1. GENERAL

The Company was incorporated as an exempted company with limited liability in the Cayman Islands under the Companies Law of the Cayman Islands and its shares are listed on The Stock Exchange of Hong Kong Limited (the "Stock Exchange"). Its ultimate holding company is Joyce Services Limited ("Joyce"), a company which is incorporated in the British Virgin Islands.

The companies in the Group underwent a group reorganisation in preparation for the listing of the Company's shares on the Stock Exchange in January 2000. Details of the group reorganisation are set out in the prospectus issued by the Company dated 18th January, 2000. The financial statements of the Group for the year ended 31st December, 2000 were prepared on the merger basis as if the Company had always been the holding company of the Group. In the opinion of the directors, the comparative financial statements, prepared on this basis, present fairly the results and cash flows of the Group as a whole.

The Company is an investment holding company. The principal activities of its subsidiaries are set out in note 31.

2. ADOPTION OF STATEMENTS OF STANDARD ACCOUNTING PRACTICE/CHANGES IN ACCOUNTING POLICIES

In the current year, the Group has adopted for the first time a number of new and revised Statements of Standard Accounting Practice ("SSAP(s)") issued by the Hong Kong Society of Accountants. Adoption of these SSAPs has led to a number of changes in the Group's accounting policies. The revised accounting policies are set out in note 3. In addition, the new and revised SSAPs have introduced additional and revised disclosure requirements which have been adopted in these financial statements. Comparative amounts for the prior year have been restated in order to achieve a consistent presentation.

The adoption of these new and revised SSAPs has resulted in the following changes to the Group's accounting policies that have affected the amounts reported for the current or prior years.

Dividends proposed or declared after the balance sheet date

In accordance with SSAP 9 (Revised) "Events after the Balance Sheet Date", dividends proposed or declared after the balance sheet date are not recognised as a liability at the balance sheet date, but are disclosed in the notes to the financial statements. This change in accounting policy has been applied retrospectively, resulting in a prior period adjustment which increased the retained profits as at 1st January, 2001 by HK$6,864,000.

2. ADOPTION OF STATEMENTS OF STANDARD ACCOUNTING PRACTICE/CHANGES IN ACCOUNTING POLICIES (Cont'd)

Leases

SSAP 14 (Revised) "Leases" has introduced some amendments to the basis of accounting for finance and operating leases, and to the disclosures specified for the Group's leasing arrangements. These changes have not had any effect on the results for the current or prior accounting periods and, accordingly, no prior period adjustment has been required. Disclosures for the Group's leasing arrangements have been modified so as to comply with the requirements of SSAP 14 (Revised). Comparative amounts have been restated in order to achieve a consistent presentation.

Goodwill

In the current year, the Group has adopted SSAP 30 "Business Combinations" and has elected not to restate goodwill previously eliminated against reserves. Accordingly, goodwill arising on acquisition prior to 1st January, 2001 is held in reserves and will be charged to the income statement at the time of disposal of the relevant subsidiary, or at such time as the goodwill is determined to be impaired.

Goodwill arising on acquisition after 1st January, 2001 is capitalised and amortised over its estimated useful life. Negative goodwill arising on acquisitions after 1st January, 2001 is presented as a deduction from assets and will be released to income based on an analysis of the circumstances from which the balance resulted.

3. SIGNIFICANT ACCOUNTING POLICIES

The financial statements have been prepared under the historical cost convention and in accordance with accounting principles generally accepted in Hong Kong. The principal accounting policies adopted are set out below:

Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and its subsidiaries made up to 31st December each year.

The result of subsidiary acquired or disposed of during the year are included in the consolidated income statement from the effective date of acquisition or up to the effective date of disposal, as appropriate.

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

3. SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

Goodwill

Goodwill arising on consolidation represents the excess of the cost of acquisition over the Group's interest in the fair value of the identifiable assets and liabilities of a subsidiary at the date of acquisition.

Goodwill arising on acquisition of subsidiaries prior to 1st January, 2001 continues to be held in reserves, and will be charged to the income statement at the time of disposal of the relevant subsidiary, or at such time as the goodwill is determined to be impaired.

Goodwill arising on acquisition of subsidiaries after 1st January, 2001 is capitalised and amortised on a straight line basis over its useful economic life. Goodwill arising on the acquisition of subsidiaries is presented separately in the balance sheet.

On disposal of a subsidiary, the attributable amount of unamortised goodwill/goodwill previously eliminated against or credited to reserves is included in the determination of the profit or loss on disposal.

Turnover

Turnover represents the net amounts received and receivable from third parties for goods sold during the year.

Revenue recognition

Sales of goods are recognised when goods are delivered and title has passed while service revenue is recognised when services are provided.

