## 1. GENERAL

The Company is incorporated in Bermuda as an exempted company with limited liability and its shares are listed on The Stock Exchange of Hong Kong Limited. The address of the registered office and principal place of business of the Company are disclosed on page 93 to the annual report.

The financial statements are presented in Hong Kong dollars, which is the same as the functional currency of the Company.

The principal activities of the Group are the manufacture, retailing and trading of garments.

## 2. APPLICATION OF HONG KONG FINANCIAL REPORTING STANDARDS/CHANGES IN ACCOUNTING POLICIES

In the current year, the Group has applied, for the first time, a number of new Hong Kong Financial Reporting Standards ("HKFRSs"), Hong Kong Accounting Standards ("HKASs") and Interpretations (hereinafter collectively referred to as "New HKFRSs") issued by the Hong Kong Institute of Certified Public Accountants (the "HKICPA") that are effective for accounting periods beginning on or after 1 January 2005. The application of the New HKFRSs has resulted in a change in the presentation of the consolidated income statement, consolidated balance sheet and consolidated statement of changes in equity. In particular, the presentation of minority interests and share of tax of jointly controlled entities have been changed. The changes in presentation have been applied retrospectively. The adoption of the New HKFRSs has resulted in changes to the Group's accounting policies in the following areas that have an effect on how the results for the current and prior accounting years are prepared and presented:

**Business combinations**

In the current year, the Group has applied HKFRS 3 "Business combinations" which is effective for business combinations for which the agreement date is on or after 1 January 2005. The principal effects of the application of HKFRS 3 to the Group are summarised below:

*Goodwill*

In previous years, goodwill arising on acquisitions prior to 1 January 2001 was held in reserves. The Group has applied the relevant transitional provisions in HKFRS 3 from 1 January 2005. Goodwill previously recognised in reserves amounting to HK$2,527,000 has been transferred to the Group's accumulated profits on 1 January 2005. Comparative figures for 2004 have not been restated.

## 2. APPLICATION OF HONG KONG FINANCIAL REPORTING STANDARDS/CHANGES IN ACCOUNTING POLICIES *(cont'd)*

**Business combinations** *(cont'd)*

*Excess of the Group's interest in the net fair value of acquiree's identifiable assets, liabilities and contingent liabilities over cost (previously known as "negative goodwill")*

In accordance with HKFRS 3, any excess of the Group's interest in the net fair value of acquiree's identifiable assets, liabilities and contingent liabilities over the cost of acquisition ("discount on acquisition") is recognised immediately in profit or loss in the period in which the acquisition takes place. In previous periods, negative goodwill arising on acquisitions prior to 1 January 2005 was held in reserves. In accordance with the relevant transitional provisions in HKFRS 3, the Group has derecognised all negative goodwill at 1 January 2005 (of which negative goodwill of HK$8,588,000 was previously recorded in capital reserve), with a corresponding increase to accumulated profits.

**Interests in jointly controlled entities**

In previous years, interests in jointly controlled entities were accounted for using the equity method. HKAS 31 "Interests in jointly controlled entities" allows entities to use either proportionate consolidation or the equity method to account for its interests in jointly controlled entities. Upon the application of HKAS 31, the Group has elected to continue applying the equity method to account for its interests in jointly controlled entities. As a result, there has been no change in accounting method in respect of the Group's interests in jointly controlled entities.

**Share-based payments**

In the current year, the Group has applied HKFRS 2 "Share-based payment" which requires an expense to be recognised where the Group buys goods or obtains services in exchange for shares or rights over shares ("equity-settled transactions"), or in exchange for other assets equivalent in value to a given number of shares or rights over shares ("cash-settled transactions"). The principal impact of HKFRS 2 on the Group is in relation to the expensing of the fair value of share options granted to directors and employees of the Company, determined at the date of grant of the share options, over the vesting period. Prior to the application of HKFRS 2, the Group did not recognise the financial effect of these share options until they were exercised. The Group has applied HKFRS 2 to share options granted on or after 1 January 2005. In relation to share options granted by 1 January 2005, the Group chooses not to apply HKFRS 2 with respect to share options granted on or before 7 November 2002 and vested before 1 January 2005. All share options are granted before 7 November 2002. Therefore, the change in accounting policy has had no effect on the results for the current or prior periods.

## 2. APPLICATION OF HONG KONG FINANCIAL REPORTING STANDARDS/CHANGES IN ACCOUNTING POLICIES *(cont'd)*

**Financial instruments**

In the current year, the Group has applied HKAS 32 "Financial Instruments: Disclosure and Presentation" and HKAS 39 "Financial Instruments: Recognition and Measurement". HKAS 32 requires retrospective application. HKAS 39, which is effective for accounting periods beginning on or after 1 January 2005, generally does not permit to recognise, derecognise or measure financial assets and liabilities on a retrospective basis. The principal effects resulting from the implementation of HKAS 32 and HKAS 39 are summarised below:

*Classification and measurement of financial assets and financial liabilities*

The Group has applied the relevant transitional provisions in HKAS 39 with respect to classification and measurement of financial assets and financial liabilities that are within the scope of HKAS 39.

At 31 December 2004, the Group classified and measured its debt and equity securities in accordance with the benchmark treatment of Statement of Standard Accounting Practice 24 ("SSAP 24"). Under SSAP 24, investments in debt or equity securities are classified as "investment securities", "other investments" or "held-to-maturity investments" as appropriate. "Investment securities" are carried at cost less impairment losses (if any) while "other investments" are measured at fair value, with unrealised gains or losses included in the profit or loss. "Held-to-maturity investments" are carried at amortised cost less impairment losses (if any). From 1 January 2005 onwards, the Group has classified and measured its debt and equity securities in accordance with HKAS 39. Under HKAS 39, financial assets are classified as "financial assets at fair value through profit or loss", "available-for-sale financial assets", "loans and receivables", or "held-to-maturity financial assets". "Financial assets at fair value through profit or loss" and "available-for-sale financial assets" are carried at fair value, with changes in fair values recognised in profit or loss and equity respectively. Available-for-sale equity investments that do not have quoted market prices 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 instruments are measured at cost less impairment after initial recognition. "Loans and receivables" and "held-to-maturity financial assets" are measured at amortised cost using the effective interest method after initial recognition.

On 1 January 2005, the Group classified and measured its equity securities in accordance with the requirements of HKAS 39. Investment securities classified under non-current assets of HK$13,793,000 were reclassified to available-for-sale investments on 1 January 2005.

*Financial assets and financial liabilities other than debt and equity securities*

From 1 January 2005 onwards, the Group has classified and measured its financial assets and financial liabilities other than debt and equity securities (which were previously outside the scope of SSAP 24) in accordance with the requirements of HKAS 39. As mentioned above, financial assets under HKAS 39 are classified as "financial assets at fair value through profit or loss", "available-for-sale financial assets", "loans and receivables" or "held-to-maturity financial assets". Financial liabilities are generally classified as "financial liabilities at fair value through profit or loss" or "other financial liabilities". Financial liabilities at fair value through profit or loss are measured at fair value, with changes in fair value being recognised in profit or loss directly. Other financial liabilities are carried at amortised cost using the effective interest method after initial recognition.

## 2. APPLICATION OF HONG KONG FINANCIAL REPORTING STANDARDS/CHANGES IN ACCOUNTING POLICIES *(cont'd)*

**Financial instruments** *(cont'd)*

*Derivatives and hedging*

In previous years, the gain or loss on a speculative forward contract is the foreign currency amount of the contract multiplied by the difference between the forward rate for the balance of the contract at the balance sheet date and the contracted forward rate. Where a forward contract is speculative the gain or loss should be credited or charged to the profit and loss account.

From 1 January 2005 onwards, all derivatives that are within the scope of HKAS 39 are required to be carried at fair value at each balance sheet date regardless of whether they are deemed as held for trading or designated as effective hedging instruments. Under HKAS 39, derivatives (including embedded derivatives separately accounted for from the non-derivative host contracts) are deemed as held-for-trading financial assets or financial liabilities, unless they qualify and are designated as effective hedging instruments. The corresponding adjustments on changes in fair values would depend on whether the derivatives are designated as effective hedging instruments, and if so, the nature of the item being hedged. For derivatives that are deemed as held for trading, changes in fair values of such derivatives are recognised in profit or loss for the period in which they arise.

There are three types of hedge relationships under HKAS 39, including fair value hedges, cash flow hedges and net investment hedges. The Group designates certain derivatives as hedging instruments to hedge against its exposure in relation to foreign currency forecast purchases. For cash flow hedges, changes in the fair value of the effective portion of hedging instruments are recognised initially in equity and 'recycled' into the income statement when the hedged items affect profit or loss. Changes in the fair value of the ineffective portion of hedging instruments are recognised directly in profit or loss.

The Group has applied the relevant transitional provisions in HKAS 39. For derivatives that are not held for hedging purposes, on 1 January 2005, the Group recognised the difference between the previous carrying amount recognised on the balance sheet and the fair value on 1 January 2005, amounting to HK$1,071,000, in the Group's accumulated profits (see note 3 for the financial impact).

## 2. APPLICATION OF HONG KONG FINANCIAL REPORTING STANDARDS/CHANGES IN ACCOUNTING POLICIES *(cont'd)*

**Financial instruments** *(cont'd)*

*Derecognition*

HKAS 39 provides more rigorous criteria for the derecognition of financial assets than the criteria applied in previous periods. Under HKAS 39, a financial asset is derecognised, when and only when, either the contractual rights to the asset's cash flows expire, or the asset is transferred and the transfer qualifies for derecognition in accordance with HKAS 39. The decision as to whether a transfer qualifies for derecognition is made by applying a combination of risks and rewards and control tests. The Group has applied the relevant transitional provisions and applied the revised accounting policy prospectively for transfers of financial assets on or after 1 January 2005. As a result, the Group's bills receivable discounted with full recourse which were derecognised prior to 1 January 2005 have not been restated. As at 31 December 2005, the Group's bills receivable discounted with full recourse have not been derecognised. Instead, the related borrowings of HK$17,055,000 have been recognised on the balance sheet date. The relevant finance costs incurred in order to obtain such borrowings are included in the carrying amount of the borrowings on initial recognition and amortised over the terms of the borrowings using the effective interest method. This change in accounting policy has had no material effect on results for the current year.

**Owner-occupied leasehold interest in land**

In previous years, owner-occupied leasehold land and buildings were included in property, plant and equipment and measured using the cost model. In the current year, the Group has applied HKAS 17 "Leases". Under HKAS 17, the land and buildings elements of a leasehold land and buildings are considered separately for the purposes of lease classification, unless the lease payments cannot be allocated reliably between the land and buildings elements, in which case, the entire lease is generally treated as a finance lease. To the extent that the allocation of the lease payments between the land and buildings elements can be made reliably, the leasehold interests in land are reclassified to prepaid lease payments under operating leases, which are carried at cost and amortised over the lease term on a straight-line basis. This change in accounting policy has been applied retrospectively (see note 3 for the financial impact).

