognised separately from goodwill and initially recognised at their fair value at the acquisition date (which is regarded as their cost).

4. SIGNIFICANT ACCOUNTING POLICIES (Continued)

Intangible assets acquired in a business combination (Continued)

Subsequent to initial recognition, intangible assets with finite useful lives are carried at costs less accumulated amortisation and any accumulated impairment losses. Amortisation for intangible assets with finite useful lives is recognised on a straight-line basis over their estimated useful lives.

Share-based payment transactions

Share options granted to employees

The fair value of services received determined by reference to the fair value of share options granted at the date of grant is expensed on a straight-line basis over the vesting period, with a corresponding increase in equity (share option reserve).

At the end of the reporting period, the Group revises its estimates of the number of options that are expected to ultimately vest. The impact of the revision of the original estimates during the vesting period, if any, is recognised in profit or loss such that the cumulative expense reflects the revised estimate, with a corresponding adjustment to share option reserve.

When the share options are exercised, the amount previously recognised in share option reserve will be transferred to share premium. When the share options are forfeited after the vesting date or are still not exercised at the expiry date, the amount previously recognised in share option reserve will be transferred to accumulated losses.

Share options granted to consultants

Share options issued in exchange for services are measured at the fair values of the services received, unless that fair value cannot be reliably measured, in which case the services received are measured by reference to the fair value of the share options granted. The fair values of the services received are recognised as expenses, with a corresponding increase in equity (share option reserve), when the counterparties render services, unless the services qualify for recognition as assets.

4. SIGNIFICANT ACCOUNTING POLICIES (Continued)

Government grants

Government grants are not recognised until there is reasonable assurance that the Group will comply with the conditions attaching to them and that the grants will be received.

Government grants are recognised in profit or loss on a systematic basis over the periods in which the Group recognises as expenses the related costs for which the grants are intended to compensate. Specifically, government grants whose primary condition is that the Group should purchase, construct or otherwise acquire non-current assets are recognised as deferred income in the consolidated statement of financial position and transferred to profit or loss on a systematic and rational basis over the useful lives of the related assets.

Government grants that are receivable as compensation for expenses or losses already incurred or for the purpose of giving immediate financial support to the Group with no future related costs are recognised in profit or loss in the period in which they become receivable.

5. KEY SOURCES OF ESTIMATION UNCERTAINTY

In the application of the Group's accounting policies, which are described in Note 4, the Directors are required to make judgements, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. 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.

The following are the key assumptions concerning the future, and other key sources of estimation uncertainty at the end of the reporting period, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year.

5. KEY SOURCES OF ESTIMATION UNCERTAINTY (Continued)

Construction contracts

The Group recognises contract revenue and profit or loss on each shipbuilding contract according to management's estimation of the outcome of the contract as well as the percentage of completion of shipbuilding works. Notwithstanding that the management reviews and revises the estimates of both contract revenue and costs for the shipbuilding contracts as the contract progresses, the actual outcome of the contract in terms of its total revenue and costs may be higher or lower than the estimates and this will affect the revenue and profit or loss recognised. The Group also revisits and revises the estimate of contract profit or loss as the contract progresses based on the information available in the market. Foreseeable losses are provided when identified. During the current year, due to unforeseen circumstances in certain shipbuilding contracts, the Group recognised foreseeable losses of approximately HK$94,142,000 (2011: HK$47,380,000) in respect of certain shipbuilding contracts, details of which are set out in Note 12 to the consolidated financial statements.

Profit recognition for construction contracts

The Group commences recognition of profit for each shipbuilding construction contract when the percentage of completion exceeds 10% for that vessel, assuming that the outcome of the contract can be reasonably ascertained, as management considers that after this stage, the total contract costs attributable to the contracts can be measured reliably.

Allowance for inventories

Inventories are valued at the lower of cost and net realisable value. Cost is calculated using the weighted average method. The Group reviews its inventory levels in order to identify slow-moving and obsolete items. When the Group identifies items of inventories which have a net realisable value lower than its carrying amount, the Group estimates the amount of write-down of inventories as allowance for inventories. At 31 December 2012, the carrying amount of inventories amounted to approximately HK$122,018,000 (2011: HK$180,369,000).

If the net realisable value of inventories of the Group become lower than its carrying amount subsequently, an additional allowance may be required.

5. KEY SOURCES OF ESTIMATION UNCERTAINTY (Continued)

Estimated impairment of property, plant and equipment and prepaid lease payments

The carrying amount of property, plant and equipment and prepaid lease payments are reviewed annually and adjusted for impairment in accordance with HKAS 36 *Impairment of Assets* whenever certain events or changes in circumstances indicate that the carrying amount may not be recoverable. The value-in-use calculation requires the Group to determine the recoverable amount of the assets based on the estimations of future expected cash flows from the usage of these assets and a suitable discount rate. Where the future cash flows are less than expected, a material impairment loss may arise. During the current year, the Group recognised an impairment loss amounting to approximately HK$90,617,000 (2011: HK$415,365,000) in respect of property, plant and equipment. Details of the recoverable amount calculation for property, plant and equipment and prepaid lease payments are disclosed in Notes 17 and 18 respectively.

Estimated impairment of trade receivables

When there is objective evidence of impairment loss, the Group estimates the future cash flows to determine the impairment loss. A considerable amount of judgement is required in assessing the ultimate realisation of these receivables, including creditworthiness, the past collection history of each customer and the customer's operation as a going concern. If the financial conditions of customers of the Group were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances may be required. At 31 December 2012, the carrying amount of trade receivables is HK$149,950,000 (net of allowance for doubtful debts of approximately HK$794,000) (31 December 2011: carrying amount of Nil, net of allowance for doubtful debts of approximately HK$39,929,000).

5. KEY SOURCES OF ESTIMATION UNCERTAINTY (Continued)

Provision for warranty

The Group provides for the estimated cost of warranties granted on shipbuilding products and undertakings to repair or replace items that do not perform satisfactorily at the time revenues for the related items are recognised. The shipbuilding products are covered by warranty for one year from the date of delivery. While the Group has put in place product quality programs and processes, warranty obligations are affected by actual product failure rates and by material usage and service delivery costs incurred in correcting a product failure. The warranty provision is established based upon the best estimates at the amounts necessary to settle future and existing claims on products sold as at the end of the reporting period. While management believes that the Group's warranty provisions are adequate and that the judgments applied are appropriate, the ultimate cost of product warranty could differ materially from the estimates. When the actual cost of quality of the products is lower than management originally anticipated, the Group releases an appropriate proportion of the provision, and if the cost of quality is higher than anticipated, the Group increases the provision.

6. CAPITAL RISK MANAGEMENT

The Group manages its capital to ensure that entities in the Group will be able to continue as a going concern while maximising the return to stakeholders through the optimisation of the debt and equity balance. The Group's overall strategy remains unchanged from prior year.

The Group also monitors the current and expected liquidity requirements regularly to ensure that sufficient working capital and adequate committed lines of funding are maintained to meet its liquidity requirements. Upon the discovery of any default, the Group would negotiate immediately with the relevant lenders for proper arrangement in order to maintain sufficient working capital. Upon the expectation of any cash insufficiency, the Company would seek new source of funding so as to maintain sufficient working capital.

The capital structure of the Group consists of net debts, which include the cash and cash equivalents, borrowings, deferred consideration, convertible notes payable, promissory notes payable and equity attributable to owners of the Company, comprising issued share capital and reserves.

6. CAPITAL RISK MANAGEMENT (Continued)

The Directors review the capital structure regularly. As part of this review, the Directors consider the cost of capital and the risks associates with each class of capital. Based on the recommendations of the Directors, the Group will balance its overall capital structure through the payment of dividends, new share issues and share buy-backs as well as issue of new debt or the redemption of existing debt.

7. FINANCIAL INSTRUMENTS

a. Categories of financial instruments

	2012 HK$'000	2011 HK$'000
Financial assets		
Fair value through profit or loss		
– Investments held for trading	**2,430**	2,750
Loans and receivables (including bank balances and cash)	**666,806**	862,077
Available-for-sale investments	**6,250**	–
	675,486	864,827
Financial liabilities		
Liabilities measured at amortised cost	**2,200,694**	2,172,736

7. FINANCIAL INSTRUMENTS (Continued)

b. Financial risk management objectives and policies

The Group's major financial instruments include pledged deposits for other borrowings, trade receivables, bills and other receivables, investments held for trading, available-for-sale investments, pledged bank deposits, bank balances and cash, trade, bills and other payables, amounts due to related parties, amount due to a director, borrowings, deferred consideration, convertible notes payable and promissory notes payable. Details of the financial instruments are disclosed in respective notes. The risks associated with these financial instruments include market risk (currency risk, interest rate risk and other price risk), credit risk and liquidity risk. The policies on how to mitigate these risks are set out below. The management manages and monitors these exposures to ensure appropriate measures are implemented on a timely and effective manner.

Market risk

(i) Currency risk

The Company and its major operating subsidiary use RMB as its functional currency and are mainly exposed to United States dollars ("USD"), Euro ("EUR") and HK$, arising from foreign currency denominated pledged bank deposits, bank balances and cash, trade receivables, other receivables, trade and other payables, borrowings, convertible notes payable, promissory notes payable and deferred consideration. The Group's other operating subsidiaries (all use HK$ as their functional currency) do not have significant foreign currency exposure.

The Group currently does not have a foreign currency hedging policy. However, the management monitors foreign currency exposure and will consider hedging significant foreign currency exposure should the need arise.

7. FINANCIAL INSTRUMENTS (Continued)

b. Financial risk management objectives and policies (Continued)

***Market risk** (Continued)*

(i) Currency risk (Continued)

The carrying amounts of the Group's foreign currency denominated monetary assets and monetary liabilities at the end of reporting period are as follows:

	Liabilities		Assets	
	2012	2011	**2012**	2011
	HK$'000	HK$'000	**HK$'000**	HK$'000
USD	**56,017**	103,568	**195,523**	36,749
EUR	**33,369**	100	**4,733**	41,578
HK$	**358,018**	378,220	**13,045**	65,099

Sensitivity analysis

The Group is mainly exposed to the currency of USD, EUR and HK$.

The following table details the Group's sensitivity to a 5% (2011: 5%) increase and decrease in RMB against the relevant foreign currencies. A 5% (2011: 5%) is the sensitivity rate used when reporting foreign currency risk internally to key management personnel and represents management's assessment of the reasonably possible change in foreign exchange rates. The sensitivity analysis includes only outstanding foreign currency denominated monetary items and adjusts their translations at the end of the reporting period for a 5% (2011: 5%) change in foreign currency rates. A positive number below indicates a decrease in loss where RMB strengthens 5% (2011: 5%) against the relevant currency. For a 5% (2011: 5%) weakening of RMB against the relevant currency, there would be an equal and opposite impact on the loss and the balances below would be negative.

7. FINANCIAL INSTRUMENTS (Continued)

b. Financial risk management objectives and policies (Continued)

***Market risk** (Continued)*

(i) Currency risk (Continued)

Sensitivity analysis (Continued)

	2012	2011
	HK$'000	HK$'000
Decrease (increase) in loss		
– USD Impact	**(6,975)**	3,341
– EUR Impact	**1,432**	(2,074)
– HK$ Impact	**17,249**	15,656

(ii) Interest rate risk

The Group is exposed to cash flow interest rate risk in relation to variable-rate bank balances and borrowings, and exposed to fair value interest rate risk in relation to pledged deposits for other borrowings, pledged bank deposits, amount due to a director, fixed-rate borrowings, the liability component of convertible notes payable and promissory notes payable.

The Group currently does not have an interest rate hedging policy. However, the management monitors interest rate exposure and will consider hedging significant interest rate exposure should the need arise.

The Group's exposures to interest rates on financial liabilities are detailed in the liquidity risk management section of this note.