Interest income is accrued on a time basis, by reference to the principal outstanding and at the interest rate applicable.

Dividend income from investments is recognised when the shareholders' right to receive payment has been established.

Investments in subsidiaries

Investments in subsidiaries are included in the Company's balance sheet at cost less any identified impairment loss. The results of subsidiaries are accounted for by the Company on the basis of dividends received and receivable during the year.

3. SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

Property, plant and equipment

Property, plant and equipment, other than construction in progress, is stated at cost less accumulated depreciation and amortisation and accumulated impairment losses.

Construction in progress is stated at cost less any impairment losses which includes all construction costs and other direct costs attributable to such projects. Construction in progress is not depreciated until completion of construction and the asset is being put into use. Costs of completed construction works are transferred to the appropriate categories of property, plant and equipment.

The cost of land use rights or leasehold land is amortised over the period of the rights or leases using the straight line method.

Depreciation is provided to write off the cost of other items of property, plant and equipment over their estimated useful lives, using the straight line method, at the following rates per annum:

Buildings	2% – 5%
Furniture and equipment	20% – 25%
Motor vehicles	20%
Plant and machinery	10%

The gain or loss arising from the disposal or retirement of an asset is determined as the difference between the sale proceeds and the carrying amount of the asset and is recognised in the income statement.

Impairment

At each balance sheet date, the Group reviews the carrying amounts of its tangible and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If the recoverable amount of an asset is estimated to be less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount. Impairment losses are recognised as an expense immediately.

Where an impairment loss subsequently reverses, the carrying amount of the asset 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 in prior years. A reversal of an impairment loss is recognised as income immediately.

3. SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

Investments in securities

Investments in securities are recognised on a trade date basis and are initially measured at cost.

Investments other than held-to-maturity debt securities are classified as investment securities and other investments.

Investment securities, which are securities held for an identified long-term strategic purpose, are measured at subsequent reporting dates at cost, as reduced by any impairment loss that is other than temporary.

Inventories

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

Taxation

The charge for taxation is based on the results for the year as adjusted for items which are non-assessable or disallowed. Timing differences arise from the recognition for tax purposes of certain items of income and expense in a different accounting period from that in which they are recognised in the financial statements. The tax effect of the resulting timing differences, computed under the liability method, is recognised as deferred taxation to the extent that it is probable that a liability or an asset will crystallise in the foreseeable future.

Foreign currencies

Transactions in currencies other than Hong Kong dollars are initially recorded at the rates of exchange ruling on the dates of the transactions. Monetary assets and liabilities denominated in such currencies are retranslated at the rates ruling on the balance sheet date. Profits and losses arising on exchange are dealt with in the income statement for the period.

On consolidation, the assets and liabilities of the Group's overseas operations are translated at exchange rates ruling on the balance sheet date. Income and expense items are translated at the average exchange rates for the period. Exchange differences arising, if any, are classified as equity and are recognised as income or as expenses in the period in which the operation is disposed of.

3. SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

Operating leases

Rentals payable under operating leases are charged to the income statement on a straight line basis over the period of the respective leases.

Retirement benefits scheme contributions

The retirement benefit costs charged to the income statement represent the contributions payable in respect of the current year to the Group's defined contribution retirement benefits scheme and the Hong Kong Mandatory Provident Fund scheme.

4. BUSINESS AND GEOGRAPHICAL SEGMENTS

In accordance with the Group's internal financial reporting, the Group has determined that geographical segments are its primary reporting format.

Business segment

The Group is solely engaged in the manufacture and sale of leather. All of the Group's turnover, contribution to operating profit and assets were attributable to this business segment.

Geographical segments

The Group reports its primary segment information by geographical location of its customers who are principally located in the United States of America ("USA") and the PRC.

4. BUSINESS AND GEOGRAPHICAL SEGMENTS (Cont'd)

Geographical segments (Cont'd)

Segment information about these geographical markets is presented below:

2001

	USA	**PRC**	**Others**	**Consolidated**
	HK$'000	HK$'000	HK$'000	HK$'000
REVENUE				
External sales	505,572	194,780	103,322	803,674
RESULT				
Segment result	35,881	31,147	4,487	71,515
Finance charges				(11,336)
Profit before taxation				60,179
Taxation				(5,334)
Profit before minority interests				54,845

2001

The following is an analysis of the carrying amount of segment assets and segment liabilities, analysed by the geographical location of its customers:

	USA	**PRC**	**Others**	**Consolidated**
	HK$'000	HK$'000	HK$'000	HK$'000
ASSETS				
Segment assets	132,535	46,337	22,779	201,651
Unallocated corporate assets				
Consolidated total assets				768,292
				969,943
LIABILITIES				
Unallocated corporate liabilities				280,293
OTHER INFORMATION				
Capital additions				46,100
Depreciation and amortisation				37,090