**Investment properties**

In the current year, the Group has, for the first time, applied HKAS 40 "Investment property". The Group has elected to use the fair value model to account for its investment properties which requires gains or losses arising from changes in the fair value of investment properties to be recognised directly in the profit or loss for the year in which they arise. In previous years, investment properties under the predecessor standard were measured at open market values, with revaluation surplus or deficit credited or charged to investment properties revaluation reserve unless the balance on this reserve was insufficient to cover a revaluation decrease, in which case the excess of the revaluation decrease over the balance on the investment properties revaluation reserve was charged to the income statement. Where a decrease had previously been charged to the income statement and revaluation subsequently arose, that increase was credited to the income statement to the extent of the decrease previously charged. The Group has applied the relevant transitional provisions in HKAS 40 and elected to apply HKAS 40 from 1 January 2005 onwards. The amount held in investment properties revaluation reserve at 1 January 2005 has been transferred to the Group's accumulated profits (see note 3 for the financial impact).

## 2. APPLICATION OF HONG KONG FINANCIAL REPORTING STANDARDS/CHANGES IN ACCOUNTING POLICIES *(cont'd)*

**Deferred taxes related to investment properties**

In previous years, deferred tax consequences in respect of revalued investment properties were assessed on the basis of the tax consequence that would follow from recovery of the carrying amount of the properties through sale in accordance with the predecessor interpretation. In the current year, the Group has applied HK(SIC)-Interpretation 21 "Income taxes – recovery of revalued non-depreciable assets" which removes the presumption that the carrying amount of investment properties is to be recovered through sale. Therefore, the deferred tax consequences of the investment properties are now assessed on the basis that reflect the tax consequences that would follow from the manner in which the Group expects to recover the property at each balance sheet date. In the absence of any specific transitional provisions in HK(SIC)-Interpretation 21, this change in accounting policy has been applied retrospectively. Comparative figures for 2004 have been restated (see note 3 for the financial impact).

## 3. SUMMARY OF THE EFFECT OF THE CHANGES IN ACCOUNTING POLICIES

The effect of the changes in the accounting policies described in note 2 on the results for the current year and prior year are as follows:

| | **2005** | 2004 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| Gain arising from fair value changes of investment properties | **22,400** | – |
| Increase in deferred taxation liabilities in relation to investment properties | **(3,920)** | – |
| Gains arising from fair value changes of derivative financial instruments | **(1,071)** | – |
| Increase in net profit for the year | **17,409** | – |

## 3. SUMMARY OF THE EFFECT OF THE CHANGES IN ACCOUNTING POLICIES *(cont'd)*

The cumulative effect of the application of the New HKFRSs on the balance sheet as at 31 December 2004 and 1 January 2005 are summarised below:

| | **As at 31 December 2004 (originally stated)** | **Adjustments** | **As at 31 December 2004 (restated)** | **Adjustments** | **As at 1 January 2005 (restated)** |
|---|---|---|---|---|---|
| | HK$'000 | HK$'000 | HK$'000 | HK$'000 | HK$'000 |
| **Balance sheet items** | | | | | |
| ASSETS AND LIABILITIES | | | | | |
| Impact on HKAS 17 | | | | | |
| Property, plant and equipment | 399,872 | (44,928) | 354,944 | – | 354,944 |
| Prepaid lease payments | – | 44,928 | 44,928 | – | 44,928 |
| Impact on HKAS 39 | | | | | |
| Investments in securities | 13,793 | – | 13,793 | (13,793) | – |
| Available-for-sale investments | – | – | – | 13,793 | 13,793 |
| Derivatives | – | – | – | 1,071 | 1,071 |
| Impact of HK(SIC) – INT 21 | | | | | |
| Deferred tax liabilities | 2,012 | 812 | 2,824 | – | 2,824 |
| RESERVES | | | | | |
| Capital reserve | 6,061 | – | 6,061 | (6,061) | – |
| Investment properties revaluation reserve | 4,636 | (812) | 3,824 | (3,824) | – |
| Accumulated profits | 301,392 | – | 301,392 | 10,956 | 312,348 |
| Minority interests | – | 800 | 800 | – | 800 |
| MINORITY INTERESTS | 800 | (800) | – | – | – |

## 3. SUMMARY OF THE EFFECT OF THE CHANGES IN ACCOUNTING POLICIES *(cont'd)*

The financial effects of the application of New HKFRSs to the Group's equity on 1 January 2004 are summarised below:

| | **Investment properties revaluation reserve** HK$ |
|---|---|
| As originally stated | 3,359 |
| Adoption of HK(SIC) – INT 21 deferred tax liabilities | (588) |
| As restated | 2,771 |

The Group has not early applied the following new standards, interpretations and amendments that have been issued but are not yet effective as at 31 December 2005 (the "2006 New Standards").

| | |
|---|---|
| HKAS 1 (Amendment) | Capital disclosures[1] |
| HKAS 19 (Amendment) | Actuarial gains and losses, group plans and disclosures[2] |
| HKAS 39 (Amendment) | Cash flow hedge accounting of forecast intragroup transactions[2] |
| HKAS 39 (Amendment) | The fair value option[2] |
| HKAS 39 & HKFRS 4 (Amendments) | Financial guarantee contracts[2] |
| HKFRS 6 | Exploration for and evaluation of mineral resources[2] |
| HKFRS 7 | Financial instruments: Disclosures[1] |
| HK(IFRIC) – INT 4 | Determining whether an arrangement contains a lease[2] |
| HK(IFRIC) – INT 5 | Rights to interests arising from decommissioning, restoration and environmental rehabilitation funds[2] |
| HK(IFRIC) – INT 6 | Liabilities arising from participating in a specific market-waste electrical and electronic equipment[3] |
| HK(IFRIC) – INT 7 | Applying the restatement approach under HKAS 29 Financial Reporting in Hyperinflationary Economies[4] |

1 Effective for accounting periods beginning on or after 1 January 2007.
2 Effective for accounting periods beginning on or after 1 January 2006.
3 Effective for accounting periods beginning on or after 1 December 2005.
4 Effective for accounting periods beginning on or after 1 March 2006.

## 3. SUMMARY OF THE EFFECT OF THE CHANGES IN ACCOUNTING POLICIES *(cont'd)*

The Group has commenced considering the potential impact of the 2006 New Standards, and determined that except for HKAS 39 and HKFRS 4 (Amendments) "Financial guarantee contracts", the management anticipates the application of the 2006 New Standards will have no material impact on the Group's financial statements.

HKAS 39 and HKFRS 4 (Amendments) requires financial guarantee contract which is within the scope of HKAS 39 to be measured at fair value on initial recognition. The management determined that it is not yet in a position to reasonably ascertain how the amendment may affect the results of operations and financial position of the Group are prepared and presented.

## 4. SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements have been prepared on the historical cost basis except for investment properties and financial instruments, which are measured at revalued amounts or fair values, as explained in the accounting policies set out below.

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 The Stock Exchange of Hong Kong Limited and by the Hong Kong Companies Ordinance.

**Basis of consolidation**

The consolidated financial statements incorporate the financial statements of the Company and its subsidiaries.

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

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 on consolidation.

Minority interests in the net assets of consolidated subsidiaries are presented separately from the Group's equity therein. Minority interests in the net assets consist of the amount of those interests at the date of the original business combination and the minority's share of changes in equity since the date of the combination. Losses applicable to the minority in excess of the minority's interest in the subsidiary's equity are allocated against the interests of the Group except to the extent that the minority has a binding obligation and is able to make an additional investment to cover the losses.

## 4. SIGNIFICANT ACCOUNTING POLICIES *(cont'd)*

**Interests in associates**

The results and assets and liabilities of associates are incorporated in these financial statements using the equity method of accounting. Under the equity method, investments in associates are carried in the consolidated balance sheet at cost as adjusted for post-acquisition changes in the Group's share of the profit or loss and of changes in equity of the associate, less any identified impairment loss. When the Group's share of losses of an associate equals or exceeds its interest in that associate (which includes any long-term interests that, in substance, form part of the Group's net investment in the associate), the Group discontinues recognising its share of further losses. An additional share of losses is provided for and a liability is recognised only to the extent that the Group has incurred legal or constructive obligations or made payments on behalf of that associate.

Where a group entity transacts with an associate of the Group, profits and losses are eliminated to the extent of the Group's interest in the relevant associate.

**Jointly controlled entities**

Joint venture arrangements that involve the establishment of a separate entity in which venturers have joint control over the economic activity of the entity are referred to as jointly controlled entities.

The results and assets and liabilities of jointly controlled entities are incorporated in the consolidated financial statements using the equity method of accounting. Under the equity method, investments in jointly controlled entities are carried in the consolidated balance sheet at cost as adjusted for post-acquisition changes in the Group's share of the profit or loss and of changes in equity of the jointly controlled entities, less any identified impairment loss. When the Group's share of losses of a jointly controlled entity equals or exceeds its interest in that jointly controlled entity (which includes any long-term interests that, in substance, form part of the Group's net investment in the jointly controlled entity), the Group discontinues recognising its share of further losses. An additional share of losses is provided for and a liability is recognised only to the extent that the Group has incurred legal or constructive obligations or made payments on behalf of that jointly controlled entity.

When a group entity transacts with a jointly controlled entity of the Group, unrealised profits or losses are eliminated to the extent of the Group's interest in the jointly controlled entity, except to the extent that unrealised losses provide evidence of an impairment of the asset transferred, in which case, the full amount of losses is recognised.

## 4. SIGNIFICANT ACCOUNTING POLICIES *(cont'd)*

**Revenue recognition**

Revenue is measured at the fair value of the consideration receive or receivable.

Sales of goods are recognised when goods are delivered and title has passed.

Rental income is recognised on a straight-line basis over the lease terms.

Interest income from a financial asset is accrued on a time basis, by reference to the 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.

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

Commission and management fee income are recognised when services are provided.

**Property, plant and equipment**

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

Depreciation and amortisation is provided to write off the cost of items of property, plant and equipment, other than construction in progress, over their estimated useful lives and taking into account their estimated residual value, using the straight-line method.

Assets held under finance leases are depreciated over their expected useful lives on the same basis as owned assets or, where shorter, the term of the relevant lease.

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 derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the item) is included in the income statement in the year in which the item is derecognised.

## 4. SIGNIFICANT ACCOUNTING POLICIES *(cont'd)*

**Investment properties**

On initial recognition, investment properties are measured at cost, including any directly attributable expenditure. Subsequent to initial recognition, investment properties are measured using the fair value model. Gains or losses arising from changes in the fair value of investment property are included in profit or loss for the period in which they arise.

An investment property is derecognised upon disposal or when the investment property is permanently withdrawn from use or no future economic benefits are expected from its disposals. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in the income statement in the year in which the item is derecognised.

**Intangible assets**

On initial recognition, intangible assets acquired separately are recognised at cost. After initial recognition, intangible assets with finite useful lives are carried at cost less accumulated amortisation and any accumulated impairment losses. Amortisation for intangible assets with finite useful lives is provided on a straight-line basis over their estimated useful lives.

Gains or losses arising from derecognition of an intangible asset are measured at the difference between the net disposal proceeds and the carrying amount of the asset and are recognised in the income statement when the asset is derecognised.

Intangible assets with finite useful lives are tested for impairment when there is an indication that an asset may be impaired.

**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*

Assets held under finance leases are recognised as assets of the Group at their fair value at the inception of the lease or, if lower, at the present value of the minimum lease payments. The corresponding liability to the lessor is included in the balance sheet as a finance lease obligation. Lease payments are apportioned between finance charges and reduction of the lease obligation so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged directly to profit or loss.