7. FINANCIAL INSTRUMENTS (Continued)

b. Financial risk management objectives and policies (Continued)

***Market risk** (Continued)*

(ii) Interest rate risk (Continued)

Sensitivity analysis

The sensitivity analysis below has been determined based on the exposure to interest rates for variable-rate bank balances and borrowings at the end of the reporting period. The analysis is prepared assuming the amounts outstanding at the end of the reporting period were outstanding for the whole year. A 5 and 50 basis points (2011: 5 and 50 basis points) increase or decrease for bank balances and borrowings is used when reporting interest rate risk internally to key management personnel and represents management's assessment of the reasonably possible change in interest rates.

If interest rates had been 50 basis points (2011: 50 basis points) higher/lower for borrowings and all other variables were held constant, the loss for the year ended 31 December 2012 would increase/decrease by approximately HK$1,758,000 (2011: HK$2,637,000).

If interest rate had been 5 basis points (2011: 5 basis points) higher/lower for bank balances, and all other variables were held constant, the loss for the year ended 31 December 2012 would decrease/increase by HK$20,000 (2011: HK$75,000).

(iii) Price risk on investments held for trading

The Group is exposed to equity price risk through its investments held for trading. The Group's equity price risk is mainly concentrated on listed equity instruments quoted in respective stock exchanges. The management manages this exposure by closely monitoring the price risk and maintaining a portfolio of investments with different risks.

7. FINANCIAL INSTRUMENTS (Continued)

b. Financial risk management objectives and policies (Continued)

***Market risk** (Continued)*

(iii) Price risk on investments held for trading (Continued)

Sensitivity analysis

The sensitivity analysis below has been determined based on the exposure to equity price risks of investments held for trading at the end of the reporting period.

If the prices of the respective equity instruments had been 5% higher/lower and all other variables were held constant, loss for the year ended 31 December 2012 would decrease/increase by approximately HK$122,000 (2011: HK$138,000) as a result of the change in fair value of investments held for trading.

Credit risk

As at 31 December 2012, the Group's maximum exposure to credit risk which will cause a financial loss to the Group due to failure to discharge an obligation by the counterparties provided by the Group is arising from the carrying amount of the respective recognised financial assets as stated in the consolidated statement of financial position.

In order to minimise the credit risk, the management of the Group has credit approvals and other monitoring procedures to ensure that follow-up action is taken to recover overdue debts. In addition, the Group reviews the recoverable amount of each individual receivable at the end of each reporting period to ensure that adequate impairment losses are made for irrecoverable amounts. In this regard, the Directors consider that the Group's credit risk on receivables is significantly reduced.

The Group has significant concentration of credit risk on the largest customer as 100% (2011: 75.0%) and significant concentration of credit risk by geographical location in Germany, in which 100% (2011: 99.5%) of total revenue is arisen from a customer in Germany. The Directors consider that the risks will be mitigated by exploring new markets other than Germany.

7. FINANCIAL INSTRUMENTS (Continued)

b. Financial risk management objectives and policies (Continued)

***Credit risk** (Continued)*

The Group has concentration of credit risk on bank deposits and balances as 51.1% (2011: 64.8%) of pledged bank deposits and bank balances and cash which were placed with three banks (2011: three banks).

The credit risk on liquid funds is limited because the counterparties are banks with good reputation.

Operational risk

The Group's exposure to operational risk is primarily attributable to heavy reliance on W. Bockstiegel GmbH & Co. Reederei KG (the "W. Bockstiegel"), the major customer of the Group in Germany. The provision of shipbuilding service to the W. Bockstiegel amounted to approximately HK$1,771,718,000 (2011: HK$1,245,192,000) which accounted for approximately 94.7% (2011: 75%) of the Group's total turnover for the year ended 31 December 2012. The Directors are closely monitoring the performance and financial position of W. Bockstiegel and are planning to expand its shipbuilding service to reduce the concentration of the operational risk.

Liquidity risk

In management of the liquidity risk, the Group monitors and maintains a level of cash and cash equivalents deemed adequate by the management to finance the Group's operations and mitigate the effects of fluctuations in cash flows.

The Group was exposed to liquidity risk at 31 December 2012 as the Group had net current liabilities and net liabilities of approximately HK$1,328,972,000 and HK$723,074,000, respectively. In order to improve the Group's liquidity position, the Directors have been implementing various operating and financing measures, details of which are set out in Note 2 to the consolidated financial statements.

The Group relied on borrowings, convertible notes payable and promissory notes payable as significant sources of liquidity, details of which are set out in Notes 30, 34 and 35 respectively to the consolidated financial statements.

7. FINANCIAL INSTRUMENTS (Continued)

b. Financial risk management objectives and policies (Continued)

***Liquidity risk** (Continued)*

The following table details the Group's remaining contractual maturity for its non-derivative financial liabilities. The table has been drawn up based on the undiscounted cash flows of financial liabilities based on the earliest date on which the Group can be required to pay. Specifically, bank borrowings with repayment on demand clause are included in the earliest time band regardless of the probability of the banks choosing to exercise their rights. The maturity dates for other non-derivative financial liabilities are based on the agreed repayment dates.

Liquidity risk tables

The table includes both interest and principal cash flows. To the extent that interest flows are at floating rate, the undiscounted amount is derived from interest rate at the end of the reporting period.

	Weighted average effective interest rate %	On demand or less than 1 month HK$'000	Over 1 month but less than 3 months HK$'000	Over 3 months but less than 1 year HK$'000	Over 1 year but less than 2 years HK$'000	Over 2 years but less than 5 years HK$'000	Total undiscounted cash flows HK$'000	Carrying amount at 31.12.2012 HK$'000
2012								
Non-derivative financial liabilities								
Trade and other payables	–	680,749	7,921	131,777	–	–	820,447	820,447
Bills payables	–	57,649	30,022	252,050	–	–	339,721	339,721
Amounts due to related parties	7.57	10,625	–	45,678	–	–	56,303	53,285
Amount due to a director	15.00	–	–	934	–	–	934	812
Convertible notes payable								
– liability component (Note)	14.01	–	–	–	225,185	94,994	320,179	278,632
Promissory notes payable (Note)	19.15	–	–	–	–	78,784	78,784	68,713
Borrowings								
– fixed rates	5.60	49,641	12,237	212,371	32,121	–	306,370	287,469
– variable rates	6.81	229,756	46,937	87,492	–	–	364,185	351,615
		1,028,420	97,117	730,302	257,306	173,778	2,286,923	2,200,694

	Weighted average effective interest rate %	On demand or less than 1 month HK$'000	Over 1 month but less than 3 months HK$'000	Over 3 months but less than 1 year HK$'000	Over 1 year but less than 2 years HK$'000	Over 2 years but less than 5 years HK$'000	Total undiscounted cash flows HK$'000	Carrying amount at 31.12.2011 HK$'000
2011								
Non-derivative financial liabilities								
Trade and other payables	–	593,217	38,077	–	–	–	631,294	631,294
Bills payables	–	75,176	73,800	378,771	–	–	527,747	527,747
Amount due to a related party	–	31,588	–	–	–	–	31,588	31,588
Amount due to a director	15.00	–	–	677	–	–	677	615
Deferred consideration	–	–	220,000	–	–	–	220,000	217,268
Convertible notes payable								
– liability component (Note)	20.36	–	–	3,375	3,375	226,688	233,438	157,135
Borrowings								
– fixed rates	7.63	–	44,139	130,134	90,810	31,800	296,883	279,663
– variable rates	7.16	24,733	70,141	216,333	26,208	–	337,415	327,426
		724,714	446,157	729,290	120,393	258,488	2,279,042	2,172,736

Note: The undiscounted amount represents the coupon interest and redemption amount on maturity on the assumption that there was no conversion prior to maturity.

7. FINANCIAL INSTRUMENTS (Continued)

b. Financial risk management objectives and policies (Continued)

***Liquidity risk** (Continued)*

Liquidity risk tables (Continued)

Bank borrowings with repayment on demand clause are included in the "on demand or less than 1 month" time band in the above maturity analysis. At 31 December 2012 and 31 December 2011, there was no principle amount of the Group's bank borrowings with unconditional repayment on demand clause.

The amounts included as above for variable interest rate instruments of non-derivative financial liabilities are subject to change if change in variable interest rates differ to those estimates of interest rate determined at the end of the reporting period.

c. Fair value

The fair value of financial assets and financial liabilities are determined as follows:

- the fair value of financial assets with standard terms and conditions and traded in active liquid markets are determined with reference to quoted market prices;

- the fair value of other financial assets and financial liabilities are determined in accordance with generally accepted pricing models based on discounted cash flow analysis; and

- the fair value of derivative instruments is calculated using option pricing models for optional derivatives.

7. FINANCIAL INSTRUMENTS (Continued)

c. Fair value (Continued)

Excepted as detailed in the following table, the Directors consider that the carrying amount of the financial liabilities recorded at amortised cost in the consolidated financial statement approximate their fair values:

	At 31.12.2012		At 31.12.2011	
	Carrying amount	**Fair value**	Carrying amount	Fair value
	HK$'000	**HK$'000**	HK$'000	HK$'000
Financial liability				
Convertible notes payable				
– liability component	**278,632**	**281,938**	157,135	153,890
Promissory notes payable	**68,713**	**63,873**	–	–

The fair value of the financial liabilities was derived from discounted rate applicable to the financial liabilities at end of the reporting period, the input was as follow:

	At 31.12.2012	At 31.12.2011
Convertible notes payable – liability component	**14.01% p.a.**	20.36% p.a.
Promissory notes payable	**19.15% p.a.**	N/A

The following table provides an analysis of financial instruments that are measured subsequent to initial recognition at fair value, grouped into Levels 1 to 3 based on the degree to which the fair value is observable.

- Level 1: fair value measurements are those derived from quoted prices (unadjusted) in active market for identical assets or liabilities;

7. FINANCIAL INSTRUMENTS (Continued)

c. Fair value (Continued)

- Level 2: fair value measurements are those derived from inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices);

- Level 3: fair value measurements are those derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data (unobservable inputs).

	At 31.12.2012			
	Level 1	**Level 2**	**Level 3**	**Total**
	HK$'000	**HK$'000**	**HK$'000**	**HK$'000**
Financial asset at FVTPL				
Non-derivative financial assets held for trading	**2,430**	**–**	**–**	**2,430**
Financial liability at FVTPL				
Convertible notes payable	**–**	**281,938**	**–**	**291,938**

	At 31.12.2011			
	Level 1	Level 2	Level 3	Total
	HK$'000	HK$'000	HK$'000	HK$'000
Financial asset at FVTPL				
Non-derivative financial assets held for trading	2,750	–	–	2,750
Financial liability at FVTPL				
Convertible notes payable	–	153,890	–	153,890

There were no transfers between Level 1, 2 and 3 in the current and prior years.

8. REVENUE AND SEGMENT INFORMATION

Information reported to the board of Directors, being the chief operating decision maker, for the purposes of resource allocation and assessment of segment performance focuses on types of goods or services delivered or provided. This is also the basis upon which the Group is organised and managed. No operating segments identified by the chief operating decision maker have been aggregated in arriving at the reportable segments of the Group.

Specifically, the Group's reportable and operating segments under HKFRS 8 *Operating Segments* are as follows:

a) Shipbuilding – provision of shipbuilding services under shipbuilding construction contracts and operated in the PRC.

b) Trading business – provision of trading and operated in Hong Kong.

Segment revenues and results

The following is an analysis of the Group's revenue and results by reportable and operating segment.

For the year ended 31 December 2012

	Shipbuilding HK$'000	Trading business HK$'000	Total HK$'000
Segment revenue	1,870,304	–	1,870,304
Segment result	(200,294)	–	(200,294)
Unallocated other income			1,179
Unallocated other gains and losses			(1,448)
Change in fair value of investments held for trading			(320)
Loss on fair value change of convertible notes payable			(20,949)
Gain on settlement of deferred consideration			52,936
Finance costs			(182,100)
Unallocated corporate expenses			(17,098)
Loss before tax			(368,094)

8. REVENUE AND SEGMENT INFORMATION (Continued)

Segment revenues and results (Continued)

For the year ended 31 December 2011

	Shipbuilding HK$'000	Trading business HK$'000	Total HK$'000
Segment revenue	1,660,254	–	1,660,254
Segment result	(510,273)	(264)	(510,537)
Unallocated other income			(258)
Unallocated other gains & losses			4,708
Change in fair value of investments held for trading			(1,188)
Gain on modification of convertible notes payable			4,262
Gain on fair value change of convertible notes payable			51,389
Loss on extinguishment of convertible notes payable			(7,241)
Finance costs			(174,370)
Unallocated corporate expenses			(14,510)
Loss before tax			(647,745)

The accounting policies of the operating segments are the same as the Group's accounting policies described in Note 4. Segment result represents the loss from each segment without allocation of certain other income, other gains or losses, change in fair value of investments held for trading, gain (loss) on modification and fair value change of convertible notes payable, loss on extinguishment of convertible notes payable, gain on settlement of deferred consideration, certain corporate expenses and finance costs. This is the measure reported to the chief operating decision maker for the purposes of resource allocation and performance assessment.

