# Notes
## to the Consolidated Financial Statements

## 1 General information

Lung Cheong International Holdings Limited (the "Company") and its subsidiaries (collectively, the "Group") are principally engaged in development, engineering, manufacture and sales of toys and moulds.

The Company is a limited liability company incorporated in the Cayman Islands. Its principal place of business is at Lung Cheong Building, 1 Lok Yip Road, Fanling, New Territories, Hong Kong.

The Company's shares are listed on the Main Board of The Stock Exchange of Hong Kong Limited.

These financial statements are presented in thousands of units of Hong Kong dollars (HK$'000), unless otherwise stated. These financial statements have been approved for issue by the Board of Directors on 28 July 2006.

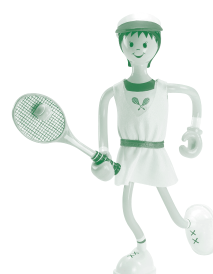
## 2 Summary of significant accounting policies

The principal accounting policies applied in the preparation of these financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

### (a) Basis of preparation

These financial statements have been prepared in accordance with Hong Kong Financial Reporting Standards ("HKFRS"). The financial statements have been prepared under the historical cost convention, as modified by the revaluation of freehold land and buildings, available-for-sale financial assets, financial assets and financial liabilities (including derivative financial instruments) at fair value through profit or loss, which are carried at fair value.

The preparation of financial statements in conformity with HKFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group's accounting policies. The areas involving a higher degree of judgement of complexity, or areas where assumptions and estimates are significant to the consolidated financial statements, are disclosed in Note 4.



## 2 Summary of significant accounting policies *(Continued)*

### (a) Basis of preparation *(Continued)*

*The adoption of new/revised HKFRS*

In the current year, the Group adopted the new/revised standards of HKFRS below, which are relevant to its operations. Last year's comparatives have been amended as required, in accordance with the relevant requirements.

| | |
|---|---|
| HKAS 1 | Presentation of Financial Statements |
| HKAS 2 | Inventories |
| HKAS 7 | Cash Flow Statements |
| HKAS 8 | Accounting Policies, Changes in Accounting Estimates and Errors |
| HKAS 10 | Events after the Balance Sheet Date |
| HKAS 16 | Property, Plant and Equipment |
| HKAS 17 | Leases |
| HKAS 21 | The Effects of Changes in Foreign Exchange Rates |
| HKAS 23 | Borrowing Costs |
| HKAS 24 | Related Party Disclosures |
| HKAS 27 | Consolidated and Separate Financial Statements |
| HKAS 32 | Financial Instruments: Disclosures and Presentation |
| HKAS 33 | Earnings per Share |
| HKAS 36 | Impairment of Assets |
| HKAS 38 | Intangible Assets |
| HKAS 39 | Financial Instruments: Recognition and Measurement |
| HKAS 39 (Amendment) | Transition and Initial Recognition of Financial Assets and Financial Liabilities |
| HKAS-Int 15 | Operating Leases — Incentives |
| HKFRS 2 | Share-based Payments |
| HKFRS 3 | Business Combinations |

## 2 Summary of significant accounting policies *(Continued)*

### (a) Basis of preparation *(Continued)*

The adoption of new/revised HKASs 1, 2, 7, 8, 10, 16, 21, 23, 24, 27, 33 and HKAS-Int 15 did not result in substantial changes to the Group's accounting policies. In summary:

— HKAS 1 has affected the presentation of the disclosures of financial statements.

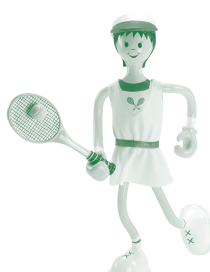
— HKASs 2, 7, 8, 10, 16, 23, 27, 33 and HKAS-Int 15 had no material effect on the Group's policies.

— HKAS 21 had no material effect on the Group's policy. The functional currency of each of the consolidated entities has been re-evaluated based on the guidance to the revised standard. All the Group entities have the same functional currency as the presentation currency for respective entity financial statements.

— HKAS 24 has affected the identification of related parties and some other related party disclosures.

The adoption of revised HKAS 17 has resulted in a change in the accounting policy relating to the reclassification of leasehold land and land use rights from property, plant and equipment to operating leases. The up-front prepayments made for the leasehold land and land use rights are expensed in the income statement on a straight-line basis over the period of the lease or where there is impairment, the impairment is expensed in the income statement. In prior years, the leasehold land and land use rights were accounted for at cost less accumulated depreciation and accumulated impairment losses, if any.

The adoption of HKASs 32, 39 and 39 (Amendment) has resulted in a change in the accounting policy relating to the classification of available-for-sale financial assets. It has also resulted in a change in the recognition, measurement and classification of derivative financial instruments. Certain interest rates swaps and foreign exchange contracts which do not quality for hedge accounting, are initially recognised at fair value on the date on which such derivative contracts are entered into and subsequently remeasured at their fair value. Changes in fair value of the derivatives are recognised immediately in the income statement.



## 2 Summary of significant accounting policies *(Continued)*

### (a) Basis of preparation *(Continued)*

The adoption of HKAS 36, HKAS 38 and HKFRS 3 has resulted in a change in the accounting policy for goodwill. Until 31 March 2005, goodwill was amortised on a straight-line basis over a period of 15 years, and assessed for an indication of impairment at each balance sheet date. In accordance with the provisions of HKFRS 3, the Group ceased amortisation of goodwill from 1 April 2005; accumulated amortisation as at 31 March 2005 has been eliminated with a corresponding decrease in the cost of goodwill; from the year ended 31 March 2006 and onwards, goodwill is tested annually for impairment, as well as when there is indication of impairment. The Group has reassessed the useful lives of its intangible assets in accordance with the provision of HKAS 38. No adjustment resulted from this reassessment. The transitional provisions allow retrospective application of this new policy under certain restricted situations, which are not applicable to the Group, and accordingly the last year's comparative figures have not reflected the effect of this change.

The adoption of HKFRS 2 has resulted in a change in the accounting policy for share-based payments. Until 31 March 2005, the provision of share options to employees did not result in an expense in the income statement. Effective 1 April 2005, the Group expenses the cost of share options in the income statement. The Group has taken advantage of the transitional provisions under which the HKFRS 2 are not applicable to those share options granted on or before 7 November 2002 and those granted after 7 November 2002 but which had vested before 1 January 2005. Since the employees' share options were granted before 7 November 2002, the HKFRS has no effect on the Group at 1 April 2005. The employees' share options lapsed during the year.