Rentals payable under operating leases are charged to profit or loss on a straight-line basis over the term of the relevant lease. Benefits received and receivable as an incentive to enter into an operating lease are recognised as a reduction of rental expense over the lease term on a straight-line basis.

## 4. SIGNIFICANT ACCOUNTING POLICIES *(cont'd)*

**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 its 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 each balance sheet date, monetary items denominated in foreign currencies are retranslated at the rates prevailing on the balance sheet 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 translation of monetary items, are recognised in profit or loss in the period in which they arise, except for exchange differences arising on a monetary item that forms part of the Company's net investment in a foreign operation, in which case, such exchange differences are recognised in equity in the consolidated financial statements. Exchange differences arising on the retranslation of non-monetary items carried at fair value are included in profit or loss for the period except for differences arising on the retranslation of non-monetary items in respect of which gains and losses are recognised directly in equity, in which cases, the exchange differences are also recognised directly in equity.

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 Company (i.e. Hong Kong dollars) at the rate of exchange prevailing at the balance sheet date, and their income and expenses are translated at the average exchange rates for the year, unless exchange rates fluctuate significantly during the period, in which case, the exchange rates prevailing at the dates of transactions are used. Exchange differences arising, if any, are recognised as a separate component of equity (the translation reserve). Such exchange differences are recognised in profit or loss in the period in which the foreign operation is disposed of.

**Taxation**

Taxation 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 as reported in the income statement 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 substantially enacted by the balance sheet date.

## 4. SIGNIFICANT ACCOUNTING POLICIES *(cont'd)*

**Taxation** *(cont'd)*

Deferred tax is the tax expected to be payable or recoverable on differences between the carrying amount of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit, and is accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognised for all taxable temporary differences, and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which 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 arising on investments in subsidiaries, associates and jointly controlled entities, except where the Group as the parent or a venturer is able to control the reversal of the temporary difference and it is probable that the temporary differences will not reverse in the foreseeable future.

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

Deferred tax is calculated at the tax rates that are expected to apply in the year when the liability is settled or the asset is realised. Deferred tax is charged or credited to the income statement, except when it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity.

**Inventories**

Inventories are stated at the lower of cost and net realisable value. Cost is calculated using first-in, first-out method. Cost comprises direct materials and, where applicable, direct labour costs and those overheads that have been incurred in bringing the inventories to their present location and condition. Net realisable value represents the estimated selling price less all estimated costs to completion and costs to be incurred in marketing, selling and distribution.

**Retirement benefit costs**

Payments to Mandatory Provident Fund Scheme and state-managed retirement benefit scheme are charged as expenses as they fall due.

## 4. SIGNIFICANT ACCOUNTING POLICIES *(cont'd)*

**Financial instruments**

Financial assets and financial liabilities are recognised on the balance sheet when a group entity becomes a party to the contractual provisions of the instruments. 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 and 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 three categories, including financial assets at fair value through profit or loss, loans and receivables and available-for-sale financial assets. The accounting policies adopted in respect of each category of financial assets are set out below.

Financial assets at fair value through profit or loss

Financial assets at fair value through profit or loss includes financial assets held for trading. At each balance sheet date subsequent to initial recognition, financial assets at fair value through profit or loss are measured at fair value, with changes in fair value recognised directly in profit or loss in the period in which they arise.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. At each balance sheet date subsequent to initial recognition, loans and receivables (including trade and bills receivables, deposits and other receivables and bank balances) are carried at amortised cost using the effective interest method, less any identified impairment losses. An impairment loss is recognised in profit or loss when there is objective evidence that the asset is impaired, and is measured as the difference between the asset's carrying amount and the present value of the estimated future cash flows discounted at the original effective interest rate. Impairment losses are reversed in subsequent periods when an increase in the asset's recoverable amount can be related objectively to an event occurring after the impairment was recognised, subject to a restriction 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 *(cont'd)*

**Financial instruments** *(cont'd)*

*Financial assets (cont'd)*

Available-for-sale financial assets

Available-for-sale financial assets are non-derivatives that are either designated or not classified as any of the other categories (set out above).

For available-for-sale 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 instruments, they are measured at cost less any identified impairment losses at each balance sheet date subsequent to initial recognition. An impairment loss is recognised in profit or loss when there is objective evidence that the asset is impaired. The amount of the impairment loss is measured as the difference between the carrying amount of the asset 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 losses will not reverse in subsequent periods.

*Financial liabilities and equity*

Financial liabilities and equity instruments issued by a group entity are classified according to the substance of the contractual arrangements entered into and the definitions of a financial liability and an equity instrument.

An equity instrument is any contract that evidences a residual interest in the assets of the Group after deducting all of its liabilities. The Group's financial liabilities are generally classified into financial liabilities at fair value through profit or loss and other financial liabilities. The accounting policies adopted in respect of financial liabilities and equity instruments are set out below.

Financial liabilities at fair value through profit or loss

Financial liabilities at fair value through profit or loss includes financial liabilities held for trading. At each balance sheet date subsequent to initial recognition, financial liabilities at fair value through profit or loss are measured at fair value, with changes in fair value recognised directly in profit or loss in the period in which they arise.

Other financial liabilities

Other financial liabilities including trade payables, bills payable, other payables and accruals, amounts due to jointly-controlled entities, amount due to an associate, bank borrowings are subsequently measured at amortised cost, using the effective interest rate method.

Equity instruments

Equity instruments issued by the Company are recorded at the proceeds received, net of direct issue costs.

## 4. SIGNIFICANT ACCOUNTING POLICIES *(cont'd)*

**Financial instruments** *(cont'd)*

*Financial liabilities and equity (cont'd)*

Derivative financial instruments and hedging

The Group uses derivative financial instruments (primarily forward contracts) to hedge its exposure against the forecast purchases. Such derivatives are measured at fair value regardless of whether they are designated as effective hedging instruments. This hedge is classified as cash flow hedges when hedges are made to hedge against exposure to variability in cash flows that are attributable to a particular risk associated with a recognised asset or liability or a highly probable forecast transaction. The accounting treatments of cash flows hedges are set out below:

Cash flow hedges

For cash flow hedges that qualify for hedge accounting, the effective portion of the gains or losses arising on the changes in fair value of hedging instruments is initially recognised in equity and "recycled" into the income statement when the hedged item affects profit or loss. The ineffective portion is recognised immediately in profit or loss.

For the hedge of a forecast transaction that subsequently results in the recognition of a non-financial asset, the associated gains or losses that were previously recognised directly in equity removed from the equity and included in the initial cost of non-financial asset.

Derivatives that do not qualify to hedge accounting

Derivatives that do not qualify for hedge accounting are deemed as financial assets held for trading or financial liabilities held for trading. Changes in fair values of such derivatives are recognised directly in profit and loss.

**Derecognition**

Financial assets are derecognised when the rights to receive cash flows from the assets expire or, the financial assets are transferred and the Group has transferred substantially all the risks and rewards of ownership of the financial assets. On derecognition of a financial asset, the difference between the asset's carrying amount and the sum of the consideration received and the cumulative gain or loss that had been recognised directly in equity is recognised in profit or loss.

For financial liabilities, they are removed from the Group's balance sheet (i.e. when the obligation specified in the relevant contract is discharged, cancelled or expired). The difference between the carrying amount of the financial liability derecognised and the consideration received or receivable is recognised in profit or loss.

## 4. SIGNIFICANT ACCOUNTING POLICIES *(cont'd)*

**Equity-settled share-based payment transactions**

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

At the time 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 profits.

**Impairment losses**

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. An impairment loss is 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, such 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.

## 5. KEY SOURCES OF ESTIMATION UNCERTAINTY

The key assumptions concerning the future, and other key sources of estimation uncertainty at the balance sheet date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year, are also discussed below.

**Allowances for bad and doubtful debts**

The policy for allowance of bad and doubtful debts of the Group is based on the evaluation of collectability and aging analysis of accounts and on management's judgment. A considerable amount of judgment is required in assessing the ultimate realisation of these receivables, including the current creditworthiness and the past collection history of each customer. 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.

**Allowances for inventories**

The management of the Group reviews an aging analysis at each balance sheet date, and makes allowance for obsolete and slow-moving inventory items identified that are no longer suitable for use in production. The management estimates the net realisable value for such finished goods and work in progress based primarily on the latest invoice prices and current market conditions. The Group carries out an inventory review on a product-by-product basis at each balance sheet date and makes allowance for obsolete items.

## 6. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

The Group's major financial instruments include trade and bills receivable, other receivables, bank balances, trade payables, bills payable, other payables and accruals and bank borrowings. Details of these financial instruments are disclosed in respective notes. The risks associated with these financial instruments and 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.

**Currency risk**

Several subsidiaries of the Company have foreign currency sales and purchases. Certain bank balances including approximately HK$66,137,000 (2004: HK$64,423,000), HK$14,476,000 (2004: HK$5,460,000), HK$2,502,000 (2004: HK$202,000) were denominated in United States Dollars, British Pounds and Euro Dollars which were derived from foreign currency sales.

In order to mitigate the foreign currency risk, foreign currency forward contracts are entered into in respect of highly probable foreign currency purchases in accordance with the Group's risk management policies. For foreign currency sales, the Group currently does not have a hedging policy but will consider hedging should the need arise.

**Interest rate risk**

The Group is exposed to cash flow interest rate risk through the impact of rate changes on it's variable interest rate bank borrowings. The interest rates and terms of repayment of bank borrowings of the Group are disclosed in note 31.

The Group manages its interest rate exposure based on the interest rate level and outlook as well as potential impact on the Group's financial position arising from volatility.

**Credit risk**

The Group's maximum exposure to credit risk in the event of the counterparties failure to perform their obligations as at 31 December 2005 in relation to each class of recognised financial assets is the carrying amount of those assets as stated in the consolidated balance sheet. In order to minimise the credit risk, the management of the Group has delegated a team responsible for determination of credit limits, 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 trade debt at each balance sheet date to ensure that adequate impairment losses are made for irrecoverable amounts. In this regard, the directors of the Company consider that the Group's credit risk is significantly reduced.

The Group's bank balances are deposited with banks of high credit rating and the Group has limited exposure to any single financial institution.

The Group has no significant concentration of credit risk, with exposure spread over a number of counterparties and customers.

## 7. TURNOVER

Turnover represents the amount received and receivable for goods sold by the Group, less returns and allowances. An analysis of the Group's turnover is as follows:

| | 2005<br>HK$'000 | 2004<br>HK$'000 |
|---|---|---|
| Manufacture and trading of garments | **1,856,872** | 1,769,026 |
| Retailing of garments | **251,625** | 194,992 |
| | **2,108,497** | 1,964,018 |

## 8. BUSINESS AND GEOGRAPHICAL SEGMENTS

**(a) Business segments**

For management purposes, the Group is currently organised into two operating divisions – (i) manufacture and trading of garments and (ii) retailing of garments. These divisions are the basis on which the Group reports its primary segment information.