4. BUSINESS AND GEOGRAPHICAL SEGMENTS (Cont'd)

Geographical segments (Cont'd)

2000

	USA	**PRC**	**Others**	**Consolidated**
	HK$'000	HK$'000	HK$'000	HK$'000
REVENUE				
External sales	632,758	123,567	58,062	814,387
RESULT				
Segment result	57,469	18,515	3,198	79,182
Finance charges				(11,871)
Profit before taxation				67,311
Taxation				(5,546)
Profit before minority interests				61,765

2000

The following is an analysis of the carrying amount of segment assets and segment liabilities, analysed by the geographical location of its customers:

	USA	**PRC**	**Others**	**Consolidated**
	HK$'000	HK$'000	HK$'000	HK$'000
ASSETS				
Segment assets	137,256	26,248	5,570	169,074
Unallocated corporate assets				710,851
				879,925
LIABILITIES				
Unallocated corporate liabilities				232,963
OTHER INFORMATION				
Capital additions				73,181
Depreciation and amortisation				34,252

4. BUSINESS AND GEOGRAPHICAL SEGMENTS (Cont'd)

Geographical segments (Cont'd)

In addition to the analysis by the geographical location of its customers, the following is an analysis of the carrying amount of segment assets, and capital expenditure, analysed by the geographical area in which the assets and liabilities are located:

	Carrying amount of segment assets		Capital expenditure	
	2001	2000	**2001**	2000
	HK$'000	HK$'000	**HK$'000**	HK$'000
Hong Kong	**32,750**	51,877	**13**	523
Elsewhere in PRC	**937,193**	828,048	**46,087**	72,658
	969,943	879,925	**46,100**	73,181

5. OPERATING PROFIT

	2001	2000
	HK$'000	HK$'000
Operating profit has been arrived at after charging:		
Directors' remunerations (note 7)	**2,854**	2,353
Retirement benefits scheme contributions	**204**	155
Other staff costs	**18,704**	16,770
Total staff costs	**21,762**	19,278
Auditors' remuneration:		
Current year	**616**	617
Overprovision in prior years	**–**	(270)
Depreciation and amortisation	**37,090**	34,252
Loss on disposal of property, plant and equipment	**–**	1,585
and after crediting:		
Gain on disposal of property, plant and equipment	**533**	–
Interest income	**1,391**	3,050

6. FINANCE CHARGES

	2001 HK$'000	2000 HK$'000
Interest on bank borrowings wholly repayable within five years	**11,336**	11,871

7. DIRECTORS' REMUNERATIONS

Details of remuneration paid by the Group to directors during the year are as follows:

	2001 HK$'000	2000 HK$'000
Directors' fees	**–**	–
Salaries and allowances of executive directors	**2,854**	2,353
Total directors' remunerations	**2,854**	2,353

The emoluments of each of the executive directors of the Company did not exceed HK$1,000,000.

During the year, no emoluments were paid by the Group to the five highest paid individuals (including directors and employees) as an inducement to join or upon joining the Group or as compensation for loss of office. None of the directors has waived any emoluments during the year.

8. EMPLOYEES' EMOLUMENTS

The aggregate emoluments of the five highest paid individuals included three (2000: three) executive directors of the Company, whose emoluments are included in note 7 above. The emoluments of the remaining two (2000: two) highest paid individuals are as follows:

	2001 HK$'000	2000 HK$'000
Salaries and allowances	**1,094**	1,187

The emoluments of each of the highest paid individuals did not exceed HK$1,000,000.

9. TAXATION

The charge represents PRC enterprise income tax calculated at the prevailing rates. Pursuant to the relevant laws and regulations in the PRC, certain of the Group's PRC subsidiaries are entitled to exemption from PRC enterprise income tax for the first two years commencing from their first profit-making year of operation and thereafter, these PRC subsidiaries will be entitled to a 50% relief from PRC enterprise income tax for the following three years. The charge of PRC enterprise income tax for the year has been provided for after taking these tax incentives into account.

No provision for Hong Kong Profits Tax has been made in the financial statements as the companies operating in Hong Kong did not have any estimated assessable income.

A portion of the Group's profit is not subject to taxation in the jurisdiction in which it operates.

There was no significant unprovided deferred taxation for the year or at the balance sheet date.

10. DIVIDEND

	2001	2000
	HK$'000	HK$'000
Final dividend of 1 Hong Kong cent per share for the year ended 31st December, 2000	**6,864**	–

The 2001 final dividend of 1.2 Hong Kong cents per share has been proposed by the directors and is subject to approval by the shareholders in the forthcoming general meeting.