All changes in the accounting policies have been made in accordance with the transition provisions in the respective standards, wherever applicable. All standards adopted by the Group require retrospective application other than:

- HKAS 16 under which the initial measurement of an item of property, plant and equipment acquired in an exchange of assets transaction is accounted at fair value prospectively only to future transaction;

- HKAS 21 which requires prospective application for accounting goodwill and fair value adjustments as part of foreign operations;

- HKAS 39 which does not permit recognition, derecognition and measurement of financial assets and liabilities in accordance with this standard on a retrospective basis. The Group applied the previous Statement of Standard Accounting Practice ("SSAP") 24 "Accounting for investments in securities" to other investments for the last year's comparative information. The adjustments required for the accounting differences between SSAP 24 and HKAS 39, if any, are determined and recognised at 1 April 2005;

## 2 Summary of significant accounting policies *(Continued)*

### (a) Basis of preparation *(Continued)*

- HKFRS — Int 15 which does not require the recognition of incentives for leases beginning before 1 April 2005

- HKFRS 2 which is only retrospectively applied for all equity instruments granted after 7 November 2002 and not vested at 1 January 2005; and

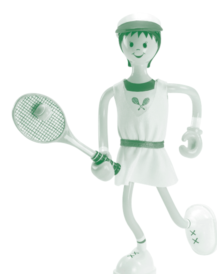
- HKFRS 3 which is applied prospectively after 1 April 2005.

(i) The adoption of revised HKAS 17 resulted in an increase in open reserves at 1 April 2004 by approximately HK$8,630,000. The details of the adjustments to the balance sheets at 31 March 2006 and 31 March 2005, income statements for the year ended 31 March 2006 and 2005 are as follows:

| | **2006** | 2005 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| Decrease in property, plant and equipment | **(55,860)** | (57,094) |
| Increase in leasehold land and land use rights | **47,458** | 48,578 |
| Increase in retained earnings | **12,283** | 12,397 |
| Decrease in buildings revaluation reserve | **(3,881)** | (3,881) |
| Increase in general and administrative expenses | **114** | 114 |

(ii) The adoption of HKFRS 3, HKAS 36 and HKAS 38 resulted in the reclassification of approximately HK$2,474,000 and HK$28,238,000 from other investments to intangible assets and available-for-sale financial assets respectively at 1 April 2005. The details of the adjustments to the balance sheet at 31 March 2006 and income statement for the year ended 31 March 2006 are as follows:

| | **2006** |
|---|---|
| | HK$'000 |
| Increase in intangible assets | **4,107** |
| Increase in available-for-sale financial assets | **28,103** |
| Decrease in other investments | **(30,577)** |
| Decrease in general and administrative expenses | **(1,633)** |



## 2 Summary of significant accounting policies *(Continued)*

### (a) Basis of preparation *(Continued)*

(iii) The adoption of revised HKAS 39 resulted in a decrease in opening reserves at 1 April 2005 by approximately HK$396,000. The details of the adjustments to the balance sheet at 31 March 2006 and income statement for the year ended 31 March 2006 are as follows:

| | **2006** |
|---|---|
| | HK$'000 |
| Increase in derivative financial instruments (assets) | **450** |
| Increase in derivative financial instruments (liabilities) | **105** |
| Increase in other gains, net | **741** |

*Standards, interpretations and amendments to published standards that are not yet effective*

Certain new standards, interpretations and amendments to existing standards have been published that are mandatory for accounting periods beginning on or after the effective date as described below, as follows:

| **New HKFRS or interpretations** | **Effective date** | **Description** |
|---|---|---|
| HKAS 1 (Amendment) | 1 January 2007 | Capital Disclosure |
| HKAS 19 (Amendment) | 1 January 2006 | Actuarial gains and losses, group plans and disclosures |
| HKAS 21 (Amendment) | 1 January 2006 | Net investment in a foreign operation |
| HKAS 39 & HKFRS 4 (Amendment) | 1 January 2006 | Financial guarantee contracts |
| HKAS 39 (Amendment) | 1 January 2006 | Cash flow hedge accounting of forecast intragroup transactions |
| HKAS 39 (Amendment) | 1 January 2006 | The fair value option |
| HKFRS 1 (Amendment) | 1 January 2006 | First-time adoption of Hong Kong Financial Reporting Standards |
| HKFRS 6 | 1 January 2006 | Exploration for and Evaluation of Mineral Resources |
| HKFRS 7 | 1 January 2007 | Financial instruments: Disclosures |
| HKFRS-Int 4 | 1 January 2006 | Determining whether an arrangement contains a lease |
| HKFRS-Int 5 | 1 January 2006 | Rights to interests arising from decommissioning, restoration and environmental rehabilitation funds |
| HK(IFRIC)-Int 6 | 1 December 2005 | Liabilities arising from participating in a specific market — waste electrical and electronic equipment |
| HK(IFRIC)-Int 7 | 1 March 2006 | Applying the restatement approach under HKAS 29 financial reporting in hyperinflationary economies |

The Group has not early adopted these new/revised HKFRSs. The Company's directors and the Group's management anticipate that the adoption of these Standards or Interpretations or Amendments will have no material impact on the financial statements of the Group and will not result in substantial changes to the Group's accounting policies.

## 2 Summary of significant accounting policies *(Continued)*

### (b) Consolidation

The consolidated financial statements include the financial statements of the Company and all its subsidiaries made up to 31 March.

Subsidiaries are all entities (including special purpose entities) over which the Group has the power to govern the financial and operating policies generally accompanying a shareholding of more than one half of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group controls another entity.

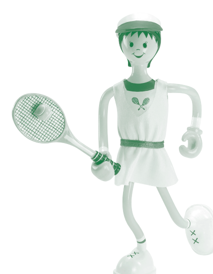
Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are de-consolidated from the date that control ceases.

The purchase method of accounting is used to account for the acquisition of subsidiaries by the Group. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any minority interest. The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognised directly in the consolidated income statement.

Inter-company transactions, balances and unrealised gains on transactions between group companies are eliminated. Unrealised losses are also eliminated but considered as an impairment indicator of an impairment of the asset transferred.

Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group.

In the Company's balance sheet the investments in subsidiaries are stated at cost less accumulated impairment losses. The results of subsidiaries are accounted for by the Company on the basis of dividends received and receivable.



## 2 Summary of significant accounting policies *(Continued)*

### (c) Segment reporting

A business segment is a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different from those of other business segments. A geographical segment is engaged in providing products or services within a particular economic environment that are subject to risks and returns that are different from those of segments operating in other economic environments.

### (d) Translation of foreign currencies

*(i) Functional and presentation currency*

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates ("the functional currency"). The consolidated financial statements are presented in Hong Kong dollars which is the Company's functional and presentation currency.

*(ii) Transactions and balances*

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement.

Translation differences on non-monetary items, such as equity instruments held at fair value through profit or loss, are reported as part of the fair value gain or loss. Translation difference on non-monetary items, such as equities classified as available-for-sale financial assets, are included in the fair value reserve in equity.

## 2 Summary of significant accounting policies *(Continued)*

### (d) Translation of foreign currencies *(Continued)*

*(iii) Group companies*

The results and financial position of all the group entities (none of which has the currency of a hyperinflationary economy) that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

- assets and liabilities for each balance sheet presented are translated at the closing rate at the date of that balance sheet;

- income and expenses for each income statement are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the dates of the transactions); and

- all resulting exchange differences are recognised as a separate component of equity.

On consolidation, exchange differences arising from the translation of the net investment in foreign entities are taken to shareholders' equity. When a foreign operation is sold, such exchange differences are recognised in the income statement as part of the gain or loss on sale.