8. REVENUE AND SEGMENT INFORMATION (Continued)

Segment assets and liabilities

The following is an analysis of the Group's assets and liabilities by reportable and operating segment:

	2012 HK$'000	2011 HK$'000
Assets		
Segment assets		
– Shipbuilding	**1,837,141**	2,613,510
– Trading business	**–**	21
Total segment assets	**1,837,141**	2,613,531
Pledged deposits for other borrowings	**33,000**	32,472
Pledged bank deposits and bank balances and cash	**309,301**	511,347
Unallocated corporate assets	**8,872**	11,932
Consolidated assets	**2,188,314**	3,169,282
Liabilities		
Segment liabilities		
– Shipbuilding	**1,820,638**	2,470,380
– Trading business	**–**	–
Total segment liabilities	**1,820,638**	2,470,380
Borrowings	**639,084**	607,089
Deferred consideration	**–**	217,268
Convertible notes payable	**278,632**	157,135
Promissory notes payable	**68,713**	–
Deferred tax liabilities	**93,649**	114,348
Unallocated corporate liabilities	**10,672**	4,457
Consolidated liabilities	**2,911,388**	3,570,677

8. REVENUE AND SEGMENT INFORMATION (Continued)

Segment assets and liabilities (Continued)

For the purposes of monitoring segment performances and allocating resources between segments:

- all assets are allocated to operating segments other than pledged deposits for other borrowings, pledged bank deposits, bank balances and cash, certain corporate property, plant and equipment and tax recoverable; and

- all liabilities are allocated to operating segments other than borrowings, deferred consideration, convertible notes payable, promissory notes payable, deferred tax liabilities and certain other payables and accruals.

Geographical information

Information about the Group's revenue from external customers is presented based on the location of customers. Information about the Group' non-current assets by geographical locations are detailed below:

Name of the country	Revenue from external customers Year ended 31 December 2012 HK$'000	2011 HK$'000	Non-current assets at 31 December 2012 HK$'000	2011 HK$'000
Germany	**1,870,304**	1,651,520	**–**	–
United States of America	**–**	8,734	**–**	–
The PRC	**–**	–	**1,077,471**	1,057,455
Others	**–**	–	**501**	870
	1,870,304	1,660,254	**1,077,972**	1,058,325

8. REVENUE AND SEGMENT INFORMATION (Continued)

Other segment information

Year ended 31 December 2012

Amounts included in the measure of segment result or segment assets:

	Shipbuilding HK$'000	Trading business HK$'000	Unallocated HK$'000	Total HK$'000
Additions to property, plant and equipment	32,982	–	165	33,147
Depreciation of property, plant and equipment	58,362	–	535	58,897
Impairment loss recognised in respect of property, plant and equipment	90,617	–	–	90,617
Amortisation of prepaid lease payments	7,234	–	–	7,234
Written-off of property, plant and equipment	7,001	–	–	7,001
Additional provision for warranty	35,530	–	–	35,530
Foreseeable losses recognised in respect of additional estimated costs	94,142	–	–	94,142
Impairment loss recognised in respect of trade receivables	794	–	–	794
Impairment loss recognised in respect of other receivables	1,090	–	–	1,090

Amounts regularly provided to the chief operating decision maker but not included in the measure of segment result:

	Shipbuilding HK$'000	Trading business HK$'000	Unallocated HK$'000	Total HK$'000
Income tax credit	–	–	(23,993)	(23,993)

8. REVENUE AND SEGMENT INFORMATION (Continued)

Other segment information (Continued)

Year ended 31 December 2011

Amounts included in the measure of segment result or segment assets:

	Shipbuilding HK$'000	Trading business HK$'000	Unallocated HK$'000	Total HK$'000
Additions to property, plant and equipment	19,965	–	6	19,971
Depreciation of property, plant and equipment	66,387	–	501	66,888
Impairment loss recognised in respect of property, plant and equipment	415,365	–	–	415,365
Amortisation of prepaid lease payments	7,167	–	–	7,167
Gain on disposal of property, plant and equipment	200	–	–	200
Additional provision for warranty	25,366	–	–	25,366
Foreseeable losses recognised in respect of additional estimated costs	47,380	–	–	47,380

Amounts regularly provided to the chief operating decision maker but not included in the measure of segment result:

	Shipbuilding HK$'000	Trading business HK$'000	Unallocated HK$'000	Total HK$'000
Income tax credit	–	–	(105,186)	(105,186)

8. REVENUE AND SEGMENT INFORMATION (Continued)

Information about major customers

Revenue from customers of the corresponding years contributing over 10% of the total revenue of the Group are as follows:

	Year ended 2012 HK$'000	Year ended 2011 HK$'000
Customer A[1]	1,771,718	1,245,192
Customer B[1]	N/A[2]	175,869

[1] Revenue from shipbuilding

[2] The corresponding revenue did not contribute over 10% of the total revenue of the Group in the respective year.

9. OTHER INCOME

	2012 HK$'000	2011 HK$'000
Interests on bank deposits	3,986	8,908
Sales of scrap materials	3,655	7,428
Government grants	2,865	172
Others	1,856	30
	12,362	16,538

10. OTHER GAINS AND LOSSES

	2012 HK$'000	2011 HK$'000
Gain on disposal of property, plant and equipment	–	200
Written-off of property, plant and equipment	(7,001)	–
Foreign exchange gain	5,553	4,508
	(1,448)	4,708

11. FINANCE COSTS

	2012 HK$'000	2011 HK$'000 (Restated)
Interests on borrowings wholly repayable within five years:		
Convertible notes payable at effective interest rates (Note 34)	41,547	29,490
Imputed interest expense on deferred consideration (Note 32)	2,643	29,725
Promissory notes payable at effective interest rates (Note 35)	10,071	–
Interest on bank borrowings and bill payables	67,564	68,151
Interest on other borrowings	25,337	9,956
Guarantee fee incurred in connection with bank borrowings	25,486	29,308
Overdue interests	9,442	4,041
Arrangement fee incurred in connection with other borrowings	–	3,342
Others	10	357
	182,100	174,370

12. LOSS BEFORE TAX

	2012 HK$'000	2011 HK$'000
Loss before tax has been arrived at after charging:		
Directors' and chief executives' emoluments (Note 14)	**4,752**	4,580
Other staff costs:		
Salaries and other benefits	**66,905**	66,862
Contributions to retirement benefits scheme	**10,221**	6,586
Total staff costs	**81,878**	78,028
Auditor's remuneration		
– Current year (including non-audit service of HK$180,000 (2011: HK$240,000))	**1,180**	1,240
– Under-provision for previous year	**–**	250
	1,180	1,490
Depreciation of property, plant and equipment	**58,897**	66,888
Amortisation of prepaid lease payments	**7,234**	7,167
Minimum lease payments under operating leases in respect of rented premises	**2,005**	1,454
Shipbuilding contract costs recognised as expenses	**1,909,483**	1,701,733
Foreseeable losses recognised in respect of additional estimated costs (included in shipbuilding contract cost and recognised as cost of sales)	**94,142**	47,380
Impairment loss recognised in respect of trade receivables	**794**	–
Impairment loss recognised in respect of other receivables	**1,090**	–

13. INCOME TAX CREDIT

	2012 HK$'000	2011 HK$'000
Current tax	–	–
Deferred tax (Note 36)	(23,993)	(105,186)
	(23,993)	(105,186)

No provision for Hong Kong Profits Tax has been made since the Group has no assessable profits for both years.

Under the law of the PRC on Enterprise Income Tax ("EIT") and Implementation Regulation of the PRC EIT Law, the tax rate of the PRC subsidiaries is 25% from 1 January 2008 onwards.

Income tax credit for the year can be reconciled to the loss before tax per the consolidated statement of comprehensive income as follows:

	2012 HK$'000	2011 HK$'000
Loss before tax	(368,094)	(647,745)
Tax at applicable domestic income tax rate of 25% (2011: 25%)	(92,024)	(161,936)
Tax effect of expenses not deductible for tax purpose	78,770	67,602
Tax effect of income not taxable for tax purpose	(14,857)	(14,528)
Tax effect of tax loss not recognised	2,718	2,426
Effect of different tax rates of subsidiaries operating in other jurisdiction	1,400	1,250
Income tax credit for the year	(23,993)	(105,186)

14. DIRECTORS' AND CHIEF EXECUTIVES' EMOLUMENTS

	Year ended 31 December 2012				Year ended 31 December 2011			
	Fees HK$'000	Salaries and other benefits HK$'000	Contributions to retirement benefits scheme HK$'000	Total HK$'000	Fees HK$'000	Salaries and other benefits HK$'000	Contributions to retirement benefits scheme HK$'000	Total HK$'000
Executive directors:								
Mr. Chau On Ta Yuen *(Chairman)*	–	1,402	14	1,416	–	1,306	12	1,318
Mr. Li Ming *(Deputy Chairman and Chief Executive Officer)*	–	1,293	14	1,307	–	1,206	12	1,218
Mr. Zhang Shi Hong	–	1,049	14	1,063	–	965	12	977
Mr. Wang San Long	–	685	2	687	–	787	2	789
Independent non-executive directors:								
Mr. Hu Bai He	93	–	–	93	80	–	–	80
Ms. Xiang Siying	93	–	–	93	80	–	–	80
Mr. Zhang Xi Ping*	–	–	–	–	38	–	–	38
Ms. Xiang Ying	93	–	–	93	80	–	–	80
	279	4,429	44	4,752	278	4,264	38	4,580

* Mr. Zhang Xi Ping was resigned on 23 June 2011.

No emoluments were paid by Group to any of the Directors or chief executives, as an inducement to join or joining the Group or as compensation for loss of office. Neither the Directors nor any of the chief executives waived any emoluments in both years. Apart from Directors, the Group has not classified any other person as chief executives during the year ended 31 December 2012 and 2011.

15. EMPLOYEES' EMOLUMENTS

Of the five individuals with the highest emoluments in the Group, three (2011: four) were Directors whose emoluments are included in Note 14 above. The emoluments of the remaining two (2011: one) highest paid individuals were as follows:

	2012 HK$'000	2011 HK$'000
Salaries and other benefits	1,704	764
Contributions to retirement benefits scheme	14	12
	1,718	776

15. EMPLOYEES' EMOLUMENTS (Continued)

Their emoluments were within the following band:

	Number of employee 2012	2011
Nil to HK$1,000,000	**2**	1

No emoluments were paid by the Group to any of the five highest paid employees as an inducement to join or upon joining the Group or as compensation for loss of office. None of the five highest paid employees waived any emoluments in both years.

16. LOSS PER SHARE

The calculation of the basic and diluted loss per share attributable to owners of the Company is based on the following data:

	2012 HK$'000	2011 HK$'000
Loss		
Loss for the year attributable to owners of the Company for the purposes of basic and diluted loss per share	**(344,101)**	(542,559)

	2012 '000	2011 '000
Number of shares		
Weighted average number of ordinary shares for the purposes of basic and diluted loss per share	**3,667,995**	3,524,785

The computation of diluted loss per share for the years ended 31 December 2012 and 2011 does not include the outstanding share options and convertible notes as the assumed exercise has an anti-dilutive effect.