11. EARNINGS PER SHARE

The calculation of the earnings per share for the year is based on profit for the year of HK$42,260,000 (2000: HK$52,526,000) and on 686,400,000 shares (2000: on the weighted average number of 681,322,521 shares) in issue during the year.

The Company has no dilutive potential ordinary shares in issue during the years ended 31st December 2000 and 2001.

12. PROPERTY, PLANT AND EQUIPMENT

	THE GROUP					
	Land and buildings	Furniture and equipment	Motor vehicles	Plant and machinery	Construction in progress	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
COST						
At 1st January, 2001	159,769	28,637	8,467	291,229	49,438	537,540
Additions	14,312	216	344	16,691	14,537	46,100
Transfer	10,089	1,849	–	37,728	(49,666)	–
Disposals	–	–	(2,302)	–	–	(2,302)
At 31st December, 2001	184,170	30,702	6,509	345,648	14,309	581,338
DEPRECIATION AND AMORTISATION						
At 1st January, 2001	23,114	27,347	7,342	86,053	–	143,856
Provided for the year	6,502	1,309	502	28,777	–	37,090
Eliminated on disposals	–	–	(2,302)	–	–	(2,302)
At 31st December, 2001	29,616	28,656	5,542	114,830	–	178,644
NET BOOK VALUES						
At 31st December, 2001	154,554	2,046	967	230,818	14,309	402,694
At 31st December, 2000	136,655	1,290	1,125	205,176	49,438	393,684

The land and buildings of the Group are situated in the PRC and held under medium-term land use rights.

13. INTERESTS IN SUBSIDIARIES

	THE COMPANY	
	2001	2000
	HK$'000	HK$'000
Unlisted shares, at cost	**476,175**	476,175
Amounts due from subsidiaries	**74,818**	52,933
	550,993	529,108

The carrying value of the unlisted shares is based on the book values of the underlying net assets of the subsidiaries attributable to the Group as at the date on which the Company became the holding company of the Group under the group reorganisation in 2000.

Details of the Company's subsidiaries at 31st December, 2001 are set out in note 31.

In the opinion of the directors, the amounts due from subsidiaries are unlikely to be repaid within one year from the balance sheet date and are therefore shown in the balance sheet as non-current.

14. INVESTMENT SECURITIES

	THE GROUP	
	2001	2000
	HK$'000	HK$'000
Capital contribution, at cost	**926**	926

The investment represents the Group's 5% equity interest in 山東高泰鞋業集團股份有限公司 which was established in the PRC as a limited liability company and is engaged in the manufacture and sale of shoes and other leather products.

The directors are of the opinion that the investment is worth at least its carrying value.

15. INVENTORIES

	THE GROUP	
	2001	2000
	HK$'000	HK$'000
Raw materials	**92,695**	81,614
Work in progress	**186,820**	150,759
Finished goods	**17,797**	9,616
	297,312	241,989

Included above is finished goods of HK$1,986,000 (2000: Nil) which is carried at net realisable value.

16. TRADE AND OTHER RECEIVABLES

The Group has a policy of allowing an average credit period of 60 days to its trade customers. Included in trade and other receivables are trade receivables of HK$201,651,000 (2000: HK$169,074,000), the aged analysis of which at the balance sheet date is as follows:

	THE GROUP	
	2001	2000
	HK$'000	HK$'000
Up to 30 days	**80,847**	88,718
31 – 60 days	**59,991**	31,029
61 – 90 days	**27,535**	28,714
More than 90 days	**33,278**	20,613
	201,651	169,074

17. AMOUNT DUE FROM ULTIMATE HOLDING COMPANY

The amount was unsecured, interest-free and was repaid during the year. The maximum amount outstanding during the year was HK$14,000.

18. TRADE AND OTHER PAYABLES

Included in trade and other payables are trade payables of HK$58,150,000 (2000: HK$16,621,000), the aged analysis of which at the balance sheet date is as follows:

	THE GROUP	
	2001	2000
	HK$'000	HK$'000
Up to 30 days	**51,525**	12,331
31 – 60 days	**2,902**	2,078
61 – 90 days	**765**	757
More than 90 days	**2,958**	1,455
	58,150	16,621

19. LOAN FROM A DIRECTOR

The balance represents a loan from Mr. Liaw Yuan Chian which is unsecured, interest-free and repayable on demand.