Goodwill and fair value adjustments arising on the acquisition of a foreign entity are treated as assets and liabilities of the foreign entity and translated at the closing rate.

### (e) Property, plant and equipment

Buildings comprise mainly factories, showrooms and offices. Freehold land and buildings are shown at fair value, based on periodic, but at least triennial, valuations by external independent valuers, less subsequent depreciation. Any accumulated depreciation at the date of revaluation is eliminated against the gross carrying amount of the asset and the net amount is restated to the revalued amount of the asset. All other property, plant and equipment are stated at historical cost less depreciation and impairment losses. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

## 2 Summary of significant accounting policies *(Continued)*

### (e) Property, plant and equipment *(Continued)*

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. All other repairs and maintenance are expensed in the income statement during the financial period in which they are incurred.

Increases in the carrying amount arising on revaluation of freehold land and buildings are credited to other reserves in shareholders' equity. Decreases that offset previous increases of the same asset are charged against other reserves directly in equity; all other decreases are expensed in the income statement.

Depreciation of property, plant and equipment is calculated using the straight-line method to allocate cost or revalued amounts to their residual values over their estimated useful lives, as follows:

| | |
|---|---|
| Buildings | 50 years |
| Leasehold improvements | 20 – 50 years |
| Plant and machinery | 5 years |
| Furniture, fixtures and equipment | 5 years |
| Motor vehicles | 5 years |
| Moulds | 5 years |

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount.

Gains and losses on disposals are determined by comparing proceeds with carrying amount. These are included in the income statement.

## 2 Summary of significant accounting policies *(Continued)*

### (f) Intangible assets

*(i) Goodwill*

Goodwill represents the excess of the cost of an acquisition over the fair value of the Group's share of the net identifiable assets of the acquired subsidiary at the date of acquisition. Goodwill on acquisitions of subsidiaries is included in intangible assets. Goodwill is tested annually for impairment and carried at cost less accumulated impairment losses, if any. Impairment losses on goodwill are not reversed.

Goodwill is allocated to cash-generating units for the purpose of impairment testing. The allocation is made to those cash-generating units or groups of cash-generating units that are expected to benefit from the business combinations in which the goodwill arose.

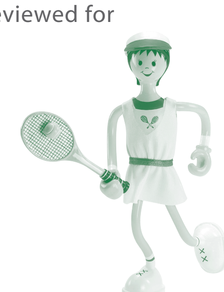
*(ii) Club memberships*

Club memberships are stated at cost less any accumulated impairment losses.

The carrying amounts are reviewed at each balance sheet date to assess whether the fair values have declined below the carrying amounts. When a decline other than temporary has occurred, the carrying amount is reduced to its fair value. The impairment loss is recognised as an expense in the income statement. This impairment loss is written back to the income statement when the circumstances and events that led to the write-downs or write-offs cease to exist and there is persuasive evidence that the new circumstances and events will persist for the foreseeable future.

### (g) Impairment of non-financial assets

Assets that have an indefinite useful life are not subject to depreciation or amortisation, which are at least tested annually for impairment and are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). Non-financial assets other than goodwill that suffered an impairment are reviewed for possible reversal of the impairment at each reporting date.



## 2 Summary of significant accounting policies *(Continued)*

### (h) Financial assets

*From 1 April 2004 to 31 March 2005:*

The Group classified its investments in securities, other than subsidiaries, as other investments.

Other investments held for non-trading purpose are stated at cost less accumulated impairment losses. The carrying amounts of individual investments are reviewed at each balance sheet date to assess whether the fair value have declined below the carrying amounts.

When a decline other than temporary has occurred, the carrying amount of such investment will be reduced to its fair value. The impairment loss is recognised as an expense in the income statement. This impairment loss is written back to profit and loss when the circumstances and events that led to the write-downs or write-offs cease to exist and there is persuasive evidence that the new circumstances and events will persist for the foreseeable future.

Trading securities were carried at fair value. At each balance sheet date, the net unrealised gains or losses arising from the changes in fair value of trading securities were recognised in the income statement. Profits or losses on disposal of trading securities, representing the difference between the net sales proceeds and the carrying amounts, were recognised in the income statement as they arise.

*From 1 April 2005 onwards:*

The Group classifies its financial assets as available-for-sale based on the purpose for which the financial assets were acquired. Management determines the classification of its financial assets at initial recognition and re-evaluates this designation at every reporting date.

Available-for-sale financial assets are non-derivatives. They are included in non-current assets unless management intends to dispose of the investment within twelve months of the balance sheet date.

Regular purchases and sales of investments are recognised on trade-date — the date on which the Group commits to purchase or sell the asset. Investments are initially recognised at fair value plus transaction costs for all financial assets not carried at fair value through profit or loss. Investments are derecognised when the rights to receive cash flows from the investments have expired or have been transferred and the Group has transferred substantially all risks and rewards of ownership. Available-for-sale financial assets are subsequently carried at fair value.

## 2 Summary of significant accounting policies *(Continued)*

### (h) Financial assets *(Continued)*

*From 1 April 2005 onwards: (Continued)*

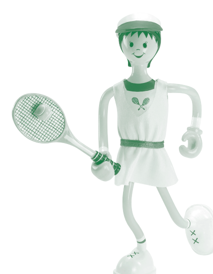
Changes in the fair value of securities classified as available-for-sale are recognised in equity. When securities classified as available-for-sale are sold or impaired, the accumulated fair value adjustments recognised in equity are included in the income statement as 'gains and losses from investment securities'. Interest on available-for-sale securities calculated using the effective interest method is recognised in the income statement.

The fair values of quoted investments are based on current bid prices. If the market for a financial asset is not active (and for unlisted securities), the Group establishes fair value by using valuation techniques. These include the use of recent arm's length transactions, reference to other instruments that are substantially the same and discounted cash flow analysis, and option pricing models, making maximum use of market inputs and relying as little as possible on entity-specific inputs.

The Group assesses at each balance sheet date whether there is objective evidence that a financial asset or a group of financial assets is impaired. In the case of equity securities classified as available for sale, a significant or prolonged decline in the fair value of the security below its cost is considered in determining whether the securities are impaired. If any such evidence exists for available-for-sale financial assets, the cumulative loss — measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in the income statement — is removed from equity and recognised in the income statement. Impairment losses recognised in the income statement on equity instruments are not reversed through the income statement.

### (i) Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is determined using the first-in, first-out (FIFO) method. The cost of finished goods and work-in-progress comprises raw materials, direct labour and an appropriate proportion of production overheads. Net realisable value is determined on the basis of anticipated sales proceeds less estimated selling expenses and, where appropriate, the cost of conversion from their existing state to a finished condition.



## 2 Summary of significant accounting policies *(Continued)*

### (j) Trade receivables

Trade and other receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less provision for impairment. A provision for impairment of trade and other receivables is established when there is objective evidence that the Group will not be able to collect all amounts due to according to the original terms of receivables. Significant financial difficulties of the debtor, probability that the debtor will enter bankruptcy or financial reorganisation, and default or delinquency in payments are considered as indicators that the trade and other receivable is impaired. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the effective interest rate. The amount of the provision is recognised in the income statement.