*Income statement for the year ended 31 December 2005*

| | Manufacture and trading of garments<br>HK$'000 | Retailing of garments<br>HK$'000 | Consolidated<br>HK$'000 |
|---|---|---|---|
| TURNOVER | | | |
| External sales | 1,849,957 | 258,540 | 2,108,497 |
| Inter-segment sales | 6,915 | (6,915) | – |
| Total | 1,856,872 | 251,625 | 2,108,497 |
| RESULT | | | |
| Segment result | 76,425 | 593 | 77,018 |
| Other income | 1,870 | 214 | 2,084 |
| | 78,295 | 807 | 79,102 |
| Increase in fair value of investment properties | | | 22,400 |
| Finance costs | | | (26,041) |
| Share of results of jointly controlled entities | | | 1,153 |
| Profit before taxation | | | 76,614 |
| Taxation | | | (9,181) |
| Profit for the year | | | 67,433 |

*Note:* The inter-segment sales were made according to the published prices and conditions offered to major customers of the Group, except that a longer credit period was usually granted.

## 8. BUSINESS AND GEOGRAPHICAL SEGMENTS *(cont'd)*

### (a) Business segments *(cont'd)*

*Balance sheet as at 31 December 2005*

| | Manufacture and trading of garments HK$'000 | Retailing of garments HK$'000 | Consolidated HK$'000 |
|---|---|---|---|
| ASSETS | | | |
| Segment assets | 1,209,917 | 139,313 | 1,349,230 |
| Unallocated corporate assets | | | 81,907 |
| Consolidated total assets | | | 1,431,137 |
| LIABILITIES | | | |
| Segment liabilities | 300,374 | 42,524 | 342,898 |
| Unallocated corporate liabilities | | | 382,097 |
| Consolidated total liabilities | | | 724,995 |

*Other information for the year ended 31 December 2005*

| | Manufacture and trading of garments HK$'000 | Retailing of garments HK$'000 | Consolidated HK$'000 |
|---|---|---|---|
| Additions to property, plant and equipment | 61,730 | 15,256 | 76,986 |
| Depreciation of property, plant and equipment | 47,790 | 10,577 | 58,367 |
| Impairment loss recognised in respect of property, plant and equipment | 747 | – | 747 |
| Gain on disposal of property, plant and equipment | 1,573 | 1,055 | 2,628 |
| Amortisation of trademarks | 692 | – | 692 |
| Allowance for bad and doubtful debts | 2,261 | 413 | 2,674 |
| (Write back) allowance for inventory obsolescence* | 28 | (894) | (866) |

* Obsolete inventory allowance write back when the relevant inventory was sold.

## 8. BUSINESS AND GEOGRAPHICAL SEGMENTS *(cont'd)*

### (a) Business segments *(cont'd)*

*Income statement for the year ended 31 December 2004*

| | Manufacture and trading of garments HK$'000 | Retailing of garments HK$'000 | Consolidated HK$'000 (restated) |
|---|---|---|---|
| TURNOVER | | | |
| External sales | 1,762,753 | 201,265 | 1,964,018 |
| Inter-segment sales | 6,273 | (6,273) | – |
| Total | 1,769,026 | 194,992 | 1,964,018 |
| RESULT | | | |
| Segment result | 79,391 | (7,128) | 72,263 |
| Other income | 2,104 | 63 | 2,167 |
| | 81,495 | (7,065) | 74,430 |
| Finance costs | | | (24,360) |
| Share of results of jointly controlled entities | | | 1,239 |
| Profit before taxation | | | 51,309 |
| Taxation | | | (5,461) |
| Profit for the year | | | 45,848 |

## 8. BUSINESS AND GEOGRAPHICAL SEGMENTS *(cont'd)*

### (a) Business segments *(cont'd)*

*Balance sheet as at 31 December 2004*

| | Manufacture and trading of garments HK$'000 | Retailing of garments HK$'000 | Consolidated HK$'000 |
|---|---|---|---|
| ASSETS | | | |
| Segment assets | 1,295,010 | 179,126 | 1,474,136 |
| Unallocated corporate assets | | | 6,435 |
| Consolidated total assets | | | 1,480,571 |
| LIABILITIES | | | |
| Segment liabilities | 280,997 | 38,003 | 319,000 |
| Unallocated corporate liabilities | | | 510,233 |
| Consolidated total liabilities | | | 829,233 |

*Other information for the year ended 31 December 2004*

| | Manufacture and trading of garments HK$'000 (restated) | Retailing of garments HK$'000 | Consolidated HK$'000 (restated) |
|---|---|---|---|
| Additions to property, plant and equipment | 80,577 | 18,399 | 98,976 |
| Depreciation of property, plant and equipment | 36,596 | 6,003 | 42,599 |
| Impairment loss recognised in respect of property, plant and equipment | – | 2,860 | 2,860 |
| Loss on disposal of property, plant and equipment | 1,503 | 687 | 2,190 |
| Amortisation of trademarks | 692 | – | 692 |
| Allowance for bad and doubtful debts | 5,938 | – | 5,938 |
| Allowance for inventory obsolescence | – | 2,943 | 2,943 |

## 8. BUSINESS AND GEOGRAPHICAL SEGMENTS *(cont'd)*

### (b) Geographical segments

The Group's operations are located in Untied States of America ("USA"), Europe, Greater China and other areas.

The following table provides an analysis of the Group's sale by geographical market, irrespective of the origin of the goods:

| | **Sales revenue by geographical market** | |
|---|---|---|
| | **2005** | 2004 |
| | **HK$'000** | HK$'000 |
| USA | **1,431,675** | 1,329,009 |
| Europe | **298,100** | 250,857 |
| Greater China | **348,875** | 364,484 |
| Others | **29,847** | 19,668 |
| | **2,108,497** | 1,964,018 |

The following is an analysis of the carrying amount of segment assets, and additions to property, plant and equipment, analysed by geographical area in which the assets are located:

| | **Carrying amount of segment assets** | | **Additions to property, plant and equipment** | |
|---|---|---|---|---|
| | **2005** | 2004 | **2005** | 2004 |
| | **HK$'000** | HK$'000 | **HK$'000** | HK$'000 |
| | | | | (restated) |
| USA | **160,348** | 140,783 | **1,063** | 375 |
| Europe | **11,430** | 18,061 | **685** | 862 |
| Greater China | **1,254,140** | 1,318,846 | **74,985** | 97,733 |
| Others | **2,682** | 2,000 | **253** | 6 |
| | **1,428,600** | 1,479,690 | **76,986** | 98,976 |

## 9. FINANCE COSTS

| | 2005 HK$'000 | 2004 HK$'000 |
|---|---|---|
| Interest on: | | |
| Bank loans, overdrafts and other borrowings wholly repayable within five years | **17,173** | 13,835 |
| Finance leases | **33** | 11 |
| Factoring expenses | **2,982** | 3,635 |
| Bank charges | **5,853** | 6,879 |
| | **26,041** | 24,360 |

## 10. DIRECTORS' REMUNERATION

The emoluments paid or payable to each of nine (2004: nine) directors were as follows:

| | | Other emoluments | | | |
|---|---|---|---|---|---|
| | Fees | Salaries and other benefits | Retirement benefits scheme contributions | Performance related incentive payments | Total emoluments |
| | HK$'000 | HK$'000 | HK$'000 | HK$'000 | HK$'000 |
| Lam Foo Wah | 80 | 5,070 | 12 | 1,000 | 6,162 |
| Hui Yip Wing | 80 | 2,567 | 12 | – | 2,659 |
| Wong Shing Loong, Raymond | 80 | 1,885 | 12 | 400 | 2,377 |
| So Siu Hang, Patricia | 80 | 1,950 | 12 | 1,000 | 3,042 |
| Ip Weng Kun | 80 | 2,220 | 11 | – | 2,311 |
| Chan Wah Tip, Michael | 80 | – | – | – | 80 |
| Wong Shiu Hoi, Peter | 160 | – | – | – | 160 |
| Leung Hok Lim | 80 | – | – | – | 80 |
| Woo King Wai | 80 | – | – | – | 80 |
| **Total for 2005** | **800** | **13,692** | **59** | **2,400** | **16,951** |

## 10. DIRECTORS' REMUNERATION *(cont'd)*

| | | Other emoluments | | | |
|---|---|---|---|---|---|
| | Fees | Salaries and other benefits | Retirement benefits scheme contributions | Performance related incentive payments | Total emoluments |
| | HK$'000 | HK$'000 | HK$'000 | HK$'000 | HK$'000 |
| Lam Foo Wah | 80 | 5,070 | 12 | 600 | 5,762 |
| Hui Yip Wing | 80 | – | – | – | 80 |
| Wong Shing Loong, Raymond | 80 | 1,885 | 12 | 220 | 2,197 |
| So Siu Hang, Patricia | 80 | 1,950 | 12 | 230 | 2,272 |
| Ip Weng Kun | 80 | 2,405 | 12 | 280 | 2,777 |
| Chan Wah Tip, Michael | 80 | – | – | – | 80 |
| Wong Shiu Hoi, Peter | 36 | – | – | – | 36 |
| Leung Hok Lim | 13 | – | – | – | 13 |
| Woo King Wai | 80 | – | – | – | 80 |
| Total for 2004 | 609 | 11,310 | 48 | 1,330 | 13,297 |

During both years, no emoluments were paid by the Group to the directors as compensation for loss of office or an inducement to join or upon joining the Group. None of the directors has waived any emoluments in both years.

## 11. EMPLOYEE'S EMOLUMENTS

The five highest paid individuals in the Group in 2005 are all directors of the Company and details of their emoluments are included in note 10 above.

In 2004, of the five individuals with the highest emoluments in the Group, four were directors of the Company whose emoluments are included in the disclosures in note 10 above. The salaries and other benefits, and contributions to retirement benefits scheme of the remaining one individual amounted to HK$1,890,000 and HK$12,000 respectively.

## 12. TAXATION

| | **2005** | 2004 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| | | (restated) |
| Current tax charge: | | |
| Hong Kong | **1,386** | 980 |
| Other jurisdictions | **8,315** | 7,010 |
| Overprovision in prior years: | | |
| Hong Kong | **(663)** | (3,417) |
| Other jurisdictions | **(1,336)** | – |
| | **7,702** | 4,573 |
| Deferred taxation *(note 32)* | **1,479** | 888 |
| | **9,181** | 5,461 |

The Hong Kong Inland Revenue Department ("IRD") recently initiated a tax audit on certain group companies for the years of assessment from 1999/2000 to 2004/2005. As a matter of IRD's practice, the IRD has issued assessments to these group companies for the year of assessment 1999/2000 (which would be statutorily time – barred after 31 March 2006) and, during the course of the audit, there may be a possibility that assessments for subsequent years be issued by the IRD to these group companies.

Since the tax audit is still at a preliminary fact-finding stage with different views being exchanged with the IRD, the outcome of the tax audit cannot be readily ascertained with any degree of accuracy. For Hong Kong tax provision purpose, the management has in the current year followed the same basis for making provision as adopted in prior years. In the opinion of the management, the provisions so made are adequate for the purpose mentioned above.

Hong Kong Profits Tax is calculated at 17.5% of the estimated assessable profit for both years. Taxation arising in other jurisdictions is calculated at the rates prevailing in the relevant jurisdictions.

In accordance with the relevant tax rules and regulations in the PRC, certain of the Company's PRC subsidiaries enjoy income tax exemptions and reductions. Certain PRC subsidiaries are subject to income taxes at tax rates ranging from 12% to 33%.