17. PROPERTY, PLANT AND EQUIPMENT

	Buildings HK$'000	Furniture and fixtures HK$'000	Motor vehicles HK$'000	Plant and machinery HK$'000	Construction in progress HK$'000	Total HK$'000
COST						
At 1 January 2011	917,725	5,390	27,489	110,703	186,451	1,247,758
Exchange adjustments	43,371	236	1,210	5,734	7,471	58,022
Additions	–	6	140	4,737	15,088	19,971
Transfer	37,009	–	1,938	37,464	(76,411)	–
Disposals	(157)	–	–	(6)	–	(163)
At 31 December 2011	997,948	5,632	30,777	158,632	132,599	1,325,588
Exchange adjustments	25,034	83	388	3,389	–	28,894
Additions	165	–	–	15	32,967	33,147
Transfer	103,895	–	–	61,671	(165,566)	–
Written-off	–	(325)	(5,142)	(11,879)	–	(17,346)
At 31 December 2012	**1,127,042**	**5,390**	**26,023**	**211,828**	**–**	**1,370,283**
ACCUMULATED DEPRECIATION AND IMPAIRMENT						
At 1 January 2011	110,257	1,675	9,594	30,367	–	151,893
Exchange adjustments	5,851	77	451	1,576	–	7,955
Depreciation provided for the year	50,851	345	3,930	11,762	–	66,888
Impairment loss recognised in the year	412,734	–	–	2,631	–	415,365
Eliminated on disposals	(35)	–	–	(3)	–	(38)
At 31 December 2011	579,658	2,097	13,975	46,333	–	642,063
Exchange adjustments	10,327	36	219	923	–	11,505
Depreciation provided for the year	36,855	595	4,209	17,238	–	58,897
Impairment loss recognised in the year	90,617	–	–	–	–	90,617
Written-off	–	(304)	(3,004)	(7,037)	–	(10,345)
At 31 December 2012	**717,457**	**2,424**	**15,399**	**57,457**	**–**	**792,737**
CARRYING VALUES						
At 31 December 2012	**409,585**	**2,966**	**10,624**	**154,371**	**–**	**577,546**
At 31 December 2011	418,290	3,535	16,802	112,299	132,599	683,525

17. PROPERTY, PLANT AND EQUIPMENT (Continued)

The above items of property, plant and equipment, except for construction in progress are depreciated on a straight-line basis at the following rates per annum:

Buildings	Over the shorter of the term of the lease, or 5%
Furniture and fixtures	20%
Motor vehicles	12.5%
Plant and machinery	6.67% – 25%

At 31 December 2012 and 2011, the buildings of the Group are situated on land in the PRC under medium-term land use right.

For the years ended 31 December 2012 and 2011, the Directors, after taking into account the economic condition and industrial development prospect, had considered that the gross operating loss incurred during the years indicated impairment loss for the Group's property, plant and equipment and therefore conducted an impairment review on the carrying amounts of the property, plant and equipment.

The Directors appointed an independent professional valuer, BMI Appraisals Limited, to perform a valuation on the property, plant and equipment as at 31 December 2012, then, an impairment loss of approximately HK$90,617,000 (2011: HK$415,365,000) has been made according to the excess of the aggregate carrying amounts of the property, plant and equipment as at 31 December 2012 over the recoverable amount based on the valuation report dated 27 March 2013. The value-in-use calculation is based on a post-tax discount rate of 14.02% (2011: 15.14%) and cash flow projections prepared from financial forecasts approved by the management of the Group, taking into account of the current economic condition and operation of shipbuilding industry. Other key assumptions for the value-in-use calculations relate to the estimation of cash inflows/outflows which include budgeted sales and gross margin. Such estimation is based on the management's expectations for the market development.

At 31 December 2012, the carrying values of plant and machinery of approximately HK$154,371,000 (2011: HK$112,299,000) and certain buildings with ownership certificates of approximately HK$409,585,000 (2011: HK$287,328,000) have been pledged to a bank and a financial institution in the PRC to secure the Group's borrowings (Note 38).

18. PREPAID LEASE PAYMENTS

The Group's prepaid lease payments comprise:

	2012 HK$'000	2011 HK$'000
Leasehold land held under medium-term lease in the PRC	**335,136**	341,034
Analysed for reporting purposes as:		
Non-current asset	**333,226**	339,192
Current asset	**1,910**	1,842
	335,136	341,034

At 31 December 2012, the Group's prepaid lease payments with carrying value of approximately HK$335,136,000 (2011: HK$341,034,000) have been pledged to various banks to secure the Group's borrowings (Note 38).

Application for land use right certificate of the lake located in Xiachao Lake Ruichang City Jiangxi Province (the "Lake") with aggregate carrying values of approximately HK$170,661,000 (2011: HK$173,664,000) was still in progress and the land use right certificate had not been issued to the Group by the relevant government authorities at 31 December 2012.

The Directors are of the opinion that the Group has acquired the beneficial title to the Lake at the end of the reporting period, and the land use right certificate can be obtained upon the settlement of the purchase consideration.

18. PREPAID LEASE PAYMENTS (Continued)

For the years ended 31 December 2012 and 2011, the Directors, after taking into account the economic condition and industrial development prospect, had considered that the gross operating loss incurred during the years indicated impairment loss for the Group's prepaid lease payments and therefore conducted an impairment review on the carrying amounts of prepaid lease payments.

The Directors appointed an independent professional valuer, BMI Appraisals Limited, to perform a valuation on the prepaid lease payments at 31 December 2012 and no impairment loss (2011: HK$Nil) was considered necessary as the market value of the prepaid lease payments was amounting to approximately HK$390,000,000 (equivalent to RMB312,000,000) (2011: HK$384,900,000 (equivalent to RMB313,000,000)) based on the valuation report dated 27 March 2013, which was exceed the carrying value of prepaid lease payments. The market value is calculated by comparison approach assuming sale with the benefit of vacant possession and by making reference to comparable sales evidences as available in the relevant market. Other key assumptions for the prepaid lease payments valuation relate to (i) the property is sold in the market without the benefit of deferred terms contract, leaseback, joint venture, management agreement or any other similar arrangement; (ii) no account has been taken of any option or right of pre-emption concerning or effecting the sale of the property and no forced sale situation in any manner; and (iii) the proper title certificates of the property have been obtained and the property could be transferred with its residual term of land use rights at no extra land premium or other onerous payment payable to the government.

19. INTANGIBLE ASSETS

	Contracted and uncontracted customer relationships HK$'000
COST	
At 1 January 2011	1,720,453
Exchange adjustments	78,281
At 31 December 2011	1,798,734
Exchange adjustments	29,248
At 31 December 2012	**1,827,982**
ACCUMULATED AMORTISATION AND IMPAIRMENT	
At 1 January 2011	1,720,453
Exchange adjustments	78,281
At 31 December 2011	1,798,734
Exchange adjustments	29,248
At 31 December 2012	**1,827,982**
CARRYING VALUES	
At 31 December 2012 and 31 December 2011	–

Intangible assets represent contracted and uncontracted customer relationships arising from the acquisition of INPAX Group (as defined in Note 34) during the year ended 31 December 2008.

Intangible assets are amortised over its estimated useful life of 10 years on a straight-line basis.

20. PLEDGED DEPOSITS FOR OTHER BORROWINGS

In August 2010, a borrowing of approximately HK$141 million (equivalent to RMB120 million) was granted to the Group by a financial institution in the PRC. Deposit amounting to approximately HK$33 million (equivalent to approximately RMB26.4 million) at 31 December 2012 (2011: approximately HK$32.5 million (equivalent to approximately RMB26.4 million)) was pledged to secure this borrowing, which will be released on the maturity date of this borrowing in August 2014. Accordingly, the deposit is classified as non-current.

21. INVENTORIES

	2012	2011
	HK$'000	HK$'000
Raw materials	**122,018**	180,369

At 31 December 2012, the Group's inventories with carrying value of approximately HK$50,911,000 (2011: HK$156,618,000) have been pledged to various banks to secure the Group's borrowings (Note 38).

22. TRADE RECEIVABLES – NON-CURRENT PORTION AND CURRENT PORTION / BILLS AND OTHER RECEIVABLES / PREPAYMENT FOR PURCHASE OF RAW MATERIALS

	2012 HK$'000	2011 HK$'000
Trade receivables – non-current portion	**134,200**	–
Trade receivables – current portion	**16,544**	39,929
Less: Allowance for doubtful debts	**(794)**	(39,929)
Trade receivables – current portion, net	**15,750**	–
Total trade receivables, net of allowance for doubtful debts (Note a)	**149,950**	–
Value-added tax recoverable (Note b)	**148,225**	258,935
Bills receivables	**–**	394
Deposits placed with a stakeholder (Note c)	**1,085**	157,324
Deposits placed to a guarantor (Note d)	**75,000**	73,800
Deposit paid for acquisition of property, plant and equipment (Note e)	**3,332**	–
Other receivables	**95,138**	87,029
Total bills and other receivables	**322,780**	577,482
Prepayment for purchase of raw materials (Note f)	**324,397**	818,869

Notes:

(a) At 31 December 2012, trade receivables of approximately HK$149,950,000 (equivalent to USD19,000,000) represent the deferred final receivable from a ship buyer, an independent third party of the Group, in relation to the final payments for the acquisition of seven vessels from the Group, by five instalments in 5.5 years.

(b) At 31 December 2012 and 2011, the Group's value-added tax recoverable has been pledged to a bank to secure the Group's bank borrowings (Note 38).

22. TRADE RECEIVABLES – NON-CURRENT PORTION AND CURRENT PORTION / BILLS AND OTHER RECEIVABLES / PREPAYMENT FOR PURCHASE OF RAW MATERIALS (Continued)

Notes: (Continued)

(c) Certain vessel buyers have made progress payments for ship construction contracts to a stakeholder rather than directly to the Group. The Group has the entitlement to these progress payments in accordance with the contracts but they are placed under custody of the stakeholder to ensure these progress payments are used to pay for the costs incurred by the Group relevant to shipbuilding construction contracts. The progress payments in custody will be paid over to the Group based on the shipbuilding contract.

(d) Guarantees have been given by an independent third party in relation to the banking facilities granted to the Group. Guarantee deposits were approximately HK$75,000,000 (equivalent to RMB60,000,000) at 31 December 2012 (2011: HK$73,800,000 (equivalent to RMB60,000,000)).

(e) Deposit paid for acquisition of property, plant and equipment was the purchase consideration paid for the property owned by a property developer in September 2008 at approximately HK$3,332,000 (equivalent to RMB2,665,700) which located in the city of Nanchang, which recorded as deposit paid for acquisition of property, plant and equipment separately under non-current asset at 31 December 2011 amounting to approximately HK$3,136,000. The premises permit has not yet obtained and the ownership of property have not been transferred to the Group as at 31 December 2012. Under this circumstance, the Directors intent to terminate the acquisition agreement and the management is in negotiation with the property developer to refund the deposit paid. The Directors are of the opinion that the balances could be fully recoverable from the property developer within one year and is therefore reclassified the balance as current asset as at 31 December 2012.

(f) Prepayment for purchase of raw materials represents amount paid for purchase of steel plates and vessel components for shipbuilding but not yet delivered to the Group at the end of the reporting period.

The following is an aged analysis of trade receivables, net of allowance for doubtful debts, presented based on delivery date at the end of the reporting periods:

	2012	2011
	HK$'000	HK$'000
Within three months	**23,625**	–
More than three months but not more than one year	**126,325**	–
	149,950	–

The Group did not have trade receivables that were overdue but not impaired at 31 December 2012 and 31 December 2011.

The Directors consider that the carrying amounts of trade, bills and other receivables approximated to their fair values.

22. TRADE RECEIVABLES – NON-CURRENT PORTION AND CURRENT PORTION / BILLS AND OTHER RECEIVABLES / PREPAYMENT FOR PURCHASE OF RAW MATERIALS (Continued)

Movement in the allowance for doubtful debts for trade receivables:

	2012 HK$'000	2011 HK$'000
At 1 January	**39,929**	39,929
Impairment loss recognised	**794**	–
Amounts written-off as uncollectible	**(39,929)**	–
At 31 December	**794**	39,929

At the end of the reporting period, the Group's trade receivables were individually determined to be impaired.