### (k) Cash and cash equivalents

Cash and cash equivalents include cash in hand, deposits held at call with banks and bank overdrafts. Bank overdrafts are shown within borrowings in current liabilities on the balance sheet.

### (l) Employee benefits

*(i) Employee leave entitlements*

Employee entitlements to annual leave are recognised when they accrue to employees. A provision is made for the estimated liability for annual leave as a result of services rendered by employees up to the balance sheet date.

Employee entitlements to sick leave and maternity leave are not recognised until the time of leave.

Employee entitlements to long service leave are recognised when they accrue to employees. A provision is made for the estimated liability for long service leave as a result of services rendered by employees up to the balance sheet date.

## 2 Summary of significant accounting policies *(Continued)*

### (l) Employee benefits *(Continued)*

*(ii) Profit sharing and bonus plans*

The expected cost of profit sharing and bonus payments are recognised as a liability when the Group has a present legal or constructive obligation as a result of services rendered by employees and a reliable estimate of the obligation can be made.

Liabilities for profit sharing and bonus plans are expected to be settled within twelve months and are measured at the amounts expected to be paid when they are settled.

*(iii) Pension obligations*

The Group participates in several defined contribution retirement benefit schemes. A defined contribution plan is a retirement benefit scheme under which the Group pays contributions, on a mandatory, contractual or voluntary basis, into a separate entity. The schemes are generally funded through payments to insurance companies or state/trustee-administered funds. The Group has no further payment obligations once the contributions have been paid. It has no legal or constructive obligations to pay further contributions if the fund does not hold sufficient assets to pay all employees the benefits relating to employee service in the current and prior periods.

The contributions are recognised as employment costs when they are due and are reduced by contributions forfeited by those employees who leave the scheme prior to vesting fully in the contributions.

*(iv) Share based compensation benefits*

The fair value of the employee services received in exchange for the grant of the options is recognised as an expense. The total amount to be expensed over the vesting period is determined by reference to the fair value of the options granted, excluding the impact of any non-market vesting conditions (for example, profitability and sales growth targets). Non-market vesting conditions are included in assumptions about the number of options that are expected to become exercisable. At each balance sheet date, the entity revises its estimates of the number of options that are expected to become exercisable. It recognises the impact of the revision of original estimates, if any, in the income statement with a corresponding adjustment to equity.

The proceeds received net of any directly attributable transaction costs are credited to share capital (nominal value) and share premium when the options are exercised.

## 2 Summary of significant accounting policies *(Continued)*

### (m) Borrowings

Borrowings are recognised initially at fair value, net of transaction costs incurred. Transaction costs are incremental costs that are directly attributable to the acquisition, issue or disposal of a financial asset or financial liability, including fees and commissions paid to agents, advisers, brokers and dealers, levies by regulatory agencies and securities exchanges, and transfer taxes and duties. Borrowings are subsequently stated at amortised cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognised in the income statement over the period of the borrowings using the effective interest method.

Borrowings are classified as current liabilities unless the Group has an unconditional right to defer settlement of the liability for at least twelve months after the balance sheet date.

### (n) Borrowing costs

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

### (o) Deferred income tax

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. However, deferred income tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

Deferred income tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

Deferred income tax is provided on temporary differences arising on investments in subsidiaries, except where the timing of the reversal of the temporary difference can be controlled by the Group and it is probable that the temporary difference will not reverse in the foreseeable future.

## 2 Summary of significant accounting policies *(Continued)*

### (p) Revenue recognition

Revenue comprises the fair value of the consideration received or receivable for the sale of goods and services in the ordinary course of the Group's activities, net of value-added tax rebates and discounts and after elimination of sales with the Group. Revenue is recognised as follows:

*(i) Sales of goods*

Sales of goods are recognised when a group entity sells a product to the customer, has delivered products to the customer, the customer has accepted the products and collectibility of the related receivables is reasonably assumed.

*(ii) Interest income*

Interest income is recognised on a time-proportion basis using the effective interest method.

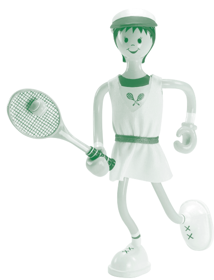
### (q) Operating leases

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are expensed in the income statement on a straight-line basis over the period of the lease.

### (r) Provisions

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation, and a reliable estimate of the amount can be made. Where the Group expects a provision to be reimbursed, the reimbursement is recognised as a separate asset but only when the reimbursement is virtually certain.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognised even if the likelihood of an outflow with respect to any one item included in the same class of obligations is small.



## 2 Summary of significant accounting policies *(Continued)*

### (s) Contingent liabilities

A contingent liability is a possible obligation that arises from past events and whose existence will only be confirmed by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the Group. It can also be a present obligation arising from past events that is not recognised because it is not probable that outflow of economic resources will be required or the amount of obligation cannot be measured reliably.

A contingent liability is not recognised but is disclosed in the financial statements. When a change in the probability of an outflow occurs so that the outflow is probable, it will then be recognised as a provision.

### (t) Share capital

Ordinary shares are classified as equity.

### (u) Dividend distribution

Dividend distribution to the Company's equity holders is recognised as a liability in the Group's financial statements in the period in which the dividends are approved by the Company's equity holders.

### (v) Derivative financial instruments

*From 1 April 2004 to 31 March 2005:*

The derivative financial instruments were previously recorded as off balance sheet items. The actual gains or losses realised upon settlement were included in the income statement on maturity.

*From 1 April 2005 onwards:*

Derivates are initially recognised at fair value on the date a derivative contract is entered into and are subsequently remeasured at their fair value. The method of recognising the resulting gain or loss depends on whether the derivative is designated as a hedging instrument, and if so, the nature of the item being hedged. Since the derivative instruments entered into by the Group do not qualify for hedge accounting, changes in the fair value of any derivative instruments are recognised immediately in the income statement.

## 3 Financial risk management

### 3.1 Financial risk factors

The Group's activities expose it to a variety of financial risks: foreign exchange risk, credit risk, liquidity risk and cash flow and fair value interest-rate risk.

*(a) Foreign exchange risk*

The Group is exposed to foreign exchange risk arising from various currency exposures, primarily with respect to United States dollars, Renminbi and Indonesia Rupiah. Foreign exchange risk arises from future commercial transactions, recognised assets and liabilities and net investments in foreign operations. The Group currently does not hedge its foreign exchange exposure.

*(b) Credit risk*

The Group has significant concentrations of credit risk. It has policies in place to ensure that sales to customers with an appropriate credit history. The carrying amount of the trade receivables included in the consolidated balance sheet represents the Group's maximum exposure to credit risk in relation to its financial assets.

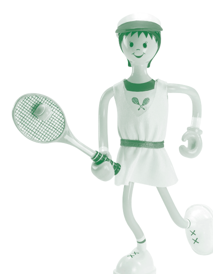
*(c) Liquidity risk*

The Group maintains availability of funding through an adequate amount of available credit facilities. The management aims to maintain flexibility in funding by keeping credit lines available.