20. BANK BORROWINGS

	THE GROUP	
	2001	2000
	HK$'000	HK$'000
Secured bank loans	**75,679**	74,958
Unsecured bank loans	**90,209**	96,107
Secured bank overdraft	**151**	–
	166,039	171,065
The bank loans are repayable as follows:		
Within one year	**165,938**	169,623
One to two years	**75**	1,442
Two to five years	**26**	–
	166,039	171,065
Less: Amount due within one year shown under current liabilities	**(165,938)**	(169,623)
Amount due after one year	**101**	1,442

21. SHARE CAPITAL

	Number of shares	Value HK$'000
Ordinary shares of HK$0.10 each		
Authorised:		
At 1st January, 2000	3,500,000	350
Increase during the year	1,496,500,000	149,650
At 31st December, 2000 and 2001	1,500,000,000	150,000
Issued and fully paid:		
At 1st January, 2000	2	–
Issue of shares as consideration for the acquisition of a subsidiary pursuant to the group reorganisation in 2000	19,193,994	1,919
Capitalisation issue of shares	598,566,004	59,857
Issue of new shares upon listing of the Company's shares on the Stock Exchange	68,640,000	6,864
At 31st December, 2000 and 2001	686,400,000	68,640

There was no movement in the Company's share capital during the year ended 31st December, 2001.

22. RESERVES

	Share premium HK$'000	Translation reserve HK$'000	Goodwill reserve HK$'000	Special reserve HK$'000 (Note i)	Contributed surplus HK$'000 (Note ii)	PRC statutory reserves HK$'000 (Note iii)	Other capital reserve HK$'000	Retained profits HK$'000	Total HK$'000
THE GROUP									
At 1st January, 2000	–	4,713	(24,509)	17,009	–	10,815	75,266	244,270	327,564
Premium arising on new issue	61,776	–	–	–	–	–	–	–	61,776
Share issue expenses	(7,598)	–	–	–	–	–	–	–	(7,598)
Capitalisation issue	(54,178)	–	–	–	–	–	–	(5,679)	(59,857)
Exchange differences arising from translation of operations in the PRC	–	1,901	–	–	–	–	–	–	1,901
On group reorganisation in 2000	–	–	–	221,957	–	–	(75,266)	–	146,691
Transfer	–	–	–	–	–	1,334	–	(1,334)	–
Minority share of reserves	–	(134)	–	–	–	(320)	–	–	(454)
Profit for the year	–	–	–	–	–	–	–	52,526	52,526
Dividend	–	–	–	–	–	–	–	(6,864)	(6,864)
At 31st December, 2000 and 1st January, 2001									
– as originally stated	–	6,480	(24,509)	238,966	–	11,829	–	282,919	515,685
– adjust for derecognition of liability for 2000 final dividend (note 2)	–	–	–	–	–	–	–	6,864	6,864
– as restated	–	6,480	(24,509)	238,966	–	11,829	–	289,783	522,549
Transfer	–	–	–	–	–	1,023	–	(1,023)	–
Profit for the year	–	–	–	–	–	–	–	42,260	42,260
Dividend	–	–	–	–	–	–	–	(6,864)	(6,864)
At 31st December, 2001	–	6,480	(24,509)	238,966	–	12,852	–	324,156	557,945

22. RESERVES (Cont'd)

	Share premium HK$'000	Translation reserve HK$'000	Goodwill reserve HK$'000	Special reserve HK$'000 (Note i)	Contributed surplus HK$'000 (Note ii)	PRC statutory reserves HK$'000 (Note iii)	Other capital reserve HK$'000	Retained profits HK$'000	Total HK$'000
THE COMPANY									
At 1st January, 2000	–	–	–	–	–	–	–	–	–
Premium arising on new issue	61,776	–	–	–	–	–	–	–	61,776
Share issue expenses	(7,598)	–	–	–	–	–	–	–	(7,598)
Capitalisation issue	(54,178)	–	–	–	(5,679)	–	–	–	(59,857)
Contributed surplus arising on the group reorganisation in 2000	–	–	–	–	474,255	–	–	–	474,255
Profit for the year	–	–	–	–	–	–	–	26,573	26,573
Dividend	–	–	–	–	–	–	–	(6,864)	(6,864)
At 31st December, 2000 and 1st January, 2001									
– as originally stated	–	–	–	–	468,576	–	–	19,709	488,285
– adjust for derecognition of liability for 2000 final dividend (note 2)	–	–	–	–	–	–	–	6,864	6,864
– as restated	–	–	–	–	468,576	–	–	26,573	495,149
Loss for the year	–	–	–	–	–	–	–	(1,014)	(1,014)
Dividend	–	–	–	–	–	–	–	(6,864)	(6,864)
At 31st December, 2001	–	–	–	–	468,576	–	–	18,695	487,271

At 31st December, 2001, the Company's reserves available for distribution to shareholders of approximately HK$487,271,000 (2000: HK$495,149,000) comprised the contributed surplus and the retained profits of approximately HK$468,576,000 (2000: HK$468,576,000) and approximately HK$18,695,000 (2000: HK$26,573,000), respectively.