Movement in the allowance for doubtful debts for other receivables:

	2012 HK$'000	2011 HK$'000
At 1 January	**–**	–
Impairment loss recognised	**1,090**	–
At 31 December	**1,090**	–

Included in trade receivables, other receivables, deposits placed with a stakeholder and prepayment for purchase of raw materials are the following amounts denominated in a currency other than the functional currency of the Group:

	2012 '000	2011 '000
USD	**25,272**	22,365
EUR	**7,718**	35,686

23. INVESTMENTS HELD FOR TRADING

	2012 HK$'000	2011 HK$'000
Listed securities:		
Equity securities listed in Hong Kong	**2,430**	2,750

The securities are measured at fair value based on quoted market prices from the Stock Exchange.

24. AVAILABLE-FOR-SALE INVESTMENTS

	2012 HK$'000	2011 HK$'000
Unlisted investments:		
Unlisted equity investments in PRC	**6,250**	–

During the year ended 31 December 2012, Jiangxi Jiangzhou Union Shipbuilding Co., Ltd., the wholly-owned subsidiary of the Company, contributed 10% issued capital in Jiujiang Jiangzhou Heavy Industry Co. Ltd ("Jiujiang Heavy"). Jiujiang Heavy is an unlisted company established in the PRC and is not yet commenced business at 31 December 2012.

The available-for-sale investments is measured at cost less accumulated impairment at the end of the reporting period because there is no quoted market price available and the range of reasonable fair values estimates is so significant that the Directors are of the opinion that their fair values cannot be measured reliably.

The Directors are of the opinion that the investments is classified as current asset as the 10% issued capital of Jiujiang Heavy are expected to sell to an independent third party, at a consideration of RMB5,000,000 in 2013. As the carrying amounts of available-for-sale investments approximated to their fair values and no impairment was considered necessary.

25. PLEDGED BANK DEPOSITS / BANK BALANCES AND CASH

Bank balances carry interest at market rates which range from 0.01% to 0.35% (2011: from 0.01% to 0.50%) per annum.

The pledged bank deposits carry fixed interest rate of 2.60% (2011: 2.60%) per annum and were pledged for secured bills payables as required by the relevant banks (Note 38).

Included in the pledged bank deposits and bank balances and cash are the following amounts denominated in a currency other than the functional currency of the Group:

	2012 '000	2011 '000
USD	5,743	694
EUR	458	3,657

26. TRADE, BILLS AND OTHER PAYABLES

	2012 HK$'000	2011 HK$'000
Trade payables	140,535	78,904
Bills payables	339,721	527,747
	480,256	606,651
Advances from customers for shipbuilding contracts not yet commenced construction	–	277,287
Refund to customers for unshaped vessels written-off (Note i and 41)	372,338	366,381
Interest payable	2,111	2,111
Dividend payable to former owners of a subsidiary	554	23,425
Consideration payable for acquisition of prepaid lease payments	47,145	46,391
Accrual of guarantee fee to a guarantor (Note ii and iii)	12,671	11,631
Contribution payables to labour union and education funds	9,439	7,603
Accrual of contractor fees	27,642	20,300
Accrual of government funds	33,541	7,380
Other payables and accruals (Note iv)	175,025	90,593
	1,160,722	1,459,753

26. TRADE, BILLS AND OTHER PAYABLES (Continued)

Notes:

(i) At 31 December 2012, the Group has one (2011: one) arbitration proceeding in progress with one (2011: one) vessel owner in respect of three (2011: three) vessels over the validity of the rescission notices.

If the result of the arbitration is unfavourable to the Group, the Group will be required to return the principal payments for the shipbuilding contracts of the vessels in arbitration and to pay interests for the principal payments calculated in accordance with the relevant shipbuilding contracts, which amount to approximately HK$372,338,000 (2011: HK$366,381,000) in aggregate, to the relevant vessel owner at 31 December 2012.

(ii) The amount due to an independent third party of approximately HK$11,820,000 (equivalent to RMB9,456,000) at year ended 31 December 2012 (2011: approximately HK$11,631,000 (equivalent to RMB9,456,000)), who provided guarantee in respect of the banking facilities granted to the Group.

(iii) The amount due to China Ruilian Holding Corporate ("China Ruilian") of approximately HK$851,000 (equivalent to RMB681,000) at 31 December 2012 in relation to the shipbuilding services including guarantee issued by China Ruilian for the Group's entering of certain shipbuilding contracts. (2011: amount due to related parties approximately HK$31,588,000 (equivalent to RMB25,681,000)).

(iv) Material balances included in other payables and accruals are as follow:

(a) The Group has entered into a loan agreement of HK$50,000,000 (equivalent to RMB40,000,000) with an independent third party in July 2012. The amount is unsecured, interest free and had been repaid in 2013.

(b) The Group has advances from an independent third party of HK$12,500,000 (equivalent to RMB10,000,000) at 31 December 2012. The amount is unsecured, interest free and repayable on demand. (2011: HK$12,300,000 (equivalent to RMB10,000,000)).

(c) The Group has an accrual of land use tax of approximately HK$13,960,000 (equivalent to approximately RMB11,170,000) at 31 December 2012 (2011: approximately HK$6,770,000 (equivalent to RMB5,500,000)).

(d) The Group has an accrual of salaries of approximately HK$13,680,000 (equivalent to approximately RMB10,940,000) at 31 December 2012 (2011: approximately HK$4,820,000 (equivalent to approximately RMB3,920,000)).

(e) The Group has an accrual of social security for and on behalf of its employees of approximately HK$18,125,000 (equivalent to approximately RMB14,500,000) (2011: approximately HK$4,420,000 (equivalent to approximately RMB3,590,000)) at 31 December 2012. Pursuant to a settlement agreement signed between Jiangxi Jiangzhou Union Shipbuilding Co., Ltd., and the relevant government authority on 12 March 2013. The amounts of accrued social security shall be repaid before June 2014.

26. TRADE, BILLS AND OTHER PAYABLES (Continued)

The following is an aged analysis of trade and bills payables presented based on invoice date or issue date, respectively, at the end of the reporting periods:

	2012 HK$'000	2011 HK$'000
0 – 30 days	**153,932**	232,378
31 – 60 days	**124,039**	123,039
61 – 90 days	**38,168**	66,884
Over 90 days	**164,117**	184,350
	480,256	606,651

Bills payables are secured by pledged bank deposits (Note 38).

Trade payables are unsecured, non-interest bearing and repayable on demand.

Included in the trade payables are the following amounts denominated in a currency other than the functional currency of the Group:

	2012 '000	2011 '000
USD	**–**	99
EUR	**–**	6

27. AMOUNTS DUE FROM (TO) CUSTOMERS FOR CONTRACT WORK

	2012 HK$'000	2011 HK$'000
Contracts in progress at the end of the reporting period:		
Contract costs incurred to date	**942,575**	1,681,825
Recognised profits less recognised losses	**(163,990)**	(151,825)
	778,585	1,530,000
Less: progress payments and progress billings	**(1,359,546)**	(2,474,635)
	(580,961)	(944,635)
Analysed for reporting purposes as:		
Amounts due from customers for contract work	**–**	12,880
Amounts due to customers for contract work	**(580,961)**	(957,515)
	(580,961)	(944,635)

During the year ended 31 December 2012 and 31 December 2011, the inactive demand for new vessels, rising labour and materials costs and appreciation of RMB continue to impact the Group's shipbuilding business.

28. AMOUNTS DUE TO RELATED PARTIES

The amounts are unsecured and repayable on demand.

29. AMOUNT DUE TO A DIRECTOR

The amount is unsecured, interest bearing of 15% (2011: 15%) per annum and will be repayable in August 2013 (2011: August 2012).

30. BORROWINGS

	2012	2011
	HK$'000	HK$'000
Bank borrowings	**274,619**	384,685
Other borrowings	**364,465**	222,404
	639,084	607,089
Secured	**210,267**	236,541
Unsecured	**428,817**	370,548
	639,084	607,089

At the end of the reporting period, the above borrowings were repayable as follows:

	2012	2011
Within one year	**608,004**	538,117
More than one year but not more than two years	**31,080**	38,603
More than two years but not more than five years	**–**	30,369
	639,084	607,089
Less: Amounts due within one year shown under current liabilities	**(608,004)**	(538,117)
Amounts due after one year shown under non-current liabilities	**31,080**	68,972

30. BORROWINGS (Continued)

The exposure of the Group's fixed-rate borrowings and the contractual maturity dates were as follows:

	2012 HK$'000	2011 HK$'000
Fixed-rate borrowings:		
Within one year	**256,389**	210,691
More than one year but not more than two years	**31,080**	38,603
More than two years but not more than five years	**–**	30,369
	287,469	279,663

The exposure of the Group's variable-rate borrowings and the contractual maturity dates were as follows:

	2012 HK$'000	2011 HK$'000
Variable-rate borrowings:		
Within one year	**351,615**	327,426

The ranges of effective interest rates (which are also equal to contracted interest rates) on the Group's borrowings are as follows:

Effective interest rates:

	2012	2011
Fixed-rate borrowings (bank and other borrowings)	**3%-15%**	5.10% to 15%
Variable-rate borrowings (bank and other borrowings)	**5.54%-10.8%**	5.35% to 8.53%

30. BORROWINGS (Continued)

During the year ended 31 December 2010, the Group obtained a new borrowing of approximately HK$141,000,000 (equivalent to RMB120,000,000), which will be repayable in 16 quarterly instalments commencing from August 2010. The borrowing carries interest of 5.34% per annum. The proceeds were used to finance the daily operation of the Group and were secured by the bank deposits of approximately HK$33,000,000 and HK$32,472,000 (equivalent to RMB26,400,000) at 31 December 2012 and 2011 respectively. At 31 December 2012, the Group has balance of approximately HK$70,648,000 (equivalent to RMB56,518,000) (2011: approximately HK$105,915,000 (equivalent to RMB86,110,000)).

During the year ended 31 December 2012, the Group obtained several new fixed-rate borrowings in aggregated of approximately HK$57,389,000 (equivalent to approximately USD7,065,000) (2011: approximately HK$77,547,000 (equivalent to approximately USD9,956,000)) which will be repayable within 100-180 days. The borrowings carry interest of a range from 5.6% to 5.8% per annum (2011: range from 5.6% to 5.9% per annum).

At 31 December 2012, the Group has a balance of loan advances from employees of approximately HK$38,563,000 (equivalent to RMB30,850,000) (2011: approximately HK$39,348,000 (equivalent to RMB31,990,000)) which bears interest rate of 15% per annum and will be repayable in August 2013. The proceeds were used to finance the daily operation of the Group.

During the year ended 31 December 2012, Jiangxi Jiangzhou Union Shipbuilding Co. Ltd., had entered into the cooperation agreement with the independent third parties for the construction of six vessels. Pursuant to the cooperation agreement, the independent third parties had paid deposit for approximately HK$197,865,000 (equivalent to RMB158,292,000) to Jiangxi Jiangzhou Union Shipbuilding Co. Ltd.. Before the commencement of the shipbuilding process, the deposit was carried interest at 90% of benchmark rate on The People's Bank of China. As at 31 December 2012, Jiangxi Jiangzhou Union Shipbuilding Co. Ltd. is in negotiation with the independent third parties to finalise the terms of the shipbuilding contracts and has not commenced the shipbuilding process.

30. BORROWINGS (Continued)

At 31 December 2012, there was no principal amount of the Group's bank borrowings with repayment on demand clause.

Included in the borrowings are the following amounts denominated in currencies other than the functional currencies of the Group:

	2012	2011
	'000	'000
USD	**7,065**	12,956
EUR	**3,288**	–

31. PROVISION FOR WARRANTY

	HK$'000
At 1 January 2011	34,097
Exchange adjustments	1,551
Additional provision for the year	25,366
Reversal of provision	(35,648)
At 31 December 2011	25,366
Exchange adjustments	413
Additional provision for the year	35,530
Reversal of provision	(25,779)
At 31 December 2012	**35,530**

The Group provides a one-year warranty on shipbuilding and undertakes to repair or replace items that fail to perform satisfactorily. The provision is estimated based on historical data of the level of repairs and replacement.