*(d) Cash flow and fair value interest-rate risk*

As the Group has no significant interest-bearing assets, the Group's income and operating cash flows are substantially independent of changes in market interest rates.

The Group's interest-rate risk arises from bank borrowings. Bank borrowings issued at variable rates expose the Group to cash flow interest-rate risk. The Group regularly seeks out the most favourable interest rates available for its bank borrowings.



## 3 Financial risk management *(Continued)*

### 3.2 Fair value estimation

The fair value of financial instruments traded in active markets is based on quoted market prices at the balance sheet date. The quoted market price used for financial assets held by the Group is the current closing price.

The fair values of financial instruments that are not traded in an active market is determined by using valuation techniques. The Group uses a variety of methods and make assumptions that are based on market conditions existing at each balance sheet date to determine fair value for the remaining financial instruments.

The nominal value less estimated credit adjustments of trade and bills receivables and trade and bills payables are assumed to approximate their fair values. The fair value of financial liabilities for disclosure purposes is estimated by discounting the future contractual cash flows at the current market interest rate that is available to the Group for similar financial instruments.

## 4 Critical accounting estimates and judgements

Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

The Group makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets or liabilities are discussed below.

### (a) Useful lives, residual values and depreciation of property, plant and equipment

The Group's management determines the estimated useful lives, residual values and related depreciation charges for its property, plant and equipment. This estimate is based on the historical experience of the actual useful lives of property, plant and equipment of similar nature and functions. Management will increase the depreciation charge where useful lives are less than previously estimated lives, it will write-off or write-down technically obsolete or non-strategic assets that have been abandoned or sold. Actual economic lives may differ from estimated useful lives; actual residual values may differ from estimated residual values. Periodic review could result in a change in depreciable lives and residual values and therefore depreciation expense in the future periods.

## 4 Critical accounting estimates and judgements *(Continued)*

### (b) Impairment of goodwill

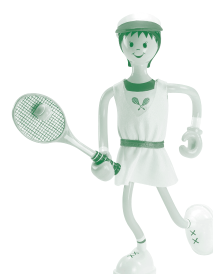
The Group tests annually whether goodwill has suffered any impairment. For the purposes of impairment reviews, the recoverable amount of goodwill is determined based on value-in-use calculations. The value-in-use calculations primarily use cash flow projections based on ten-year financial budgets approved by management. There are a number of assumptions and estimates involved in the preparation of cash flow projections for the period covered by the approved budgets. Key assumptions include the expected growth in revenues, timing of future capital expenditures, growth rates and selection of discount rates to reflect the risks involved. Management prepares the financial budgets reflecting actual and prior year performance and market development expectations. Judgement is required to determine key assumptions adopted in the cash flow projections and changes to key assumptions can significantly affect these cash flow projections and therefore the results of the impairment reviews.

### (c) Net realisable value of inventories

Net realisable value of inventories is the estimated selling price in the ordinary course of business, less estimated costs of completion and variable selling expenses. These estimates are based on the current market condition and the historical experience of manufacturing and selling products of similar nature. It could change significantly as a result of changes in customer taste and competitor actions in response to severe industry cycle. Management reassesses the estimations at each balance sheet date.

### (d) Trade and other receivables

The Group's management determines the provision for impairment of trade and other receivable based on an assessment of the recoverability of the receivables. This assessment is based on the credit history of its customers and other debtors and the current market condition. Management reassesses the provision at each balance sheet date.



## 4 Critical accounting estimates and judgements *(Continued)*

### (e) Income taxes and deferred tax

The Group is subject to income taxes in Hong Kong and Mainland China. There are certain transactions and calculations for which the ultimate tax determination is uncertain during the ordinary course of business. The Group recognises liabilities for anticipated tax audit issues based on estimates of whether additional taxes will be due. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the income tax and deferred tax provisions in the period in which such determination is made.

Deferred tax assets relating to certain temporary differences and tax losses are recognised when management considers it is likely that future taxable profits will be available against which the temporary differences or tax losses can be utilised. When the expectations are different from the original estimates, such differences will impact the recognition of deferred tax assets and income tax charges in the period in which such estimates have been changed.

## 5 Turnover and segment information

The Group is principally engaged in the development, engineering, manufacturing and sale of toys and moulds. Turnover recognised during the year are as follows:

| | **Group** | |
|---|---|---|
| | **2006** | 2005 |
| | **HK$'000** | HK$'000 |
| Turnover | | |
| Sale of goods | **717,055** | 743,597 |
| Sale of moulds | **33,565** | 31,113 |
| | **750,620** | 774,710 |

### Primary reporting format — business segments

The Group's turnover and results are substantially derived from manufacturing of toys. Accordingly, no analysis by business segment is presented.

## 5 Turnover and segment information *(Continued)*

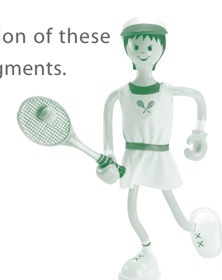
### Secondary reporting format — geographical segments

| | Turnover 2006 HK$'000 | Total assets 2006 HK$'000 | Capital expenditure 2006 HK$'000 |
|---|---|---|---|
| United States of America | **307,521** | **59,134** | **68** |
| Europe (Note) | **112,495** | **5,919** | **—** |
| Japan | **165,683** | **101,468** | **—** |
| Mainland China | **91,965** | **586,877** | **94,817** |
| Indonesia | **1,691** | **22,981** | **1,065** |
| Hong Kong | **26,141** | **245,671** | **28,149** |
| Others | **45,124** | **2,937** | **—** |
| Total | **750,620** | **1,024,987** | **124,099** |

| | Turnover 2005 HK$'000 | Total assets 2005 HK$'000 (Restated) | Capital expenditure 2005 HK$'000 |
|---|---|---|---|
| United States of America | 344,080 | 123,757 | 35 |
| Europe (Note) | 118,542 | 1,218 | — |
| Japan | 162,360 | 55,345 | — |
| Mainland China | 61,809 | 483,184 | 100,720 |
| Indonesia | 2,896 | 35,800 | 143 |
| Hong Kong | 18,755 | 302,184 | 19,826 |
| Others | 66,268 | 19,282 | — |
| Total | 774,710 | 1,020,770 | 120,724 |

No analysis of contribution to operating profit by geographical segment has been prepared as no contribution to operating profit from any of the above segments is substantially out of line with the ratio of profit to turnover.

Note: The turnover derived from Europe represents sales of toys for shipments directly to Europe under the instruction of these customers. The respective trade receivables are included in the United States of America, Japan and Hong Kong segments.