Note:

(i) The special reserve of the Group represents the difference between the nominal amount of the ordinary share capital issued by the Company in exchange for the nominal amount of the share capital of Hua Lien Group (Holding) Company, Limited acquired pursuant to the group reorganisation in 2000.

22. RESERVES (Cont'd)

(ii) The contributed surplus of the Company represents the difference between the book value of the underlying net assets of the subsidiaries acquired by the Company under the group reorganisation in 2000 and the nominal value of the Company's shares issued for the acquisition.

(iii) PRC statutory reserves refer to the statutory surplus reserve fund and enterprise expansion fund. As stipulated by the relevant laws and regulations for foreign investment enterprises in the PRC, the PRC subsidiaries of the Group are required to provide for three reserve funds, being a statutory surplus reserve fund, an enterprise expansion fund and a staff welfare and incentive bonus fund. Appropriations to such reserve funds are made out of net profit after taxation of the statutory financial statements of the PRC subsidiaries and the amount and allocation basis are decided by their respective board of directors annually. The statutory surplus reserve fund can be used to make up prior year losses of the PRC subsidiaries, if any, and can be applied in conversion into capital by means of capitalisation issue. The enterprise expansion fund is used for expanding the capital base of the PRC subsidiaries by means of capitalisation.

The amounts transferred to the staff welfare and incentive bonus fund in the statutory financial statements of the PRC subsidiaries have been adjusted in the consolidated financial statements as cost of sales as in the opinion of the directors, this fund will be used to pay incentive bonus and other benefits to the PRC subsidiaries' employees.

23. RECONCILIATION OF PROFIT FROM ORDINARY ACTIVITIES BEFORE TAXATION TO NET CASH INFLOW FROM OPERATING ACTIVITIES

	2001	2000
	HK$'000	HK$'000
Profit from ordinary activities before taxation	**60,179**	67,311
Depreciation and amortisation of property, plant and equipment	**37,090**	34,252
(Gain) loss on disposal of property, plant and equipment	**(533)**	1,585
Interest income	**(1,391)**	(3,050)
Interest expense	**11,336**	11,871
(Increase) decrease in inventories	**(55,323)**	29,215
Increase in trade and other receivables	**(39,047)**	(57,815)
Decrease (increase) in amount due from ultimate holding company	**14**	(14)
Increase (decrease) in trade and other payables	**44,946**	(11,422)
(Decrease) increase in bills payable	**(859)**	2,780
Increase (decrease) in amounts due to minority shareholders	**1,728**	(2,192)
Net cash inflow from operating activities	**58,140**	72,521

24. ANALYSIS OF CHANGES IN FINANCING DURING THE YEAR

	Bank loans with original maturity of more than 3 months	Loan from a director	Share capital (including share premium)
	HK$'000	HK$'000	HK$'000
At 1st January, 2000	141,138	20,721	148,610
Currency realignment	–	(960)	–
On group reorganisation in 2000	–	–	(146,691)
Issue of shares on new issue	–	–	68,640
Expenses incurred on new issue	–	–	(7,598)
Capitalisation issue	–	–	5,679
Borrowings raised	23,585	867	–
Repayment of loans	(19,371)	(15,561)	–
At 31st December, 2000 and 1st January, 2001	145,352	5,067	68,640
Borrowings raised	34,745	8,192	–
Repayment of borrowings	(60,643)	(2,747)	–
At 31st December, 2001	119,454	10,512	68,640

25. ANALYSIS OF THE BALANCES OF CASH AND CASH EQUIVALENTS

	2001	2000
	HK$'000	HK$'000
Bank balances and cash	**27,527**	46,782
Trust receipt and import loans	**(46,434)**	(25,713)
Bank overdraft	**(151)**	–
	(19,058)	21,069

26. COMMITMENTS

(a) Operating lease commitments:

	THE GROUP	
	2001	2000
	HK$'000	HK$'000
Minimum lease payments paid during the year under operating leases in respect of land and buildings	**1,334**	1,319

At the balance sheet date, the Group had commitments for future minimum lease payments under non-cancellable operating leases which fall due as follows:

	THE GROUP	
	2001	2000
	HK$'000	HK$'000
Within one year	**1,206**	1,305
In the second to fifth year inclusive	**5,097**	4,621
Over five years	**6,931**	8,086
	13,234	14,012

Operating lease payments principally represent rentals payable by the Group for certain of its factory properties. Leases are negotiated for an average term of 13 years and rentals are fixed for an average term of 13 years.