## 12. TAXATION *(cont'd)*

The taxation for the year can be reconciled to the profit before taxation per the consolidated income statement as follows:

| | 2005 HK$'000 | 2004 HK$'000 (restated) |
|---|---|---|
| Profit before taxation | **76,614** | 51,309 |
| Tax at the income tax rate of 17.5% | **13,407** | 8,979 |
| Effect of different tax rates of subsidiaries operating in other jurisdictions | **876** | 1,213 |
| Tax effect of share of results of jointly controlled entities | **(202)** | (217) |
| Tax effect of income not taxable for tax purpose | **(12,830)** | (14,262) |
| Tax effect of expenses not deductible for tax purpose | **2,110** | 4,917 |
| Tax effect of tax losses not recognised | **12,266** | 12,356 |
| Utilisation of tax losses previously not recognised | **(4,447)** | (4,108) |
| Overprovision in prior years | **(1,999)** | (3,417) |
| Taxation for the year | **9,181** | 5,461 |

## 13. PROFIT FOR THE YEAR

Profit for the year has been arrived at after charging (crediting):

| | 2005 HK$'000 | 2004 HK$'000 (restated) |
|---|---|---|
| Cost of inventories recognised as expenses | 1,507,171 | 1,405,474 |
| Depreciation and amortisation | | |
| Owned assets | 57,976 | 42,221 |
| Leased assets | 391 | 378 |
| Amortisation of intangible assets (included in selling and distribution expenses) | 692 | 692 |
| Amortisation of prepaid lease payments | 1,327 | 1,528 |
| | 60,386 | 44,819 |
| Allowance for bad and doubtful debts (included in selling and distribution cost) | 2,674 | 5,938 |
| (Write back) allowance for inventory obsolescence* (included in cost of sales) | (866) | 2,943 |
| Auditors' remuneration | 3,274 | 2,859 |
| Operating lease rentals in respect of equipment | 65 | 221 |
| Minimum lease payments in respect of land and buildings | 68,114 | 59,676 |
| Staff costs (including directors' remuneration - note 10) | | |
| Wages, salaries and bonuses | 292,785 | 267,853 |
| Retirement benefits contributions | 5,647 | 3,365 |
| *Less:* Forfeited contributions | (85) | (69) |
| | 5,562 | 3,296 |
| | 298,347 | 271,149 |
| Net foreign exchange loss (gain) | 4,232 | (4,601) |
| Temporary textile quota expenses | 3,779 | 2,112 |
| (Gain) loss on disposal of property, plant and equipment | (2,628) | 2,190 |
| Gain on disposal of available-for-sale investments | (642) | – |
| Gain on financial derivatives | (23,445) | (1,664) |
| Gross rental income from investment properties | (8,201) | (4,675) |
| *Less:* Outgoings for investment properties rented out | 1,485 | 1,369 |
| Net rental income | (6,716) | (3,306) |
| Sub-letting rental income (included in selling and distribution expenses) | (3,339) | (3,337) |
| Interest income | (3,155) | (2,167) |
| Share of tax of jointly controlled entities (included in share of results of jointly controlled entities) | 247 | 202 |

* Allowance for obsolete inventory is reversed when the relevant inventory was sold.

## 14. DIVIDENDS

| | 2005 HK$'000 | 2004 HK$'000 |
|---|---|---|
| Additional final dividend paid for 2003 arising from shares issued under option scheme | – | 34 |
| Interim, paid – HK3 cents per ordinary share (2004: HK3 cents) | 9,995 | 9,881 |
| Proposed final – HK5 cents per ordinary share (2004: HK5 cents) | 16,658 | 16,658 |
| | 26,653 | 26,573 |
| Dividends paid | 26,653 | 19,703 |

The final dividend of HK5 cents (2004: HK5 cents) per share has been proposed by the directors and is subject to the approval by the Company's shareholders at the forthcoming annual general meeting.

## 15. EARNINGS PER SHARE

The basic and diluted earnings per share for the year ended 31 December 2005 together with the comparative figures for 2004 are calculated as follows:

| | 2005 HK$'000 | 2004 HK$'000 |
|---|---|---|
| Profit for the purpose of basic and diluted earnings per share | 67,433 | 72,400 |
| | Number | Number |
| Weighted average number of ordinary shares for the purpose of basic earnings per share | 332,318,673 | 328,635,730 |
| Effect of dilutive potential ordinary shares assuming exercise of share options | 3,426,494 | 6,069,967 |
| Weighted average number of ordinary shares for the purpose of diluted earnings per share | 335,745,167 | 334,705,697 |

The following table summarise the impact on both basic and diluted earnings per share for both years as a result of application of New HKFRSs:

| | Impact on basic earnings per share | | Impact on diluted earnings per share | |
|---|---|---|---|---|
| | 2005 cents | 2004 cents | 2005 cents | 2004 cents |
| Figures before adjustments | 15.1 | 22.0 | 14.9 | 21.6 |
| Adjustments arising from changes in accounting policies *(see note 3)* | 5.2 | – | 5.2 | – |
| | 20.3 | 22.0 | 20.1 | 21.6 |

## 16. PROPERTY, PLANT AND EQUIPMENT

| | Buildings (Hong Kong) HK$'000 | Buildings (elsewhere) HK$'000 | Construction in progress HK$'000 | Leasehold improvements HK$'000 | Plant and equipment HK$'000 | Furniture and fixtures HK$'000 | Motor vehicles HK$'000 | Total HK$'000 |
|---|---|---|---|---|---|---|---|---|
| COST | | | | | | | | |
| At 1 January 2004 | | | | | | | | |
| – As originally stated | 33,401 | 218,145 | 11,123 | 30,246 | 219,087 | 70,421 | 22,017 | 604,440 |
| – Reclassified to prepaid lease payments | (8,897) | (42,167) | – | – | – | – | – | (51,064) |
| – As restated | 24,504 | 175,978 | 11,123 | 30,246 | 219,087 | 70,421 | 22,017 | 553,376 |
| Additions | – | 11,412 | 39,954 | 15,943 | 18,949 | 8,231 | 4,487 | 98,976 |
| Transfers | – | 13,196 | (41,464) | – | 28,268 | – | – | – |
| Transfer to investment properties *(note 18)* | (4,604) | – | – | – | – | – | – | (4,604) |
| Disposals | – | (6,136) | – | (5,430) | (25,284) | (13,082) | (3,811) | (53,743) |
| Exchange realignment | – | – | – | 975 | 648 | 105 | 186 | 1,914 |
| At 31 December 2004 | 19,900 | 194,450 | 9,613 | 41,734 | 241,668 | 65,675 | 22,879 | 595,919 |
| Additions | – | 7,313 | 32,742 | 2,310 | 11,301 | 18,695 | 4,625 | 76,986 |
| Transfers | – | 9,002 | (36,253) | (17,932) | 25,484 | 19,084 | 615 | – |
| Disposals | – | (9,340) | – | (72) | (4,440) | (7,609) | (2,243) | (23,704) |
| Exchange realignment | – | 4,432 | 136 | (195) | 3,505 | (1) | 60 | 7,937 |
| **At 31 December 2005** | **19,900** | **205,857** | **6,238** | **25,845** | **277,518** | **95,844** | **25,936** | **657,138** |
| ACCUMULATED DEPRECIATION AND IMPAIRMENT | | | | | | | | |
| At 1 January 2004 | | | | | | | | |
| – As originally stated | 5,386 | 31,345 | – | 16,397 | 110,630 | 54,997 | 15,456 | 234,211 |
| – Reclassified to prepaid lease payments | (946) | (3,236) | – | – | – | – | – | (4,182) |
| – As restated | 4,440 | 28,109 | – | 16,397 | 110,630 | 54,997 | 15,456 | 230,029 |
| Provided for the year | 453 | 6,304 | – | 7,755 | 21,586 | 4,257 | 2,244 | 42,599 |
| Transfer to investment properties *(note 18)* | (357) | – | – | – | – | – | – | (357) |
| Impairment loss recognised in the income statement | – | – | – | – | 1,000 | 1,860 | – | 2,860 |
| Eliminated on disposals | – | (1,133) | – | (4,722) | (15,468) | (10,967) | (3,299) | (35,589) |
| Exchange realignment | – | – | – | 692 | 593 | 33 | 115 | 1,433 |
| At 31 December 2004 | 4,536 | 33,280 | – | 20,122 | 118,341 | 50,180 | 14,516 | 240,975 |
| Provided for the year | 398 | 7,083 | – | 6,670 | 27,382 | 13,875 | 2,959 | 58,367 |
| Impairment loss recognised in the income statement | – | 747 | – | – | – | – | – | 747 |
| Eliminated on disposals | – | (5,153) | – | (71) | (2,705) | (6,630) | (1,650) | (16,209) |
| Transfers | – | 216 | – | (9,925) | (984) | 10,693 | – | – |
| Exchange realignment | – | 639 | – | (7) | 1,279 | (9) | 29 | 1,931 |
| **At 31 December 2005** | **4,934** | **36,812** | **–** | **16,789** | **143,313** | **68,109** | **15,854** | **285,811** |
| NET BOOK VALUES | | | | | | | | |
| **At 31 December 2005** | **14,966** | **169,045** | **6,238** | **9,056** | **134,205** | **27,735** | **10,082** | **371,327** |
| At 31 December 2004 | 15,364 | 161,170 | 9,613 | 21,612 | 123,327 | 15,495 | 8,363 | 354,944 |

## 16. PROPERTY, PLANT AND EQUIPMENT *(cont'd)*

Included in buildings (elsewhere) were properties in the PRC with an aggregate amount of HK$4,500,000 (2004: HK$5,391,000), the title of which has been kept by the court in the PRC to secure the Group's application on the freeze of assets of its agent to recover the amount owed by the agent to the Group.

| | **2005** | 2004 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| Buildings in Hong Kong: | | |
| Medium term leases | **14,966** | 15,364 |
| Buildings outside Hong Kong: | | |
| Long term leases | **–** | 1,999 |
| Medium term leases | **169,045** | 159,171 |
| | **184,011** | 176,534 |

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

| | |
|---|---|
| Buildings | 2% to 5% |
| Leasehold improvements | Over the lease terms |
| Plant and equipment | 9% to 20% |
| Furniture and fixtures | 9% to 25% |
| Motor vehicles | 9% to 25% |

The net book value of the motor vehicles includes an amount of HK$811,000 (2004: HK$910,000) in respect of assets held under finance leases.

During the year, the directors have reassessed the recoverable amount of the medium-term leasehold buildings situated outside Hong Kong and recognised an impairment loss of approximately HK$747,000 with reference to the market price.

## 17. PREPAID LEASE PAYMENTS

| | 2005<br>HK$'000 | 2004<br>HK$'000 |
|---|---|---|
| The Group's prepaid lease payments comprise: | | |
| Medium-term leasehold land in Hong Kong | **6,169** | 6,207 |
| Medium-term leasehold land outside Hong Kong | **40,115** | 38,721 |
| | **46,284** | 44,928 |
| Analysed for reporting purposes as: | | |
| Non-current asset | **44,957** | 43,538 |
| Current asset | **1,327** | 1,390 |
| | **46,284** | 44,928 |

## 18. INVESTMENT PROPERTIES

| | HK$'000 |
|---|---|
| FAIR VALUE | |
| At 1 January 2004 | 34,500 |
| Transfers from property, plant and equipment at carrying amount | 4,247 |
| Transfers from prepaid lease payments | 1,576 |
| Revaluation surplus recognised in equity | 1,277 |
| At 31 December 2004 | 41,600 |
| Increase in fair value recognised in the income statement | 22,400 |
| **At 31 December 2005** | **64,000** |

The fair value of the Group's investment properties at 31 December 2005 have been arrived at on the basis of a valuation carried out on that date by Centaline Surveyors Ltd., independent qualified professional valuers not connected with the Group. Centaline Surveyors Ltd. are members of the Institute of Valuers, and have appropriate qualifications and recent experiences in the valuation of similar properties in the relevant locations. The valuation, which conforms to International Valuation Standards, was arrived at by reference to market evidence of transaction prices for similar properties.