32. DEFERRED CONSIDERATION

	2012	2011
	HK$'000	HK$'000
At 1 January	**217,268**	187,543
Imputed interest expense (Note 11)	**2,643**	29,725
Settlement	**(219,911)**	–
At 31 December	**–**	217,268

The amount was interest free and originally repayable on 31 December 2009. The amount represented HK$200,000,000 deferred consideration payable for the acquisition of INPAX Group (as defined in Note 34) during the year ended 31 December 2008. The imputed interest rate was 16.25% (2011: 16.25%) per annum.

On 30 November 2009, the Company entered into an agreement with the creditor, Million King Investments Limited ("Million King"), an independent third party, to defer its payment to 31 January 2010.

On 7 January 2010, Million King further agreed to defer the repayment date to 31 January 2011 and an interest would be charged at Hong Kong prime rate thereafter. On 23 April 2010, Million King further agreed to defer the repayment date from 31 January 2011 to 31 January 2012 (the "Deferred Consideration Extensions").

The Deferred Consideration Extensions constitute substantial modifications of the terms of the existing liability and hence is accounted for as an extinguishment of the existing liability having a previous carrying amount of HK$200,000,000 and replaced by the incurrence of a new liability having a fair value of approximately HK$163,986,000 at 23 April 2010.

The fair value of the new deferred consideration was calculated based on the present value of the contractually determined stream of future cash flows discounted at 15.85% per annum.

32. DEFERRED CONSIDERATION (Continued)

On 30 January 2012, the Company entered into a settlement deed (the "Settlement Deed") with Million King. Pursuant to the Settlement Deed, the Company's payment obligation of the deferred consideration HK$200,000,000 and the relevant interests shall be fully settled and discharged by cash, offset against other receivables, issuance of the convertible notes with principal amount of HK$105 million ("CBIV") and the promissory notes with principal amount of HK$95 million ("PN") from the Company to Million King and/or its nominees. Completion of the Settlement Deed shall take place upon fulfillment of some conditions precedent. The Directors considered that all conditions precedent have been fulfilled on 28 February 2012.

On 28 February 2012, the excess of the carrying amount of the deferred consideration, over (i) the fair value of CBIV and PN, and (ii) outstanding interest payment, which was amounted to approximately HK$52,936,000, was credited to the consolidated statement of comprehensive income during the year ended 31 December 2012.

Details of the gain on settlement of the deferred consideration on 28 February 2012 are as follows:

	2012 HK$'000
Accumulated deferred consideration	
At 1 January	217,268
Imputed interest expense	2,643
	219,911
Settled by	
Cash	(10,000)
Offset against other receivables	(2,192)
Fair value of HK$105 million CBIV (Note 34)	(90,910)
Fair value of HK$95 million PN (Note 35)	(63,873)
	(166,975)
Gain on settlement of deferred consideration	52,936

33. SHARE CAPITAL

	Number of shares		Amount	
	2012	2011	**2012**	2011
			HK$'000	HK$'000
Ordinary shares of HK$0.05 each				
Authorised:				
At 1 January	**20,000,000,000**	5,000,000,000	**1,000,000**	250,000
Increase in authorised share capital (Note a)	**–**	15,000,000,000	**–**	750,000
At 31 December	**20,000,000,000**	20,000,000,000	**1,000,000**	1,000,000
Issued and fully paid:				
At 1 January	**3,667,994,886**	2,255,249,126	**183,400**	112,762
Issue of shares upon conversion of convertible notes (Note b)	**–**	1,412,745,760	**–**	70,638
At 31 December	**3,667,994,886**	3,667,994,886	**183,400**	183,400

Notes:

(a) Pursuant to an ordinary resolution at the annual general meeting held on 23 June 2011, the authorised share capital of the Company was increased from HK$250,000,000 divided into 5,000,000,000 ordinary shares to HK$1,000,000,000 divided into 20,000,000,000 ordinary shares by the creation of additional 15,000,000,000 shares. The new shares rank pari passu in all respects with the existing issued shares of the Company.

(b) On 7 February 2011, certain convertible notes holders surrendered of approximately HK$282.55 million of convertible notes for the subscription of 1,412,745,760 new shares.

All the shares issued during the year ended 31 December 2011 ranked pari passu with the then existing shares in all respects.

34. CONVERTIBLE NOTES PAYABLE

a) Issuance of convertible notes for INPAX Group Acquisition

On 5 November 2007, the Company entered into a conditional agreement to issue convertible notes for the acquisition of the entire interest in INPAX Technology Limited and its wholly owned subsidiary, Jiangxi Jiangzhou Union Shipbuilding Co., Ltd. (collectively known as the "INPAX Group"). Upon completion, a convertible notes ("CBI") were issued on 16 April 2008 as part of the consideration for the acquisition.

CBI comprised restricted convertible notes and unrestricted convertible notes.

The aggregate principal amount of the unrestricted convertible notes issued is HK$2,400 million.

The initial aggregate principal amount of the restricted convertible notes issued is HK$600 million, which is subject to a downward adjustment for the potential shortfall between the guaranteed profit of HK$600 million and the audited profit after taxation of INPAX Group for the year ended 31 December 2008. Based on the audited profit after taxation for the year ended 31 December 2008 of INPAX Group of HK$217 million, the shortfall is determined to be approximately HK$383 million as compared to the guaranteed profit of HK$600 million.

The difference between i) the aggregate principal amount of the CBI of HK$2,617 million, representing the aggregate amount of the principal amount of the unrestricted convertible notes of HK$2,400 million and the adjusted principal amount of the restricted convertible notes issued of HK$217 million; and ii) the fair value of the liability component of the CBI of approximately HK$1.7 billion, representing the conversion option of approximately HK$0.9 billion was credited directly to equity as convertible notes reserve during the year ended 31 December 2008.

The holder(s) of the restricted convertible notes may convert the whole or any part of the principal amount of the restricted convertible notes outstanding into ordinary shares of the Company from 1 April 2009 to 15 April 2011, the date of maturity, at the initial conversion price of HK$0.15 per share, which was adjusted to HK$4.30 following (i) the share placements and the share consolidation in 2009; and (ii) the open offer and the related bonus element in 2010.

34. CONVERTIBLE NOTES PAYABLE (Continued)

a) Issuance of convertible notes for INPAX Group Acquisition (Continued)

The holder(s) of the unrestricted convertible notes may convert the whole or any part of the principal amount of the unrestricted convertible notes outstanding into ordinary shares of the Company from 16 April 2008, the date of issue of the convertible notes, to 15 April 2011, the date of maturity, at an initial conversion price of HK$0.15 per conversion share, which is subject to anti-dilutive adjustments and was adjusted to HK$4.30 following (i) the share placements and the share consolidation in 2009; and (iii) the open offer and the related bonus element in 2010.

In respect of the restricted convertible notes, no interest will be payable. For the unrestricted convertible notes, coupon interest at the rate of 1.5% per annum will be accrued on a day-to-day basis on the outstanding principal amount, payable semi-annually in arrears.

The CBI is not redeemable at the option of the noteholder(s) prior to maturity. The Company shall have the right to redeem any portion of the CBI outstanding at an amount equals to the principal amount of the CBI together with any interest accrued at its sole and absolute discretion at any time prior to the maturity date of the CBI. In the opinion of the Directors, such redemption option has risks and characteristics that are closely related to CBI as the redemption option's exercise price is approximately equal on each exercise date to the amortised cost of the host instrument before separating the equity component. Unless previously converted or redeemed, the Company shall redeem the CBI at par on the maturity date of the CBI.

The CBI is freely transferrable, provided that the noteholder(s) of the CBI must inform and obtain written consent from the Company of each transfer or assignment made by them.

34. CONVERTIBLE NOTES PAYABLE (Continued)

a) Issuance of convertible notes for INPAX Group Acquisition (Continued)

On 27 April 2010, the Group announced to have entered into an extension agreement with the CBI holders whereby the parties agreed to extend the maturity date of the outstanding convertible notes from 15 April 2011 to 15 April 2012. Except for the extension of the maturity date of the outstanding CBI, each and every term and condition under CBI shall remain unchanged. The extension became effective upon the approval by the shareholders of the Company at a special general meeting held on 25 June 2010 and obtaining of consents and approvals by the Stock Exchange on 29 June 2010. The maturity date of the convertible notes has therefore been extended to 15 April 2012 (the "CN Extension").

The effect of CN Extension represents the extinguishment of CBI having a carrying amount of HK$440,323,001 by the issue of new convertible notes having the exact terms and conditions other than an extended maturity date of CBI (the "CBII"), which has a fair value of HK$399,334,556 comprising a liability portion of approximately HK$399 million and an insignificant conversion option derivative at the date when the CN Extension became effective. The difference of approximately HK$41 million between CBI and CBII on the date of the CN Extension was credited to the consolidated statement of comprehensive income during the year ended 31 December 2010.

On 21 December 2010, the Group entered into subscription agreements with certain holders of CBII to surrender the CBII notes held by them of principal amount of approximately HK$282,549,000 in consideration for the subscription of 1,412,745,760 shares of the Company having a par value of HK$0.05 each at a subscription price of HK$0.2 per subscription share. For the remaining portion of CBII notes with principal amount of HK$225,000,000, the Group entered into agreements with the holders that, i) the conversion price is reduced from HK$4.30 per share to HK$0.22 per share; ii) the maturity date is extended from April 2012 to April 2014; and iii) other terms and conditions remain unchanged (the "CN Modification"). The transactions became unconditional upon consents and approvals obtained from the Stock Exchange on 31 January 2011 and shareholders at a special general meeting held on 28 January 2011.

34. CONVERTIBLE NOTES PAYABLE (Continued)

a) Issuance of convertible notes for INPAX Group Acquisition (Continued)

The fair value of the Company's shares issued to settle CBII with principal amount of approximately HK$282,549,000 through the share subscription was approximately HK$247,231,000 based on the closing price of the Company's shares on 31 January 2011 of HK$0.175 each. The excess of approximately HK$7,241,000, representing the difference between the fair value of the Company's shares and the carrying amount of the relevant portion of the CBII of HK$239,990,000, have been recognised by the Group as a loss on extinguishment of part of CBII in the consolidated statement of comprehensive income during the year ended 31 December 2011.

The valuation of the remaining CBII including the conversion option derivative and liability portion was performed by, Greater China Appraisal Limited ("Greater China"), an independent professional valuer not connected to the Group. The inputs used in the model in determining the fair value were as follows:

	Convertible notes modified on 31 January 2011
Share price	HK$0.175
Exercise price	HK$0.22
Contractual life	3.21 years
Risk-free rate	1.040%
Expected dividend yield	0%
Volatility	53.26%

34. CONVERTIBLE NOTES PAYABLE (Continued)

a) Issuance of convertible notes for INPAX Group Acquisition (Continued)

The effect of CN Modification represents the extinguishment of CBII having a carrying amount of HK$193,266,282 with revised terms and conditions as mentioned above (the "CBIII"), which has a fair value of HK$189,004,303 comprising a liability portion of approximately HK$138 million and a conversion option derivative at the date when the CN Modification became effective. The difference of approximately HK$4,262,000 between CBII and CBIII on the date of the CN Modification was credited to the consolidated statement of comprehensive income during the year ended 31 December 2011.

At 31 December 2011, CBIII having a carrying amount of approximately HK$208,524,000 which has a fair value of approximately HK$157,135,000 comprising a liability portion of approximately HK$154 million and an insignificant conversion option. The difference of approximately HK$51,389,000 was credited to the consolidated statement of comprehensive income during the year ended 31 December 2011.

The fair value of the conversion option component of CBIII was calculated using the Binominal option pricing model while the fair value of the liability component of CBIII was calculated based on the present value of the contractually determined stream of future cash flows discounted at 20.36%, being the effective interest rate of CBIII.