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

(b) Capital commitments:

	THE GROUP	
	2001	2000
	HK$'000	HK$'000
Capital expenditure contracted for but not provided in the financial statements in respect of the acquisition of property, plant and equipment	**8,737**	4,969

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

26. COMMITMENTS (Cont'd)

(c) Other commitments:

Under the terms of the cooperative joint venture agreement in respect of Xin Hui Hua Lien Tannery Co., Ltd. ("Xin Hui Hua Lien"), a subsidiary of the Company, Galloon International (Holding) Company, Limited ("Galloon International") is entitled to all of the net profit or loss of Xin Hui Hua Lien throughout the entire cooperative joint venture period after the payment of a pre-determined distribution by Xin Hui Hua Lien each year to the PRC joint venture partner. In the event that Xin Hui Hua Lien does not have sufficient distributable profit to make the required payments to the PRC joint venture partner, Galloon International is responsible for making such payments to the PRC joint venture partner as compensation. At 31st December, 2001, the pre-determined distributions to be paid to the PRC joint venture partner over the entire cooperative joint venture period are as follows:

	THE GROUP	
	2001	2000
	HK$'000	HK$'000
Amount payable:		
Within one year	**5,239**	5,239
One to two years	**5,239**	5,239
Two to five years	**15,180**	15,716
Over five years	**72,388**	77,091
	98,046	103,285

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

27. CONTINGENT LIABILITIES

	THE GROUP	
	2001	2000
	HK$'000	HK$'000
Bills discounted with recourse	**1,339**	–

The Company did not have any significant contingent liabilities at the balance sheet date.

28. BANKING FACILITIES

At 31st December, 2001, the Group's short-term bank borrowings were secured by the following:

(i) certain of the Group's leasehold land and buildings with a carrying value of approximately HK$46 million (2000: HK$49 million);

(ii) bank deposits of the Group and the Company of approximately HK$15 million (2000: HK$11 million) and HK$0.5 million (2000: Nil) respectively;

(iii) cross-guarantees between subsidiaries;

(iv) the Company's corporate guarantees (at the balance sheet date, the aggregate amounts utilised by these subsidiaries amounted to approximately HK$54 million (2000: HK$8.3 million));

(v) corporate guarantee given by Xian People's Tannery, a minority shareholder of a subsidiary; and

(vi) certain of the plant and machinery of Xian Hua Lien Tannery Co., Ltd. ("Xian Hua Lien") with an aggregate carrying value of approximately HK$33 million (2000: HK$38 million).

29. RETIREMENT BENEFITS SCHEMES

The Group operates a Mandatory Provident Fund ("MPF") Scheme for all qualifying employees in Hong Kong. The assets of the MPF scheme are held separately from those of the Group in funds under the control of trustees.

The PRC subsidiaries are required to contribute a certain percentage, ranging from 18% to 20%, of the payroll of their employees to the retirement benefits schemes to fund the benefits. The only obligation of the Group with respect to the retirement benefits schemes is to make the required contributions under the respective schemes.

At the balance sheet date, there were no significant forfeited contributions, which arose upon employees leaving the retirement benefits schemes, available to reduce the contribution payable in the future periods.

30. RELATED PARTY TRANSACTIONS AND BALANCES

During the year, the Group had certain transactions with related parties. Details of these transactions for the year and balances at 31st December, 2001 with these related parties are as follows:

(a) Transactions

(i) A subsidiary entered into a lease agreement (the "Lease Agreement") with Xian People's Tannery to lease the land use rights related to the site on which the factory building of the subsidiary is located at a monthly rental of RMB102,000 (approximately HK$96,000). During the year, the Group paid rental expense of approximately HK$1,155,000 (2000: HK$1,155,000) to Xian People's Tannery and the amount paid was in accordance with terms of the Lease Agreement.

(ii) During the year, a subsidiary sold raw materials amounting to approximately HK$5,119,000 (2000: Nil) to Chai Watana Tannery Public Company Limited, a shareholder of the Company. The transactions were carried out at cost plus a percentage profit mark-up.

(b) Balances

Details of balances with the related parties at the balance sheet date are set out in the consolidated balance sheet, notes 17 and 19.

(c) Other

(1) The Group was committed to pay a pre-determined distribution to the PRC joint venture partner of Xin Hui Hua Lien, details of which are set out in note 26(c).

(2) The Group's banking facilities were secured by guarantee given by a related party, details of which are set out in note 28.