All of the Group's property interests held under operating leases to earn rentals or for capital appreciation purposes are measured using the fair value model and are classified and accounted for as investment properties. As at 31 December 2005, the carrying amount of such property interests amounted to HK$64,000,000 (31 December 2004: HK$41,600,000).

The Group's investment properties are situated in Hong Kong and are held under medium-term leases.

## 19. INTANGIBLE ASSETS

| | Trade marks |
|---|---|
| | HK$'000 |
| COST | |
| At 1 January 2004, 31 December 2004, 1 January 2005 and 31 December 2005 | 6,917 |
| ACCUMULATED AMORTISATION | |
| At 1 January 2004 | 1,556 |
| Provided for the year | 692 |
| At 31 December 2004 | 2,248 |
| Provided for the year | 692 |
| At 31 December 2005 | 2,940 |
| NET BOOK VALUES | |
| **At 31 December 2005** | **3,977** |
| At 31 December 2004 | 4,669 |

The amount is amortised over 10 years.

## 20. INTERESTS IN ASSOCIATES

| | 2005 | 2004 |
|---|---|---|
| | HK$'000 | HK$'000 |
| Cost of investment in associates, unlisted | **2,000** | 2,000 |
| Share of post acquisition losses | **(2,000)** | (2,000) |
| | **–** | – |

The amount due to an associate is unsecured, interest-free and is repayable on demand.

The directors consider the carrying amounts approximate to their fair values.

## 20. INTERESTS IN ASSOCIATES *(cont'd)*

Details of the Group's associates at 31 December 2005 are set out as follows:

| Name of entity | Form of business structure | Place of incorporation or registration/ operation | Proportion of nominal value of issued share capital/ registered capital held by the Group | Principal activities |
|---|---|---|---|---|
| | | | % | |
| Sherman-Theme (China) Limited | Incorporated | Hong Kong | 37.5 | Investment holding |
| Shenyang Sherman–Theme Fashion Limited | Incorporated | PRC | 22.5 | Inactive |

The summarised financial information in respect of the Group's associates is set out below:

| | **2005** | 2004 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| Total assets | **–** | – |
| Total liabilities | **(1,569)** | (1,566) |
| Net liabilities | **(1,569)** | (1,566) |
| Group's share of net assets of associates | **–** | – |
| Revenue | **–** | – |
| Loss for the year | **(3)** | (3) |
| Group's share of associates for the year | **–** | – |

The Group has discontinued recognition of its share of losses of certain associates. The amounts of unrecognised share of those associates, extracted from the relevant audited financial statements of associates, both for the year and cumulatively, are as follows:

| | **2005** | 2004 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| Unrecognised share of losses of associates for the year | **1** | 1 |
| Accumulated unrecognised share of losses of associates | **1,404** | 1,403 |

## 21. INTERESTS IN JOINTLY CONTROLLED ENTITIES

| | 2005 HK$'000 | 2004 HK$'000 |
|---|---|---|
| Cost of unlisted investments in jointly controlled entity | **9,467** | 6,486 |
| Share of post-acquisition profits | **5,228** | 4,075 |
| | **14,695** | 10,561 |

The amounts due to jointly controlled entities aged within 90 days.

The amounts due from and to jointly controlled entities are unsecured, interest-free and is repayable on demand.

The directors consider the carrying amounts approximate to their fair values.

At 31 December 2005, the Group had interests in the following jointly controlled entities:

| Name | Form of business structure | Place of registration and operations | Percentage of Ownership interest % | Percentage of Voting power % | Percentage of Profit sharing % | Principal activities |
|---|---|---|---|---|---|---|
| Hangzhou Dalifu Silk Finishing Co., Ltd. | Incorporated | PRC | 51 | 50 | 51 | Dyeing, printing and sandwashing of fabrics |
| Suzhou High Fashion Garment Co., Ltd. ("Suzhou High Fashion") | Incorporated | PRC | 51 | 60 *(Note)* | 51 | Garment manufacturing |

*Note:* The Group holds 51% of the registered capital of Suzhou High Fashion. However, under the terms of memorandum and articles of association of Suzhou High Fashion, all significant events must be mutually agreed by the Group and the other significant shareholder. Therefore, Suzhou High is classified as a jointly controlled entity of the Group.

## 21. INTERESTS IN JOINTLY CONTROLLED ENTITIES *(cont'd)*

The summarised financial information in respect of the Group's jointly controlled entities which are accounted for using the equity method is set out below:

| | **2005** | 2004 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| Current assets | **29,126** | 24,240 |
| Non-current assets | **20,966** | 19,000 |
| Current liabilities | **21,278** | 22,532 |
| Group's share of net assets of jointly controlled entities | **14,695** | 10,561 |
| Income | **65,617** | 84,261 |
| Expenses | **63,356** | 81,674 |
| Group's share of results of jointly controlled entities for the year | **1,153** | 1,239 |

## 22. AVAILABLE-FOR-SALE INVESTMENTS

Available-for-sale investments as at 31 December 2005 comprises:

| | HK$'000 |
|---|---|
| Unlisted securities: | |
| – equity securities | 1,000 |
| *Less:* Impairment loss recognised | (325) |
| | 675 |

The above unlisted investments represent investments in unlisted equity securities issued by a private entity incorporated in the British Virgin Islands ("BVI"). They are measured at cost less impairment at each balance sheet date because the range of reasonable fair value estimates is so significant that the directors of the Company are of the opinion that their fair values cannot be measured reliably.

The directors reviewed the carrying value of the available-for-sale investments by reference to the carrying amount of net assets of the relevant audited financial statements of the investee and considered that no additional impairment loss is required.

## 23. INVESTMENTS IN SECURITIES

Investment securities as at 31 December 2004 comprises:

| | HK$'000 |
|---|---|
| Unlisted equity investments, at cost | 14,118 |
| *Less:* Impairment loss recognised | (325) |
| | 13,793 |

Upon the application of HKAS 39 on 1 January 2005, investment securities were reclassified to available-for-sale investments under HKAS 39 (see note 3 for details).

## 24. INVENTORIES

| | **2005** | 2004 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| Raw materials | **101,602** | 118,384 |
| Work in progress | **128,654** | 83,874 |
| Finished goods | **102,795** | 126,528 |
| | **333,051** | 328,786 |

Included above are raw materials of approximately HK$12,394,000 (2004: HK$42,745,000) and finished goods of approximately HK$57,885,000 (2004: HK$71,562,000) which are carried at net realisable value.

## 25. TRADE RECEIVABLES

The credit terms granted by the Group to its customers normally range from 30 days to 90 days.

The aged analysis of the Group's trade receivables at the balance sheet date is as follows:

| | **2005** | 2004 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| Within 90 days | **248,232** | 234,313 |
| 91 to 180 days | **14,014** | 7,993 |
| 181 to 360 days | **4,824** | 5,645 |
| Over 360 days | **5,681** | 3,218 |
| | **272,751** | 251,169 |

The directors consider that the carrying amounts of trade receivables approximate to their fair values.

## 26. OTHER CURRENT FINANCIAL ASSETS AND FINANCIAL LIABILITIES

All bills receivable and bills payable are aged within 90 days.

Bank deposits are short term highly liquid investments carrying interest at market rate which are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value, and have a short maturity of generally within three months when acquired.

The directors consider that the carrying amounts of the other current financial assets and other current liabilities approximate to their fair values.

## 27. DERIVATIVES

| | **2005**<br>**HK$'000** |
|---|---|
| Cash flow hedges – Foreign currency forward contracts | **4,000** |

Cash flow hedges:
The aggregate notional amount of the outstanding forward contracts at 31 December 2005 was HK$465 million for Renminbi at exchange rates ranging from RMB1.0289 to RMB1.05 against HK$1 and the maturity periods were within one year. They are designated as highly effective hedging instruments in order to manage the Group's foreign currency exposure in relation to foreign currency forecast purchases.

As at 31 December 2005, a fair value gain of HK$4,000,000 has been deferred in equity and is expected to be released to the income statement at various dates in the coming year after the balance sheet date, the period in which the inventories are recognised as expenses.

The terms of the foreign exchange contracts have been negotiated to match the terms of the forecast purchases.

The derivatives are measured at fair value at 31 December 2005. The fair values are determined based on the quoted prices provided by financial institutions.

## 28. CERTIFICATE OF DEPOSITS

| | 2005 HK$'000 | 2004 HK$'000 |
|---|---|---|
| Unlisted certificate of deposits, at market value | – | 10,000 |

## 29. TRADE PAYABLES

The following is an aged analysis of the trade payables at the reporting date:

| | 2005 HK$'000 | 2004 HK$'000 |
|---|---|---|
| Trade payables: | | |
| Within 90 days | 126,471 | 156,408 |
| 91 to 180 days | 4,973 | 17,141 |
| 181 to 360 days | 6,807 | 13,009 |
| Over 360 days | 10,331 | 11,113 |
| | 148,582 | 197,671 |
| Accrued purchases | 23,675 | 18,404 |
| | 172,257 | 216,075 |

The directors consider the carrying amounts approximate to their fair values.

## 30. OBLIGATIONS UNDER FINANCE LEASES

| | Minimum lease payments | | Present value of minimum lease payments | |
|---|---|---|---|---|
| | **2005** | 2004 | **2005** | 2004 |
| | **HK$'000** | HK$'000 | **HK$'000** | HK$'000 |
| Amounts payable under finance leases: | | | | |
| Within one year | **255** | 294 | **222** | 262 |
| In the second year | **305** | 205 | **290** | 191 |
| In the third to fifth years, inclusive | **–** | 71 | **–** | 71 |
| | **560** | 570 | **512** | 524 |
| *Less:* Future finance charges | **(48)** | (46) | **–** | – |
| Present value of lease obligations | **512** | 524 | **512** | 524 |
| *Less:* Amount due for settlement within 12 months (shown under current liabilities) | | | **(222)** | (262) |
| Amount due for settlement after 12 months (shown under non-current liabilities) | | | **290** | 262 |

The Group leases certain of its motor vehicles. The average lease term is one to three years. For the year ended 31 December 2005, the average effective borrowing rate was 8%. Interest rates are fixed at the contract date.

All leases are on a fixed repayment basis and no arrangements have been entered into for contingent rental payments.

## 31. BANK BORROWINGS

| | 2005 | 2004 |
|---|---|---|
| | HK$'000 | HK$'000 |
| Bank overdrafts | 1,393 | 3,160 |
| Trust receipt loans | 1,750 | 4,278 |
| Bank loans | 365,580 | 445,690 |
| | 368,723 | 453,128 |
| Analysed as: | | |
| Secured | 36,528 | – |
| Unsecured | 332,195 | 453,128 |
| | 368,723 | 453,128 |
| The maturity profile of the above borrowings is as follows: | | |
| On demand or within one year | 305,723 | 345,128 |
| More than one year, but not exceeding two years | 60,000 | 54,000 |
| More than two years, but not exceeding five years | 3,000 | 54,000 |
| | 368,723 | 453,128 |
| *Less:* Amounts due within one year shown under current liabilities | (305,723) | (345,128) |
| Amounts due after one year shown under non-current liabilities | 63,000 | 108,000 |

All the Group's borrowings are variable rate borrowings which carry interest at 3.56% to 7.75% (2004: 1.37% to 3.04%). Interest is repriced every six months.