34. CONVERTIBLE NOTES PAYABLE (Continued)

a) Issuance of convertible notes for INPAX Group Acquisition (Continued)

The valuation of the entire CBIII including the conversion option derivative and liability portion was performed by Greater China. The inputs used in the model in determining the fair value were as follows:

	CBIII at 31 December 2011
Share price	HK$0.102
Exercise price	HK$0.22
Contractual life	2.29 years
Risk-free rate	0.393%
Expected dividend yield	0%
Volatility	38.77%

b) Issuance of convertible notes for extinguishment of deferred consideration

On 28 February 2012, part of the deferred consideration was settled by issuing CBIV and PN to Million King and/or its nominees.

The aggregated principal amount of the CBIV is HK$105 million, coupon interest at a rate of 3% per annum and will be accrued on a day-to-day basis on the outstanding principal amount of the CBIV, payable semi-annually in arrears. The holders of the CBIV may convert the whole or any part of the outstanding principal amount of the CBIV into ordinary shares of the Company from 28 February 2012 to 28 February 2015, the date of maturity, at the initial conversion price of HK$0.15 per share.

34. CONVERTIBLE NOTES PAYABLE (Continued)

b) Issuance of convertible notes for extinguishment of deferred consideration (Continued)

The valuation of the CBIII and CBIV including the conversion option derivative and liability portion was performed by Greater China. The inputs used in the model in determining the fair value were as follows:

	CBIV at 28 February 2012
Share price	HK$0.118
Exercise price	HK$0.150
Contractual life	3.00 years
Risk-free rate	0.334%
Expected dividend yield	0%
Volatility	42.24%

At 31 December 2012, CBIII and CBIV having a carrying amount of approximately HK$257,683,000 which has a fair value of HK$281,938,000 comprising a liability portion of approximately HK$278,632,000 and an equity portion of approximately HK$3,306,000. The difference of a liability portion approximately HK$20,949,000 was debt to the consolidated statement of comprehensive income during the year ended 31 December 2012.

The fair value of the conversion option component of CBIII and CBIV were calculated using the Binominal option pricing model while the fair value of the liability component of CBIII and CBIV were calculated based on the present value of the contractually determined stream of future cash flows discounted at 14.040% and 13.959%, being the effective interest rate of CBIII and CBIV respectively.

34. CONVERTIBLE NOTES PAYABLE (Continued)

As at 31 December 2012, the valuation of the CBIII and CBIV including the conversion option derivative and liability portion was performed by Greater China. The inputs used in the model in determining the fair value were as follows:

	CBIII at 31 December 2012	CBIV at 31 December 2012
Share price	**HK$0.066**	HK$0.066
Exercise price	**HK$0.22**	HK$0.150
Contractual life	**1.29 years**	2.16 years
Risk-free rate	**0.106%**	0.112%
Expected dividend yield	**0%**	0%
Volatility	**41.35%**	40.48%

The movements of the liability and equity component of CBII, CBIII and CBIV were as follows:

	Liability component HK$'000	**Equity component** HK$'000	**Total** HK$'000
At 1 January 2011	427,293	–	427,293
Gain on modification of CBII	(4,262)	–	(4,262)
Gain on fair value change of CBIII	(51,389)	–	(51,389)
Loss on extinguishment of part of CBII	7,241	–	7,241
Conversion of share	(247,231)	–	(247,231)
Interest charged (Note 11)	29,490	–	29,490
Interest paid	(4,007)	–	(4,007)
At 31 December 2011	157,135	–	157,135

34. CONVERTIBLE NOTES PAYABLE (Continued)

The movements of the liability and equity component of CBII, CBIII and CBIV were as follows: (Continued)

	Liability component HK$'000	Equity component HK$'000	Total HK$'000
At 1 January 2012	157,135	–	157,135
Issuance of CBIV (Note 32)	63,938	26,972	90,910
Loss on fair value change of CBIII and CBIV	20,949	–	20,949
Interest charged (Note 11)	41,547	–	41,547
Interest paid	(4,937)	–	(4,937)
At 31 December 2012	**278,632**	**26,972**	**305,604**

35. PROMISSORY NOTES PAYABLE

On 28 February 2012, part of the deferred consideration was settled by issuing CBIV and PN to Million King and/or its nominees.

The aggregated principal amount of the PN is HK$95 million, bears interest at the rate of 3% per annum and will be accrued on a day-to-day basis on the outstanding principal amount of the PN, payable semi-annually in arrears, up to the maturity date on 31 December 2014. The PN is transferable only if the relevant principal amount and corresponding interest would be transferred together.

The movements of the liability component of PN were as follows:

	2012 HK$'000
Issuance of PN (Note 32)	63,873
Offset against other receivables	(3,817)
Interest charged (Note 11)	10,071
Interest paid	(1,414)
Liability component of PN at 31 December	**68,713**

On 31 December 2012, the Company entered into a settlement agreement with Million King and one PN holder. Pursuant to the settlement agreement, other receivables of HK$3,000,000 from Million King shall be fully settled and discharged by HK$5,000,000 principal amount of the PN of the PN holder.

36. DEFERRED TAX LIABILITIES

The following are the major deferred tax liabilities recognised and movements thereon during the current and prior years:

	Withholding tax on undistributed earnings of the PRC subsidiaries	Fair value adjustments on properties and intangible assets	Total
	HK$'000	HK$'000	HK$'000
At 1 January 2011	30,762	179,954	210,716
Exchange adjustments	–	8,818	8,818
Credit to profit and loss (Note 13)	–	(105,186)	(105,186)
At 31 December 2011	30,762	83,586	114,348
Exchange adjustments	–	3,294	3,294
Credit to profit and loss (Note 13)	–	(23,993)	(23,993)
At 31 December 2012	**30,762**	**62,887**	**93,649**

At the end of the reporting period, the Group had unused tax losses of approximately HK$22,493,000 (2011: HK$11,621,000) available to offset against future profits. No deferred tax asset has been recognised due to unpredictability of future profits streams. Tax losses may be carried forward indefinitely.

37. CAPITAL COMMITMENTS

	2012	2011
	HK$'000	HK$'000
Capital expenditure in respect of acquisition of property, plant and equipment contracted for but not provided in the consolidated financial statements	**3,819**	7,947

38. PLEDGE OF ASSETS

At the end of the reporting period, the following assets were pledged for the Group's banking facilities, bills payables and borrowings:

	2012	2011
	HK$'000	HK$'000
Deposits	**302,447**	393,313
Inventories	**50,911**	156,618
Properties, plant and equipment	**563,956**	399,627
Prepaid lease payments	**335,136**	341,034
Value-added tax recoverable	**148,225**	258,935
	1,400,675	1,549,527

39. SHARE OPTION SCHEME

The Company has adopted a share option scheme on 27 May 2002 (the "Scheme 2002"). Pursuant to an ordinary resolution passed at the annual general meeting of the Company held on 27 June 2012, the Scheme 2002 was expired and those options under the Scheme 2002 shall remain exercisable pursuant to the rules of the Scheme 2002, and a new share option scheme (the "Scheme 2012") was adopted.

The purpose of the Scheme 2002 and Scheme 2012 is to enable the Company to grant options to eligible employees, including Directors and its subsidiaries, to subscribe for shares of the Company as incentives and to provide them with a direct economic interest in attaining the long-term business objective of the Company.

At 31 December 2012, the number of outstanding share options under the Scheme 2012 was 46,449,780 (2011: the Scheme 2002 was 46,449,780), representing 1.27% (2011: 1.27%) of the shares of the Company in issue at that date. The total number of shares in respect of which options may be granted under the Scheme 2002 and Scheme 2012 are not permitted to exceed 10% of the shares of the Company in issue at any point in time without prior approval from the Company's shareholders.

39. SHARE OPTION SCHEME (Continued)

The number of shares issued and to be issued in respect of which options granted and may be granted to any individual in any one year is not permitted to exceed 1% of the shares of the Company in issue at any point in time without prior approval from the Company's shareholders. Options granted must be taken up within 21 days of the date of grant, upon payment of HK$1 per person. Options may be exercised at any time during the exercise period. The subscription price of the option shall be determined by the board but in any case shall not be less than the higher of (i) the closing price of the shares as stated in the daily quotations sheet of the Stock Exchange on the date of grant which must be a trading day; (ii) the average closing price of the shares as stated in the daily quotations sheet of the Stock Exchange for the five trading days immediately preceding the date of grant; or (iii) the nominal value of a share.

No share option has been granted under the Scheme 2002 or Scheme 2012 by the Company during the year ended 31 December 2012 and 2011.

The following table discloses details of the options held by directors, employees and consultants and movements in such holdings during the years ended 31 December 2012 and 2011:

Name	Date of grant	Exercisable period	Exercise price per share (Note a)	Number of share options Outstanding at 1.1.2012 and 31.12.2012
Directors	5 March 2008	5 March 2008 to 4 March 2018	HK$5.693	2,529,600
		5 March 2009 to 4 March 2018	HK$5.693	1,897,200
		5 March 2010 to 4 March 2018	HK$5.693	1,897,200
				6,324,000

39. SHARE OPTION SCHEME (Continued)

Name	Date of grant	Exercisable period	Exercise price per share (Note a)	Number of share options Outstanding at 1.1.2012 and 31.12.2012
	7 May 2008	7 May 2008 to 6 May 2018	HK$4.523	1,644,240
		7 May 2009 to 6 May 2018	HK$4.523	1,233,180
		7 May 2010 to 6 May 2018	HK$4.523	1,233,180
				4,110,600
				10,434,600
Employees	7 May 2008	7 May 2008 to 6 May 2018	HK$4.523	935,952
		7 May 2009 to 6 May 2018	HK$4.523	701,964
		7 May 2010 to 6 May 2018	HK$4.523	701,964
				2,339,880
Consultants (Note b)	7 May 2008	7 May 2008 to 6 May 2018	HK$4.523	33,675,300
				46,449,780

Notes:

a. The initial exercise prices of the shares options granted on 5 March 2008 and 7 May 2008 are HK$0.18 and HK$0.143 respectively. Upon the share consolidation became effective on 25 June 2009 and the open offer and the related bonus element became effective on 7 September 2010, the exercise prices of shares options were adjusted to HK$5.693 and HK$4.523 accordingly.

b. The consultants provided consultancy service with regard to the acquisition and operation of INPAX Group.

The remaining contractual life of these outstanding share options is approximately 5.4 years.

39. SHARE OPTION SCHEME (Continued)

No share options were exercised during the years ended 31 December 2012 and 2011. The estimated fair values of the options granted on 5 March 2008 and 7 May 2008 are approximately HK$18,086,000 and HK$30,502,000 respectively.

These fair values were calculated using the Binominal option pricing model. The inputs into the model were as follows:

	5 March 2008	7 May 2008
Grant date share price	HK$0.180	HK$0.138
Exercise price	HK$0.180	HK$0.143
Contractual life	10 years	10 years
Expected volatility	43.73%	44.73%
Dividend yield	0%	0%
Risk-free interest rate	2.766%	2.802%

Expected volatility was determined by using the historical volatility of the Company's share price over the previous 5 years. The expected life used in the model has been adjusted, based on management's best estimate, for the effects of non-transferability, exercise restrictions and behavioural considerations.

40. RETIREMENT BENEFITS SCHEME

The Group operates a Mandatory Provident Fund Scheme (the "MPF Scheme") for all its qualifying employees in Hong Kong. The assets of the MPF Scheme are held separately from those of the Group and in funds under the control of trustees. The Group contributes 5% or HK$1,250 (31 December 2011: HK$1,000) in maximum of relevant payroll costs to the MPF Scheme, which is matched by employees.

40. RETIREMENT BENEFITS SCHEME (Continued)

The Company's subsidiary in the PRC is a member of the state-managed retirement benefits scheme operated by the government of PRC. The retirement scheme contributions, which are based on a certain percentage of the basic salaries of the relevant subsidiary's employees, are charged to the consolidated statement of comprehensive income in the period to which they relate and represent the amount of contributions payable by the subsidiary to the scheme. The only obligation of the Group with respect to the retirement benefits scheme operated by the government of PRC is to make the required contributions under the scheme.

The retirement benefit cost charged to the consolidated statement of comprehensive income represents contributions payable to the scheme by the Group at rate specified in the rules of the scheme.