31. SUBSIDIARIES

Details of the Company's subsidiaries at 31st December, 2001 are as follows:

Name of company	Place of incorporation/ operations	Nominal value of issued and fully paid share capital/ registered capital	Effective proportion of issued/ registered capital held by the Company	Principal activities
Hua Lien Group (Holding) Company, Limited ("Hua Lien Group (Holding)")	British Virgin Islands/Hong Kong	Ordinary shares US$19,193,996 Note (i)	100%	Investment holding
Galloon International (Holding) Company, Limited ("Galloon International")	British Virgin Islands/Taiwan	Ordinary shares US$1	100%	Sale and marketing of leather, raw materials sourcing and investment holding
Hua Lien (Hong Kong) Company Limited ("Hua Lien Hong Kong")	Hong Kong	Ordinary shares HK$10,000 Non-voting deferred shares HK$15,000,000 Note (ii)	100%	Provision of management services
新會華聯製皮工業有限公司 Xin Hui Hua Lien Tannery Co., Ltd.	PRC	Registered capital US$14,522,000	70.5% Note (iii)	Manufacture and sale of leather
新會嘉聯皮革工業有限公司 Xin Hui Galloon Tannery Co., Ltd. ("Xin Hui Galloon")	PRC	Registered capital US$21,700,000 Note (iv)	100%	Manufacture and sale of leather
西安華聯製皮工業有限公司 Xian Hua Lien Tannery Co., Ltd.	PRC	Registered capital US$7,530,000	51% Note (v)	Manufacture and sale of leather

31. SUBSIDIARIES (Cont'd)

Notes:

(i) Hua Lien Group (Holding) is held by the Company directly. All other subsidiaries are held by the Company indirectly.

(ii) The deferred shares of Hua Lien Hong Kong, which are not held by the Group, practically carry no rights to dividends or to receive notice of or to attend or vote at any of its general meetings or to participate in any distribution on its winding up.

(iii) Xin Hui Hua Lien was initially established as a limited liability equity joint venture enterprise for a term of 20 years commencing 27th August, 1992. Pursuant to a management agreement (the "Management Agreement") entered into between Galloon International and Xin Hui Hua Lien, Galloon International guaranteed that Xin Hui Hua Lien's distributable profit would reach pre-determined levels (the "Guaranteed Profit") for each of the five years commencing 1st April, 1996. In the event that Xin Hui Hua Lien failed to make the Guaranteed Profit, Galloon International would be responsible to pay such Guaranteed Profit to Xin Hui Hua Lien to ensure that its distributable profit reached such levels. If the distributable profit of Xin Hui Hua Lien exceeded the Guaranteed Profit, Galloon International would be entitled to all such excess profits.

On 26th June, 1998, Xin Hui Hua Lien was converted into a limited liability cooperative joint venture enterprise and its term of operation was extended to 26th August, 2022. The Management Agreement was then terminated. Under the terms of the cooperative joint venture agreement, Galloon International holds 70.5% of the registered capital of Xin Hui Hua Lien, but it is entitled to all of the net profit or loss of Xin Hui Hua Lien throughout the entire cooperative joint venture period, after the payment of a pre-determined distribution by Xin Hui Hua Lien each year to the cooperative joint venture partner, details of which are set out in note 26(c).

At the end of the cooperative joint venture period, Galloon International is entitled to the distribution of all the remaining assets of Xin Hui Hua Lien according to its capital contribution ratio in Xin Hui Hua Lien.

(iv) As at the date of this report, the registered capital of Xin Hui Galloon was paid up to the extent of US$14,000,000 (2000: US$14,000,000).

31. SUBSIDIARIES (Cont'd)

(v) The Group holds a 51% equity interest in Xian Hua Lien with the remaining 49% held by Xian People's Tannery. Xian Hua Lien was established on 18th December, 1992 as a limited liability sino-foreign equity joint venture enterprise ("EJV") for a term of operation of 20 years. Since the establishment of Xian Hua Lien, Xian People's Tannery received 40% of the profit distribution made by Xian Hua Lien in respect of the period from the date of its establishment to 31st December, 2001 (rather than in proportion to the 49% equity interest that it holds in Xian Hua Lien) and, pursuant to an agreement dated 31st December, 2001 made between Galloon International, Hua Lien Hong Kong, Xian Hua Lien and itself, Xian People's Tannery waived its remaining entitlement to such profit distribution in favour of the Group. The Group therefore effectively had a 60% attributable economic interest in Xian Hua Lien for the period from the date of establishment of Xian Hua Lien to 31st December, 2001.

At the end of the equity joint venture period, the Group is entitled to the distribution of all the remaining assets in Xian Hua Lien according to its capital contribution ratio in Xian Hua Lien.

In May 2000, Xian Hua Lien was converted into a limited liability sino-foreign cooperative joint venture enterprise ("CJV") with the same operating terms. According to the conversion document, the conversion would be effective on issuance of the renewed business licence, which had not been issued up to the date of this report. As a result, Xian Hua Lien continues to be treated as an EJV at the balance sheet date. Under the terms of the joint venture agreement of the CJV, Xian People's Tannery would entitle to receive 39% of the profit distribution each year from Xian Hua Lien, rather than in proportion to the 49% equity interest that it holds in Xian Hua Lien as an EJV.

None of the subsidiaries had any debt securities outstanding at the end of the year, or at any time during the year.