The Group's borrowings amounting to approximately HK$217,269,000 (2004: HK$303,216,000), HK$16,346,000 (2004: HK$90,566,000), HK$134,235,000 (2004: HK$59,346,000) and HK$873,000 (2004: nil) were denominated in Hong Kong Dollars, Renminbi, United States Dollars and British Pounds respectively.

At 31 December 2005, certain bank loans were secured by bank deposits of HK$159,000 (2004: HK$5,554,000), bills receivable of HK$17,055,000 (2004: nil) and trade receivables of HK$98,185,000 (2004: HK$57,449,000).

## 32. DEFERRED TAXATION

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

| | Deferred tax assets | | | | | Deferred tax liabilities | | |
|---|---|---|---|---|---|---|---|---|
| | Unrealised profit arising on intra-group transactions | Bad and doubtful debts | Allowance on obsolete inventories | Unrealised exchange losses | Total | Accelerated tax depreciation | Revaluation of investment properties | Total |
| | HK$'000 | HK$'000 | HK$'000 | HK$'000 | HK$'000 | HK$'000 | HK$'000 | HK$'000 |
| At 1 January 2004, as originally stated | (1,769) | – | – | – | (1,769) | 2,012 | – | 2,012 |
| Effects of changes in accounting policies *(note 3)* | – | – | – | – | – | – | 588 | 588 |
| At 1 January 2004, as restated | (1,769) | – | – | – | (1,769) | 2,012 | 588 | 2,600 |
| Charge to income statement for the year | 888 | – | – | – | 888 | – | – | – |
| Charge to equity for the year | – | – | – | – | – | – | 224 | 224 |
| At 31 December 2004 and 1 January 2005 | (881) | – | – | – | (881) | 2,012 | 812 | 2,824 |
| Charge (credit) to income statement for the year | 188 | (91) | (870) | (938) | (1,711) | (730) | 3,920 | 3,190 |
| Exchange realignment | – | 3 | 25 | 27 | 55 | – | – | – |
| **At 31 December 2005** | **(693)** | **(88)** | **(845)** | **(911)** | **(2,537)** | **1,282** | **4,732** | **6,014** |

The ultimate realisation of these deferred tax assets depend principally on Taiwan segment achieving profitability and generating sufficient taxable profits to utilise the underlying deferred tax assets. Based on the taxable profit and loss projections of this business segment, it is probable that the Group can fully utilise the deferred tax assets recognised within the utilisation periods. It may be necessary for some or all of these deferred tax assets be reduced and charged to the income statement if there is a significant adverse change in the projected performance and resulting projected taxable profits of these businesses.

The Group has tax losses arising in Hong Kong of HK$825,138,000 (2004: HK$834,278,000) and tax losses arising in overseas of HK$226,130,000 (2004: HK$172,310,000) for offsetting against future taxable profits of the companies in which the losses arose. Deferred tax assets have not been recognised in respect of these losses as they have arisen in subsidiaries that have been loss-making for some time.

## 33. PROVISION FOR LONG SERVICE PAYMENTS

| | HK$'000 |
|---|---|
| At 1 January 2004 | 3,153 |
| Amount utilised during the year | (559) |
| At 31 December 2004 | 2,594 |
| Amount utilised during the year | (570) |
| **At 31 December 2005** | **2,024** |

The Group provides for the probable future long service payments expected to be made to employees under the Hong Kong Employment Ordinance. The provision represents management's best estimate of the probable future payments which have been earned by the employees from their service up to the Group to the balance sheet date.

## 34. SHARE CAPITAL

| | **Number of shares** '000 | **Amount** HK$'000 |
|---|---|---|
| Ordinary shares of HK$0.10 each | | |
| Authorised: | | |
| At 1 January 2004, 31 December 2004, 1 January 2005 and 31 December 2005 | 1,000,000 | 100,000 |
| Issued and fully paid: | | |
| At 1 January 2004 | 327,402 | 32,740 |
| Exercise of share options | 1,950 | 195 |
| At 31 December 2004 and 1 January 2005 | 329,352 | 32,935 |
| Exercise of share options *(Note)* | 3,800 | 380 |
| **At 31 December 2005** | **333,152** | **33,315** |

All the issued shares rank pari passu in all respects including all rights as to dividends, voting and return of capital.

*Note:* During the year, the subscription rights attaching to 3,800,000 share options were exercised at the subscription price of HK$0.505 per share, resulting in the issue of 3,800,000 shares of HK$0.10 each for a total cash consideration of approximately HK$1,919,000.

## 35. SHARE OPTION SCHEMES

### (A) Share option schemes of the Company

On 26 March 2002, the share option scheme adopted by the Company on 18 March 1994 (the "Old Scheme") was terminated and a new scheme (the "New Scheme") was adopted by the shareholders of the Company. As a result, the Company can no longer grant any further options under the Old Scheme. However, all options granted prior to the termination of the Old Scheme will remain in full force and effect. The purpose of the New Scheme is to enable the Company to grant options to eligible participants, thereby (a) providing alternative recognition of their contributions; (b) strengthening the relationship between the Group and its employees and executives; (c) attracting and retaining key employees and executives; and (d) motivating employees and executives. Eligible participants of the New Scheme include the directors and employees of the Group. Unless otherwise terminated or amended, the New Scheme will remain in force for 10 years from date of adoption.

Pursuant to the New Scheme, the total number of shares which may be issued upon exercise of all outstanding options granted and yet to be exercised under the New Scheme and options granted and yet to be exercised under any other schemes will not exceed 30% of the issued share capital of the Company from time to time. The maximum number of shares issuable under share options to each eligible participant within any 12-month period is limited to 1% of the Company's shares in issue at any time. The offer of a grant of share options may be accepted within 28 days from the date of the offer with no consideration being payable by the grantee. The exercise period of the share options granted is determinable by the directors, but no later than 10 years from the date of the offer. The subscription price for the shares in respect of which options are granted is determinable by the directors, but may not be less than the higher of (1) the closing price of the Company's shares as stated in the Stock Exchange's daily quotation sheet on the date of grant of the option; (2) the average closing price of the Company's shares as stated in the Stock Exchange's daily quotation sheets for the five trading days immediately preceding the date of grant of the option; and (3) the par value of the Company's shares.

Share options do not confer rights on the holders to dividends or to vote at shareholders' meetings.

At the balance sheet date, the Company had 2,140,000 share options outstanding, which represented approximately 0.6% of the Company's shares in issue as at that date. The exercise in full of the remaining share options would, under the present capital structure of the Company, result in the issue of 2,140,000 additional ordinary shares of the Company for a cash consideration of approximately HK$1,081,000 (before issue expenses).

## 35. SHARE OPTION SCHEMES *(cont'd)*

### (A) Share option schemes of the Company *(cont'd)*

The following share options were outstanding during the year:

| | | | Number of share options | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| Name or category of participant | Date of grant | Exercise price HK$ | At 1 January 2004 | Exercised during the year | Lapsed during the year | At 31 December 2004 and 1 January 2005 | Exercised during the year | Lapsed during the year | At 31 December 2005 |
| Directors | | | | | | | | | |
| Lam Foo Wah | 5 May 1999 | 0.505 | 3,800,000 | – | – | 3,800,000 | (3,800,000) | – | – |
| Ip Weng Kun | 5 May 1999 | 0.505 | 1,500,000 | – | – | 1,500,000 | – | (1,500,000) | – |
| So Siu Hang, Patricia | 5 May 1999 | 0.505 | 720,000 | – | – | 720,000 | – | – | 720,000 |
| Wong Shing Loong, Raymond | 5 May 1999 | 0.505 | 1,000,000 | – | – | 1,000,000 | – | – | 1,000,000 |
| Other employees | 5 May 1999 | 0.505 | 2,730,000 | (1,950,000) | (360,000) | 420,000 | – | – | 420,000 |
| | | | 9,750,000 | (1,950,000) | (360,000) | 7,440,000 | (3,800,000) | (1,500,000) | 2,140,000 |

*Notes:*

(1) 40% of the options granted are exercisable during the period from 5 May 2002 to 4 May 2009, 30% of the options granted are exercisable during the period from 5 May 2003 to 4 May 2009 and the remaining 30% of the options granted are exercisable during the period from 5 May 2004 to 4 May 2009.

(2) Ip Weng Kun resigned as director on 30 December 2005.

(3) The weighted average closing price of the Company's shares immediately before the dates of which the options were exercised was HK$1.58 (2004: HK$1.18).

(4) All options are vested on the first day of respective exercisable period.

## 35. SHARE OPTION SCHEMES *(cont'd)*

### (B) Share option scheme of Theme International Holdings Limited ("Theme")

Theme operates a share option scheme (the "Theme Share Option Scheme") for the purpose of providing incentives and rewards to eligible participants who contribute to the success of the Theme and its subsidiaries operations. Eligible participants of the Theme Share Option Scheme include any employee or executive or any non-executive directors of the Theme and its subsidiaries, including any full-time or part-time employees or executives, executive directors, non-executive directors, independent non-executive directors and secretary of any member of the Theme and its subsidiaries. The Theme Share Option Scheme became effective on 26 March 2002 and, unless otherwise cancelled or amended, will remain in force for 10 years from that date.

The maximum number of unexercised share options currently permitted to be granted under the Theme Share Option Scheme is an amount equivalent, upon their exercise, to 10% of the shares of Theme in issue at any time. The maximum number of shares issuable under share options to each eligible participant in the Theme Share Option Scheme within any 12-month period, is limited to 1% of the shares of the Theme in issue at any time. Any further grant of share options in excess of this limit is subject to the approval of Theme's shareholders in a general meeting.

Share options granted to a director, chief executive or substantial shareholder of Theme, or to any of their associates, are subject to approval in advance by the independent non-executive directors of Theme. In addition, any share options granted to a substantial shareholder or an independent non-executive director of Theme, or to any of their associates, in excess of 0.1% of the shares of Theme in issue at any time or with an aggregate value (based on the price of the Theme's shares at the date of the grant) in excess of HK$5 million, within any 12-month period, are subject to approval of Theme's shareholders in advance in a general meeting.

The offer of a grant of share options of Theme may be accepted within 28 days from the date of the offer with no consideration being payable by the grantee. The share option may be exercised at any time during the Theme Share Option Scheme period.

The exercise price of the share options is determinable by the board of directors of Theme, but may not be less than the higher of (i) the Stock Exchange closing price of the Theme's shares on the date of the offer of the share options; (ii) the average Stock Exchange closing price of the Theme's shares for the five trading days immediately preceding the date of the offer; and (iii) the par value of the Theme's shares.

No share options were granted under Theme Share Option Scheme during the year nor outstanding as at the balance sheet date.

## 36. NON-CASH TRANSACTIONS

During the year ended 31 December 2004, the Group entered into finance lease arrangements in respect of assets with a total capital value at the inception of the leases of HK$313,000.