## 6 Other gains — net

| | 2006<br>HK$'000 | 2005<br>HK$'000 |
|---|---|---|
| Interest income | **617** | 472 |
| Derivative financial instruments: | | |
| — forward contracts and interest swaps: transactions not qualifying as hedges | **741** | — |
| Sample income | **1,680** | 466 |
| Other | **325** | 114 |
| | **3,363** | 1,052 |

## 7 Expenses by nature

Expenses included in cost of sales, selling and distribution costs, general and administrative expenses are analysed as follows:

| | 2006<br>HK$'000 | 2005<br>HK$'000<br>(restated) |
|---|---|---|
| Cost of inventories sold | **408,505** | 443,706 |
| Auditors' remuneration | **2,065** | 1,435 |
| Amortisation of goodwill | **—** | 1,633 |
| Provision for obsolete inventories | **574** | — |
| Amortisation of leasehold land and land use rights | **1,120** | 1,057 |
| Depreciation of property, plant and equipment | **43,474** | 45,755 |
| Loss on disposal of property, plant and equipment | **—** | 121 |
| Write-off/Impairment loss of other investments in unlisted shares overseas | **1,224** | 1,174 |
| Unrealised loss on listed trading securities | **—** | 1,515 |
| Loss on disposal of listed trading securities | **1,386** | 1,357 |
| Employee benefit expense (Note 13) | **115,798** | 106,391 |
| Operating lease rentals in respect of land and buildings | **5,573** | 5,746 |
| Net exchange losses | **4,568** | 8,501 |

## 8 Finance costs

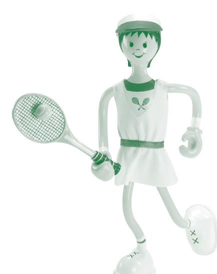
| | 2006<br>HK$'000 | 2005<br>HK$'000 |
|---|---|---|
| Interest on loans from banks and financial institutions and overdrafts | **22,947** | 9,514 |
| Arrangement fees on bank loans | **754** | 1,942 |
| | **23,701** | 11,456 |

## 9 Income tax credit/(expense)

Hong Kong profits tax has been provided at the rate of 17.5% (2005: 17.5%) on the estimated assessable profit for the year. Taxation on profits of Mainland China subsidiaries has been calculated on the estimated assessable profit for the year at the rates of taxation as applicable to the local subsidiaries.

The amount of tax credit/ (charge) to the consolidated income statement represents:

| | 2006<br>HK$'000 | 2005<br>HK$'000 |
|---|---|---|
| Current income tax | | |
| Hong Kong profits tax | | |
| — current year | **(1,687)** | (3,466) |
| — (under)/ overprovision in prior years | **(3)** | 80 |
| Mainland China enterprise income tax | | |
| — current | **(993)** | (1,695) |
| — overprovision in prior years | **1,370** | 176 |
| Deferred income tax (Note 30) | **1,878** | 733 |
| | **565** | (4,172) |



## 9 Income tax credit/(expense) *(Continued)*

The taxation on the Group's profit before income tax differs from the theoretical amount that would arise using the Hong Kong profits tax rate as follows:

| | **2006** | 2005 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| | | (Restated) |
| Profit before income tax | **(15,244)** | (24,377) |
| Calculated at a taxation rate of 17.5% (2005: 17.5%) | **(2,668)** | (4,266) |
| Effect of different taxation rates in other countries | **1,310** | 1,261 |
| Income not subject to taxation | **1,034** | 1,554 |
| Expenses not deductible for taxation purposes | **(3,882)** | (2,113) |
| Tax exemption | **3,808** | 4,377 |
| Tax losses not recognised | **(404)** | (5,241) |
| Overprovision in prior years | **1,367** | 256 |
| Tax credit/(expense) | **565** | (4,172) |

## 10 Profit attributable to equity holders of the Company

The consolidated profit attributable to equity holders of the Company includes a profit of approximately HK$21,216,000 (2005: loss of approximately HK$45,210,000), including dividend from a subsidiary of HK$21,000,000 (2005: HK$27,000,000), dealt with in financial statements of the Company.

## 11 Dividends

| | **2006** | 2005 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| Ordinary shares | | |
| Interim, of HK Nil cents (2005: HK$0.50 cents) per ordinary share | **—** | 2,419 |
| Final, proposed, of HK Nil cents (2005: HK$0.50 cents) per ordinary share | **—** | 2,419 |
| | **—** | 4,838 |

At a meeting held on 28 July 2006, the Board has resolved not to pay a final dividend for the year ended 31 March 2006.

## 12 Earnings per share

### Basic

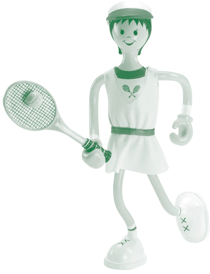
Basic earnings per share is calculated by dividing the profit attributable to equity holders of the Company by the weighted average number of ordinary shares in issue during the year.

| | 2006<br>HK$'000 | 2005<br>HK$'000<br>(Restated) |
|---|---|---|
| Profit attributable to equity holders of the Company | **16,673** | 20,165 |
| Weighted average number of ordinary shares in issue | **483,733,333** | 483,733,333 |
| Basic earnings per share (HK cents) | **3.45** | 4.17 |

### Diluted

Diluted earnings per share is calculated by adjusting the weighted average number of ordinary shares outstanding assuming conversion of all dilutive potential ordinary shares. The Company has one category of dilutive potential ordinary shares which is the share options granted to employees. For the share options, a calculation is done to determine the number of shares that could have been acquired at fair value (determined as the average annual market price of the Company's shares) based on the monetary value of the subscription rights attached to outstanding share options. The number of shares calculated as above is compared with the number of shares that would have been issued assuming the exercise of the share options.

There were no dilutive earnings per share for the year ended 31 March 2005 and 2006. The exercise of the outstanding share options would be anti-dilutive for the year ended 31 March 2005 while all the share options lapsed during the year ended 31 March 2006.



## 13 Employee benefit expense

Employee benefit expense excluding directors' emoluments comprises:

| | **2006** | 2005 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| Wages and salaries | **109,321** | 100,447 |
| Other staff benefits | **3,792** | 3,723 |
| Pension costs — defined contribution plans (Note 15) | **2,685** | 2,221 |
| | **115,798** | 106,391 |

## 14 Directors' and senior management's emoluments

### (a) Directors' emoluments

The aggregate amounts of emoluments paid and payable to the directors of the Company are as follows:

| | **2006** | 2005 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| Fees for independent non-executive directors | **180** | 150 |
| Fees for non-executive director | **60** | 60 |
| Other emoluments: | | |
| Basic salaries, bonus, housing allowances, other allowances and benefits in kind | **6,416** | 6,487 |
| Provident fund scheme contributions | **84** | 84 |
| | **6,740** | 6,781 |

No emoluments have been paid by the Group to the directors as an inducement to join or upon joining the Group or as compensation for loss of office during the year. No directors waived their emoluments in respect of the years ended 31 March 2006 and 2005.