41. CONTINGENT LIABILITIES

(a) At 31 December 2012, the Group has an arbitration proceeding in progress with one vessel owner in respect of three vessels over the validity of the rescission notices.

If the result of the arbitration is unfavourable to the Group, the Group will be required to return the principal payments for the shipbuilding contracts of the vessels in arbitration and to pay interests for the principal payments calculated in accordance with the relevant shipbuilding contracts up to the settlement date. At 31 December 2012, the principal payments and the interests accrued up to 31 December 2012 of approximately HK$372,338,000 (2011: HK$366,381,000) in aggregate, were recorded as "Trade, bills and other payables" in the consolidated statement of financial position.

41. CONTINGENT LIABILITIES (Continued)

(b) At 31 December 2012, the Group has not paid the social security for and on behalf of its employees and expose the Group to the risk of being imposed the penalty by the relevant government authority. At 31 December 2012, the social security accrued up to 31 December 2012 of approximately HK$18,125,000 (equivalent to approximately RMB14,500,000) in aggregate, were recorded as "Trade, bills and other payables" in the consolidated statement of financial position. (2011: approximately HK$4,420,000 (equivalent to approximately RMB3,590,000)).

A repayment agreement was signed between Jiangxi Jiangzhou Union Shipbuilding Co., Ltd. and the relevant government authority on 12 March 2013 in respect of the accrued social security, all amounts should repaid before June 2014. The Directors considered that if the Group could settle the accrued social security before June 2014, no penalty would be imposed by the relevant government authority.

(c) At 31 December 2012, the Group has not paid the housing provident fund contributions for and on behalf of its employees and expose the Group to the risk of being imposed the penalty by the relevant government authority. The housing provident fund contributions accrued up to 31 December 2012 of approximately HK$3,063,000 (equivalent to approximately RMB2,450,000) in aggregate, were recorded as "Trade, bills and other payables" in the consolidated statement of financial position. (2011: approximately HK$1,260,000 (equivalent to approximately RMB1,020,000)).

The delay in the settlement of housing provident fund contributions may expose the Group to the risk of being imposed the penalty by the relevant government authority.

Other than disclosed above, the Directors are of the opinion that the Group has no other material contingent liabilities at 31 December 2012.

42. OPERATING LEASE COMMITMENTS

At the end of the reporting period, the Group had commitments for future minimum lease payments payable under non-cancellable operating leases in respect of rented premises which fall due as follows:

	2012 HK$'000	2011 HK$'000
Within one year	1,694	894
In the second to fifth year inclusive	692	200
	2,386	1,094

Operating lease payments represent rental payables by the Group for certain of its office premises. Leases are negotiated and rentals are fixed for an average term of 2 years (2011: 2 years).

43. RELATED PARTY TRANSACTIONS

In addition to related party balances detailed in the consolidated financial statement, the Group had the following significant transactions with related parties during the years as follows:

(a) During the year ended 31 December 2011, the Group paid fees of approximately HK$15,990,000 (equivalent to RMB13,000,000) to China Ruilian in respect of shipbuilding services including guarantee issued by China Ruilian for the Group's entering of certain shipbuilding contracts. The Company's executive director, Mr. Li, has beneficial interests in both the Company and China Ruilian and has significant influence on China Ruilian.

As Mr. Li sold his interests in China Ruilian to a third party in July 2012, China Ruilian ceased to be a related party of the Group thereafter.

At 31 December 2012, the amount due to China Ruilian of approximately HK$851,000 (equivalent to RMB681,000) included in other payables. (2011: HK$31,588,000 (equivalent to RMB25,681,000) included in amount due to a related party). The amount is unsecured, interest free and repayable on demand.

43. RELATED PARTY TRANSACTIONS (Continued)

(b) During the year ended 31 December 2012, the Group borrowed of approximately HK$39,848,000 (equivalent to RMB31,878,000) (2011: HK$Nil) from Guangchang Zongbang Credit Loan Co., Ltd. ("Zongbang Credit"). The proceeds were used to finance the daily operation of the Group. The Company's executive director, Mr. Li has beneficial interests in Zongbang Credit. The loans are unsecured, interest-bearing at a range from 1.5% to 1.85% per month and repayable in April to May 2013.

(c) During the year ended 31 December 2012, Zha Jiu Peng and Wu Ge are the senior management of the Group, have advanced loan of HK$312,000 and HK$2,500,000 (equivalent to RMB250,000 and RMB2,000,000) respectively to the Group. The loan is unsecured, interest-bearing at 15% per annum and repayable in August 2013.

(d) During the year ended 31 December 2012, the Group borrowed of approximately HK$4,375,000 (equivalent to RMB3,500,000) from Jiujiang Jiangzhou Heavy Industry Co., Ltd. ("Jiujiang Heavy"). The equity interest of Jiujiang Heavy is owned as to 10% by Jiangxi Jiangzhou Union Shipbuilding Co., Ltd, the wholly-owned subsidiary of the Company. The proceeds were used to finance the daily operation of the Group. The Company's executive director, Mr. Wang San Long ("Mr. Wang") is the representative of Jiujiang Heavy. The loan is unsecured, interest free and repayable on demand.

(e) During the year ended 31 December 2012, the Group borrowed of approximately HK$6,250,000 (equivalent to RMB5,000,000) from Shanghai Xianglong Investment Management Co., LTD ("Shanghai Xianglong"). The equity interest of Shanghai Xianglong is owned as to 20% by Jiujiang Heavy. The proceeds were used to finance the daily operation of the Group. The loan is unsecured, interest free and repayable on demand.

(f) Mr. Wang, the executive director of the Company, has provided a free counter-guarantee in favor of the Group to guarantee a facility of RMB236,100,000 (2011: RMB120,000,000) granted by banks in the PRC for the year ended 31 December 2012. During the year ended 31 December 2012, Mr. Wang has advanced loan of HK$812,000 (equivalent to RMB650,000) (2011: HK$615,000 (equivalent to RMB500,000)) to the Group. The loan is unsecured, interest-bearing at 15% per annum and repayable in August 2013.

(g) The remuneration of Directors and chief executives during the years ended 31 December 2012 and 2011 has been disclosed in Note 14. The remuneration of Directors and chief executives is recommended by the remuneration committee having regarded to the performance of individual and market trends.

The Directors are of the view that terms of the above related party transactions are fair and reasonable, based on normal commercial terms where no charge over the assets of the Group is created in respect of the above transactions. Accordingly, the transactions are exempted from all reporting, announcement and independent shareholders' approval requirement under the Listing Rules.

44. STATEMENT OF FINANCIAL POSITION OF THE COMPANY

	Notes	2012 HK$'000	2011 HK$'000
NON-CURRENT ASSETS			
Property, plant and equipment		**38**	60
Investments in subsidiaries	(a)	**1**	1
		39	61
CURRENT ASSETS			
Other receivables		**20**	2,335
Amounts due from subsidiaries	(a)	**7,182**	59,921
Investments held for trading		**2,430**	2,750
Bank balances and cash		**3,538**	600
		13,170	65,606
CURRENT LIABILITIES			
Other payables		**9,920**	3,767
Deferred consideration		**–**	217,268
		9,920	221,035
NET CURRENT ASSETS (LIABILITIES)		**3,250**	(155,429)
NON-CURRENT LIABILITIES			
Convertible notes payable		**278,632**	157,135
Promissory notes payable		**68,713**	–
		347,345	157,135
NET LIABILITIES		**(344,056)**	(312,503)
CAPITAL AND RESERVES			
Share capital		**183,400**	183,400
Reserves	(b)	**(527,456)**	(495,903)
		(344,056)	(312,503)

44. STATEMENT OF FINANCIAL POSITION OF THE COMPANY (Continued)

Notes:

(a) (i) Investments in subsidiaries

	2012 HK$'000	2011 HK$'000
Unlisted investment, at cost	**3,067,687**	3,067,687
Less: Accumulated provision for impairment	**(3,067,686)**	(3,067,686)
	1	1

(ii) Amounts due from subsidiaries

	2012 HK$'000	2011 HK$'000
Amounts due from subsidiaries	**177,538**	207,995
Less: Accumulated provision for impairment	**(170,356)**	(148,074)
	7,182	59,921

Amounts due from subsidiaries are unsecured, interest free and repayable on demand.

(b) Reserves

	Share premium HK$'000	Contributed surplus HK$'000	Convertible notes reserve HK$'000 (Note 34)	Share option reserve HK$'000	Accumulated losses HK$'000	Total HK$'000
At 1 January 2011	152,321	3,368,411	–	43,693	(3,785,542)	(221,117)
Loss for the year, representing total comprehensive expenses for the year	–	–	–	–	(451,379)	(451,379)
Issue of shares upon conversion of convertible notes	176,593	–	–	–	–	176,593
At 31 December 2011	328,914	3,368,411	–	43,693	(4,236,921)	(495,903)
Loss for the year, representing total comprehensive expenses for the year	–	–	–	–	(58,525)	(58,525)
Recognition of equity component of convertible notes payable	–	–	26,972	–	–	26,972
At 31 December 2012	**328,914**	**3,368,411**	**26,972**	**43,693**	**(4,295,446)**	**(527,456)**

45. PARTICULARS OF SUBSIDIARIES

Particulars of the Company's subsidiaries at 31 December 2012 are as follows:

Name of subsidiaries	Place of incorporation/ operation	Issued share capital	Proportion of nominal value of issued share capital held by the Company 2012		Principal activities
			Directly %	Indirectly %	
INPAX Technology Limited	British Virgin Islands*	10,000 ordinary shares of USD1 each	100	–	Investment holding
Merge Limited	Hong Kong	1 ordinary share of HK$1 each	100	–	Trading
China Ocean Shipbuilding Holdings Limited	British Virgin Islands*	1 ordinary share of USD1 each	100	–	Investment holding
Smart Victor Holdings Limited	British Virgin Islands*	1 ordinary share of USD1 each	100	–	Investment holding
China Ocean Shipbuilding Services Limited	Hong Kong	1 ordinary share of HK$1 each	–	100	Inactive
China Ocean Shipbuilding (Hong Kong) Limited	Hong Kong	1 ordinary share of HK$1 each	–	100	Sale agent for shipbuilding
Golden Device Limited	Hong Kong	1 ordinary share of HK$1 each	–	100	Inactive
Jiangxi Jiangzhou Union Shipbuilding Co., Ltd **	PRC	USD59,000,000 paid-up registered capital	–	100	Manufacturing metal vessel, vessel ancillary products and reparation of vessels

* The companies are engaged in investment business and have no specific principal place of operation.

** The company is registered in the form of a wholly foreign owned enterprise.

None of the subsidiaries had any debt securities at 31 December 2012 and 2011 or at any time during both years.

46. EVENTS AFTER THE REPORTING PERIOD

The Group had no material subsequent event after the reporting period.

47. DIVIDEND

No dividends were paid or proposed for the year ended 31 December 2012, nor has any dividend been proposed since the end of the reporting period (2011:Nil).

48. COMPARATIVE FIGURES

In order to conform with the current year presentation, certain items in the consolidated statement of comprehensive income for the year ended 31 December 2011 has been reclassified.

Details of the restatement are provided as follows:

	Amount original stated	Reclassification	Amount as restated
	HK$'000	HK$'000	HK$'000
Items on consolidated statement of comprehensive income for the year ended 31 December 2011			
Administrative expenses	(87,460)	4,041	(83,419)
Finance costs	(170,329)	(4,041)	(174,370)

Financial Summary

	Year ended 31 December				
	2012	2011	2010	2009	2008
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
RESULTS					
LOSS FOR THE YEAR	**(344,101)**	(542,559)	(867,385)	(1,956,362)	(468,996)

	At 31 December				
	2012	2011	2010	2009	2008
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
ASSETS AND LIABILITIES					
TOTAL ASSETS	**2,188,314**	3,169,282	3,530,272	4,514,681	5,588,298
TOTAL LIABILITIES	**(2,911,388)**	(3,570,677)	(3,638,627)	(4,007,865)	(3,294,889)
NET (LIABILITIES) ASSETS	**(723,074)**	(401,395)	(108,355)	506,816	2,293,409