## 37. PLEDGE OF ASSETS

At the balance sheet date, the Group has pledged the following assets to secure credit facilities granted to the Group.

| | **2005** | 2004 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| Trade receivables | **98,185** | 57,449 |
| Bills receivable | **17,055** | – |
| Bank deposits | **159** | 5,554 |
| | **115,399** | 63,003 |

## 38. CONTINGENT LIABILITIES

At the balance sheet date, contingent liabilities not provided for in the financial statements were as follows:

| | **2005** | 2004 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| Bills discounted with recourse | **–** | 30,594 |
| Trade receivables factored with recourse | **–** | 13,011 |
| | **–** | 43,605 |

## 39. OPERATING LEASES

### (a) The Group as lessor

The Group leases its investment properties and subleases certain of its rented shops under operating lease arrangements with average lease term of one to two years.

At 31 December 2005, the Group had contracted with tenants for the following future minimum lease payment:

| | **2005** | 2004 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| Within one year | **9,552** | 7,951 |
| In the second to fifth years, inclusive | **7,264** | 9,601 |
| | **16,816** | 17,552 |

### (b) The Group as lessee

The Group had commitments for future minimum lease payments under non-cancellable operating leases which fall due as follows:

| | **2005** | 2004 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| Land and buildings: | | |
| Within one year | **37,980** | 41,723 |
| In the second to fifth years, inclusive | **59,905** | 73,006 |
| Over five years | **12,605** | 17,995 |
| | **110,490** | 132,724 |
| Equipment: | | |
| Within one year | **148** | – |
| In the second to fifth years, inclusive | **392** | – |
| | **540** | – |
| | **111,030** | 132,724 |

Operating lease payments represents rental payable by the Group for certain of its office premises, rental shops, factories and office equipment. Leases are negotiated for terms ranging from one to ten years.

## 40. COMMITMENTS

In addition to the operating lease commitments detailed in note 39 above, the Group had the following commitments at the balance sheet date:

**(a)** At the balance sheet date, the Group had entered into agreements for forward sales of foreign currencies contracts and the notional amounts are set out below.

| | **2005** | 2004 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| United States dollars | – | 77,390 |
| Euro dollars | – | 4,094 |
| British pounds | – | 16,478 |
| | – | 97,962 |

**(b)** Capital commitments

| | **2005** | 2004 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| Capital expenditure in respect of the acquisition of property, plant and equipment contracted for but not provided for in the financial statements | **1,247** | 1,680 |
| Capital expenditure in respect of the acquisition of property, plant and equipment authorised but not contracted for | **94** | – |

## 41. RELATED PARTY TRANSACTIONS

The Group had the following material transactions with related parties during the year:

| | **2005** | 2004 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| Purchases of raw materials and finished goods from jointly controlled entities | **47,611** | 50,129 |
| Sales of raw materials and finished goods to jointly controlled entities | **89** | 3,958 |
| Professional fees paid to Wilkinson & Grist *(note)* | **366** | 165 |

*Note:* Mr. Chan Wah Tip, Michael, director of the Company, is a partner of Wilkinson & Grist.

## 42. PARTICULARS OF PRINCIPAL SUBSIDIARIES

Details of the Company's principal subsidiaries at 31 December 2005 are as follows:

| Name of subsidiary | Place of incorporation or registration/ operations | Issued and fully paid share capital/ registered capital | Proportion of nominal value of issued capital/ registered capital held by the Group | Principal activities |
|---|---|---|---|---|
| | | | % | |
| Angel Star Investment Limited | Hong Kong | HK$2 Ordinary<br>HK$2 Non-voting deferred | 75<br>75 | Holding of trademarks |
| August Silk Inc. | USA | US$10 | 100 | Marketing and garment trading |
| Anway Garment Limited | Hong Kong | HK$2 | 100 | Garment trading |
| Bramead International Inc. | British Virgin Islands/USA | US$1 | 100 | Holding of trademarks |
| Cantabian Limited | Hong Kong | HK$2 Ordinary<br>HK$2 Non-voting deferred | 100<br>100 | Investment holding |
| Dongguan Dalisheng Fashion Co., Ltd. (Formerly known as Dongguan Daliwai Fashion Co. Ltd.) *(Note 1)* | PRC | HK$28,000,000 | 100 | Garment manufacturing |
| Dongguan Sanyue Fashions Limited *(Note 2)* | PRC | HK$10,000,000 | 69 | Garment manufacturing |
| Eminent Garment Limited | Hong Kong | HK$2 | 100 | Garment trading |
| Guangdong Theme-Huayu Fashion Company Limited | PRC | RMB5,000,000 | 75 | Garment retailing |
| Hangzhou High Fashion Knitwear Co., Ltd. *(Note 1)* | PRC | RMB3,000,000 | 100 | Garment manufacturing |

## 42. PARTICULARS OF PRINCIPAL SUBSIDIARIES *(cont'd)*

| Name of subsidiary | Place of incorporation or registration/ operations | Issued and fully paid share capital/ registered capital | Proportion of nominal value of issued capital/ registered capital held by the Group % | Principal activities |
|---|---|---|---|---|
| High Fashion Apparel Limited | British Virgin Islands/Hong Kong | US$1,000 | 100 | Investment holding |
| High Fashion (BVI) Limited | British Virgin Islands/PRC | US$1 | 100 | Product sourcing and development |
| High Fashion Garments, Inc. | USA | US$5,000 | 100 | Marketing and garment trading |
| High Fashion (China) Co., Ltd. *(Note 1)* | PRC | US$14,600,00 | 100 | Garment manufacturing and dyeing, printing and sandwashing of fabrics |
| High Fashion (FG) Limited | British Virgin Islands/PRC | US$1 | 100 | Garment manufacturing |
| High Fashion Garments Company Limited | Hong Kong | HK$2 ordinary<br>HK$10,000,000 Non-voting deferred | 100<br>100 | Garment trading |
| High Fashion Garments Macao Commercial Offshore Limited | Macau | MOP100,000 | 100 | Garment trading |
| High Fashion Garments Management Limited | Hong Kong | HK$20 Ordinary<br>HK$20 Non-voting deferred | 100<br>100 | Provision of management services |
| High Fashion Home Textiles Company Limited | Hong Kong | HK$2 | 100 | Garment Trading |
| High Fashion International (USA) Inc. | USA | US$1,800 | 100 | Investment holding |

## 42. PARTICULARS OF PRINCIPAL SUBSIDIARIES *(cont'd)*

| Name of subsidiary | Place of incorporation or registration/ operations | Issued and fully paid share capital/ registered capital | Proportion of nominal value of issued capital/ registered capital held by the Group % | Principal activities |
|---|---|---|---|---|
| High Fashion (HZ) Limited | British Virgin Islands/PRC | US$1 | 100 | Garment manufacturing |
| High Fashion Knitwear Overseas Limited | Hong Kong | HK$2 Ordinary<br>HK$10,000 Non-voting deferred | 100<br>100 | Garment trading |
| High Fashion Silk (Zhejiang) Co., Ltd. *(Note 1)* | PRC | US$20,000,000 | 100 | Silk weaving |
| High Fashion (UK) Limited | United Kingdom | GBP20,000 | 70.5 | Garment trading |
| Navigation Limited | British Virgin Islands/Hong Kong | US$1 | 100 | Investment holding |
| Stage II Limited | Hong Kong | HK$800,000 | 75 | Garment retailing |
| Taiwan Vision Company Limited | Taiwan | NT$80,000,000 | 75 | Garment retailing |
| Theme Corporate Fashion (Asia) Limited | Hong Kong | HK$1 | 75 | Garment trading |
| Theme Corporate Fashion (Europe) Limited | Hong Kong | HK$1 | 75 | Garment trading |
| Theme Corporate Fashion (Overseas) Limited | Hong Kong | HK$1 | 75 | Garment trading |
| Theme (Dongguan) Limited | British Virgin Islands/PRC | US$1 | 75 | Garment trading |
| Theme Garments (Shenzhen) Company Limited | PRC | RMB10,000,000 | 75 | Garment retailing and trading |

## 42. PARTICULARS OF PRINCIPAL SUBSIDIARIES *(cont'd)*

| Name of subsidiary | Place of incorporation or registration/ operations | Issued and fully paid share capital/ registered capital | Proportion of nominal value of issued capital/ registered capital held by the Group % | Principal activities |
|---|---|---|---|---|
| Theme Fashion (Singapore) Pte. Ltd. | Singapore | S$100,000 | 75 | Garment trading |
| Theme Industry Hangzhou Company Limited | PRC | US$2,000,000 | 75 | Garment retailing and trading |
| The King Garment Limited | Hong Kong | HK$2 | 100 | Garment trading |
| Theme International Holdings Limited ("Theme") | Bermuda/ Hong Kong | HK$50,166,588 | 75 | Investment holding |
| Theme International Limited | Hong Kong | HK$2 Ordinary<br>HK$1,000,000 Non-voting deferred | 75<br>75 | Garment trading |
| Winsmart Overseas Limited | Hong Kong | HK$2 | 100 | Garment trading |
| Zhejiang Xinchang High Fashion Silk Co., Ltd. *(Note 1)* | PRC | US$6,000,000 | 100 | Silk weaving |

*Notes:*

(1) These companies are registered as a wholly foreign owned enterprise.

(2) These companies are registered as a sino-foreign equity joint venture.

The subsidiaries listed above are indirectly held by the Company.

The shares of Theme are listed on The Stock Exchange of Hong Kong Limited. The market value of Theme's shares held by the Group amounted to HK$97,824,000, as at 31 December 2005 (2004: HK$135,450,000).

## 42. PARTICULARS OF PRINCIPAL SUBSIDIARIES *(cont'd)*

The above table lists the subsidiaries of the Company which, in the opinion of the directors, principally affected the results or assets and liabilities of the Group. To give details of other subsidiaries would, in the opinion of the directors, result in particulars of excessive length.

Except for Theme which issued a convertible note to the Company, none of the subsidiaries had issued any debt securities at the end of the year.

## 43. SUBSEQUENT EVENTS

On 26 January 2006, two indirect subsidiaries of the Company in Hangzhou entered into an agreement with the 杭州工業項目推進領導小組辦公室 and 杭州市土地儲備中心 ("土地儲備中心") in relation to the relocation from Liuxia Street of Hangzhou City within 18 months from the agreement and would handover the land to 杭州市土地儲備中心 for sale by public auction. Advance payments of HK$21,307,000 for compensation and HK$12,856,000 for reimbursement removal expenses were received respectively in February 2006. In the event of such sale, 45% of the proceeds from the sale of land (after deduction of such advance payments) would be paid as compensation to the Group for the construction of the world's top class silk enterprise and world class apparel enterprise in Hangzhou.

On 30 March 2006, an indirect wholly-owned subsidiary of the Company, entered into an acquisition agreement with an independent third party for the acquisition of the trademark, the current retail network and part of the fixed and current assets and liabilities at the total consideration of not more than RMB22,000,000 (approximately HK$21,275,000). The acquisition is effective on 1 April 2006.

In the opinion of the directors, it is impracticable to disclose the carrying amounts and fair values of each class of assets, liabilities and contingent liabilities at the date of acquisition as the information with respect to the carrying amounts and fair values have not yet been finalised up to the date of issue of the financial statements.