## 14 Directors' and senior management's emoluments *(Continued)*

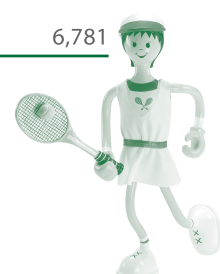
### (a) Directors' emoluments *(Continued)*

The remuneration of every Director of the year ended 31 March 2006 is as set out below:

| Name of Director | Fees | Basic salaries and bonus | Housing allowances, other allowances and benefits in kind | Employer's contribution to pension scheme | Total |
|---|---|---|---|---|---|
| Mr Leung Lun | — | 1,500 | 780 | 12 | 2,292 |
| Mr Leung Chun Ming | — | 1,567 | 576 | 12 | 2,155 |
| Mr Zhong Bing Quan | — | 324 | — | 12 | 336 |
| Ms Cheng Yun Tai | — | 589 | — | 12 | 601 |
| Mr Wong Tze On, Andy | — | 720 | 360 | 36 | 1,116 |
| Mr Wong Lam | 60 | — | — | — | 60 |
| Mr Ye Tian Liu | 60 | — | — | — | 60 |
| Mr Ko Peter, Ping Wah | 60 | — | — | — | 60 |
| Mr Lai Yun Hung | 60 | — | — | — | 60 |
| | 240 | 4,700 | 1,716 | 84 | 6,740 |

The remuneration of every Director for the year ended 31 March 2005 is set out below:

| Name of Director | Fees | Basic salaries and bonus | Housing allowances, other allowances and benefits in kind | Employer's contribution to pension scheme | Total |
|---|---|---|---|---|---|
| Mr Leung Lun | — | 1,545 | 780 | 12 | 2,337 |
| Mr Leung Chun Ming | — | 1,578 | 576 | 12 | 2,166 |
| Mr Zhong Bing Quan | — | 390 | — | 12 | 402 |
| Ms Cheng Yun Tai | — | 533 | — | 12 | 545 |
| Mr Wong Tze On, Andy | — | 735 | 350 | 36 | 1,121 |
| Mr Wong Lam | 60 | — | — | — | 60 |
| Mr Ye Tian Liu | 60 | — | — | — | 60 |
| Mr Ko Peter, Ping Wah | 60 | — | — | — | 60 |
| Mr Lai Yun Hung | 30 | — | — | — | 30 |
| | 210 | 4,781 | 1,706 | 84 | 6,781 |



## 14 Directors' and senior management's emoluments *(Continued)*

### (b) Five highest paid individuals

The five individuals whose emoluments were the highest in the Group for the year include four (2005: four) Directors whose emoluments are disclosed in the analysis presented above. The emoluments payable to the remaining one (2005: one) individual during the year are as follows:

| | **2006** | 2005 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| Basic salaries, housing allowances, other allowances and benefits in kind | **627** | 634 |
| Bonus | **18** | — |
| Provident fund scheme contributions | **33** | 31 |
| | **678** | 665 |

During the years ended 31 March 2006 and 2005, no share options were granted to the individuals under the Old Scheme to acquire ordinary shares in the Company, and no options were exercised by the afore-mentioned highest paid individuals.

The emoluments of the afore-mentioned one (2005: one) highest paid individual fell within the band of Nil to HK$1,000,000 for both years. The emoluments represent the amount paid to or receivable by the individuals in the respective financial years.

No emoluments were paid to the highest paid individual as an inducement to join the Group or as compensation for loss of office.

## 15 Provident fund scheme arrangements

The Group has two provident fund scheme arrangements for its Hong Kong employees: (a) the ORSO Scheme and (b) the MPF Scheme.

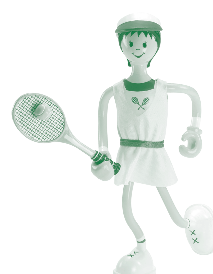
The ORSO Scheme has been granted an exemption from registration for MPF purposes. Under the ORSO Scheme, contributions of both the employers and employees are calculated at 5% of the monthly salary of the employees. The employees are entitled to all the employers' contributions after 10 years of completed service, or at a reduced scale after completion of 3 to 9 years' service. Forfeited contributions are used to reduce the employers' contributions.

Under the MPF Scheme, contributions amounting to 5% of the employee's relevant income, as defined in the MPF Ordinance, up to a maximum of HK$1,000 are respectively made by the Group and the employees. The contributions are fully and immediately vested in the employees as accrued benefits once they are paid to the approved trustee of the MPF Scheme.

The Group contributes to certain defined contribution schemes for its employees in Mainland China, Indonesia and the United States of America. Contributions are made at a certain percentage of the basic salaries of employees.

The total amount of retirement benefit costs charged to the Group's income statement for the year ended 31 March 2006 was HK$2,685,000 (2005: HK$2,221,000).

At 31 March 2006 and 2005 no forfeited contributions are available to offset future contributions of the Group to the ORSO Scheme. The unvested benefits so utilised under the ORSO Scheme during the year ender 31 March 2006 was HK$27,000 (2005: HK$60,000).



## 16 Intangible assets

| | Group | | |
|---|---|---|---|
| | **Club memberships** HK$'000 (Note) | **Goodwill** HK$'000 | **Total** HK$'000 |
| At 1 April 2004 | | | |
| Cost | — | 24,488 | 24,488 |
| Accumulated amortisation and impairment | — | (3,615) | (3,615) |
| Net book amount | — | 20,873 | 20,873 |
| Year ended 31 March 2005 | | | |
| Opening net book amount | — | 20,873 | 20,873 |
| Amortisation expense (Note 7) | — | (1,633) | (1,633) |
| Closing net book amount | — | 19,240 | 19,240 |
| At 31 March 2005 | | | |
| Cost | — | 24,488 | 24,488 |
| Accumulated amortisation and impairment | — | (5,248) | (5,248) |
| Net book amount | — | 19,240 | 19,240 |
| Year ended 31 March 2006 | | | |
| Opening net book amount and closing net book amount | 2,474 | 19,240 | 21,714 |
| At 31 March 2006 | | | |
| Cost | 2,474 | 19,240 | 21,714 |
| Accumulated amortisation and impairment | — | — | — |
| Net book amount | 2,474 | 19,240 | 21,714 |

Note:

As a result of the adoption of HKAS 38, club memberships amounted to approximately HK$2,474,000 were reclassified from other investments to intangible assets at 1 April 2005.

## 16 Intangible assets *(Continued)*

### Impairment tests for goodwill

Goodwill is allocated to the Group's cash-generating units (CGUs) identified according to country and business segment.

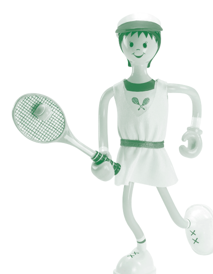
As at 31 March 2006, the Group's goodwill is allocated to the toys trading business in the United States.

The recoverable amount of a CGU is determined based on value-in-use calculations. These calculations use cash flow projections based on financial budgets approved by management covering a ten-year period. The growth rate does not exceed the long-term average growth rate for the toys business in which the CGU operates.

Key assumptions used for value-in-use calculations:

| | **United States of America** |
|---|---|
| Growth rate | 3% |
| Discount rate | 8% |

Management determined growth rate based on past performance and its expectations for the market development. The discount rate used are pre-tax and reflect specific risks relating to the relevant segments.



## 17 Leasehold land and land use rights

The Group's interests in leasehold land and land use rights represent prepaid operating lease payments and their net book value are analysed as follows:

| | Group | |
|---|---|---|
| | **2006** | 2005 |
| | **HK$'000** | HK$'000 |
| In Mainland China, held on: | | |
| Land use rights of over 50 years | **5,419** | 5,502 |
| Land use rights of between 10 to 50 years | **22,223** | 22,793 |
| In Hong Kong, held on: | | |
| Land use rights of between 10 to 50 years | **19,816** | 20,283 |
| | **47,458** | 48,578 |

| | Group | |
|---|---|---|
| | **2006** | 2005 |
| | **HK$'000** | HK$'000 |
| Opening balance | **48,578** | 45,384 |
| Additions | **—** | 4,251 |
| Amortisation | **(1,120)** | (1,057) |
| Closing balance | **47,458** | 48,578 |

## 18 Property, plant and equipment — Group

| | Group | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Freehold land and buildings HK$'000 | Leasehold improvements HK$'000 | Plant and machinery HK$'000 | Furniture, fixtures and equipment HK$'000 | Motor vehicles HK$'000 | Moulds HK$'000 | Construction in progress HK$'000 | Total HK$'000 |
| At 1 April 2004 | | | | | | | | |
| Cost or valuation | 54,211 | 96,353 | 160,798 | 27,287 | 6,809 | 148,656 | — | 494,114 |
| Accumulated deprecation | — | (28,818) | (120,850) | (21,181) | (4,235) | (89,028) | — | (264,112) |
| Net book amount | 54,211 | 67,535 | 39,948 | 6,106 | 2,574 | 59,628 | — | 230,002 |
| Year ended 31 March 2005 | | | | | | | | |
| Opening net book amount | 54,211 | 67,535 | 39,948 | 6,106 | 2,574 | 59,628 | — | 230,002 |
| Exchange differences | (1,345) | — | (142) | (4) | — | — | — | (1,491) |
| Additions | 945 | 296 | 9,476 | 1,287 | 1,221 | 13,841 | 89,407 | 116,473 |
| Disposals | — | (89) | — | — | (156) | — | — | (245) |
| Depreciation | (1,663) | (7,053) | (15,022) | (2,026) | (751) | (19,240) | — | (45,755) |
| Closing net book amount | 52,148 | 60,689 | 34,260 | 5,363 | 2,888 | 54,229 | 89,407 | 298,984 |
| At 31 March 2005 | | | | | | | | |
| Cost or valuations | 53,811 | 96,470 | 169,570 | 28,462 | 7,825 | 162,497 | 89,407 | 608,042 |
| Accumulated depreciation | (1,663) | (35,781) | (135,310) | (23,099) | (4,937) | (108,268) | — | (309,058) |
| Net book amount | 52,148 | 60,689 | 34,260 | 5,363 | 2,888 | 54,229 | 89,407 | 298,984 |
| Year ended 31 March 2006 | | | | | | | | |
| Opening net book amount | 52,148 | 60,689 | 34,260 | 5,363 | 2,888 | 54,229 | 89,407 | 298,984 |
| Exchange differences | 1,241 | 1,591 | 531 | 127 | 34 | 161 | 1,579 | 5,264 |
| Additions | — | 4,538 | 4,059 | 1,143 | 1,981 | 25,912 | 86,466 | 124,099 |
| Revaluation surplus | 2,536 | — | — | — | — | — | — | 2,536 |
| Depreciation | (1,118) | (7,197) | (11,693) | (2,055) | (898) | (20,513) | — | (43,474) |
| Closing net book amount | 54,807 | 59,621 | 27,157 | 4,578 | 4,005 | 59,789 | 177,452 | 387,409 |
| At 31 March 2006 | | | | | | | | |
| Cost or valuation | 56,847 | 103,783 | 177,886 | 29,999 | 9,754 | 190,134 | 177,452 | 745,855 |
| Accumulated deprecation | (2,040) | (44,162) | (150,729) | (25,421) | (5,749) | (130,345) | — | (358,446) |
| Net book amount | 54,807 | 59,621 | 27,157 | 4,578 | 4,005 | 59,789 | 177,452 | 387,409 |

The Group's freehold land and buildings were revalued at 31 March 2006. Valuations were made on the basis of open market value carried out by RHL Appraisal Ltd. and Satyatama Graha Tara, independent firms of professional valuers.

## 19 Investments in subsidiaries

| | Company 2006 HK$'000 | 2005 HK$'000 |
|---|---|---|
| Unlisted investments, at cost | **115,801** | 115,801 |
| Amounts due from subsidiaries (Note) | **493,431** | 412,369 |
| Less: provision for impairment loss | **(74,000)** | (74,000) |
| | **419,431** | 338,369 |
| | **535,232** | 454,170 |

Note

The amounts are due from certain wholly-owned subsidiaries. They are unsecured and will not be demanded for repayment within the next twelve months from 31 March 2006. Out of the total amount, HK$300,000,000 (2005: HK$240,000,000 is interest bearing at Hong Kong Interbank Offered Rate plus 0.735% per annum) is interest bearing at Hong Kong Interbank Offered Rate plus 0.735% per annum, while the remaining balance is interest-free.

Particulars of the subsidiaries of the Company at 31 March 2006 are as follows:

| Name of company | Place of incorporation and operations | Particulars of issued share capital/ registered capital | Effective percentage holding 2006 | Effective percentage holding 2005 | Nature of business |
|---|---|---|---|---|---|
| Shares held directly: | | | | | |
| Lung Cheong (BVI) Holdings Limited | British Virgin Islands | Ordinary US$130,660 | **100** | 100 | Investment holding |

## 19 Investments in subsidiaries *(Continued)*

| Name of company | Place of incorporation and operations | Particulars of issued share capital/ registered capital | Effective percentage holding 2006 | 2005 | Nature of business |
|---|---|---|---|---|---|
| **Shares/investments held indirectly:** | | | | | |
| Dongguan Lung Cheong Plastic Products Co., Ltd. (Note) | Mainland China | HK$6,500,000 | **100** | 100 | Manufacture and trading of toys |
| Dongguan Lung Cheong Toys Co., Ltd. (Note) | Mainland China | HK$124,030,000 | **100** | 100 | Manufacture of toys |
| Dongguan Standard Tooling and Products Co., Ltd. (Note) | Mainland China | HK$7,700,000 | **100** | 100 | Manufacture of moulds |
| L C Technology Limited | Hong Kong | Ordinary HK$10,000 | **100** | 100 | Trading of consumer electronic products |
| Lung Cheong Resources Management Limited | Hong Kong | Deferred HK$10,000<br>Ordinary HK$2 | **100** | 100 | Management services |
| Kid Galaxy Limited | Hong Kong | Ordinary HK$10,000 | **100** | 100 | Trading of toys |
| Lung Cheong Overseas Corporation | British Virgin Islands | Ordinary US$50,000 | **100** | 100 | Trading of toys |
| Lung Cheong Toys Limited | Hong Kong | Deferred HK$1,000,000<br>Ordinary HK$2 | **100** | 100 | Trading of toys |

# Notes
## to the Consolidated Financial Statements

## 19 Investments in subsidiaries *(Continued)*

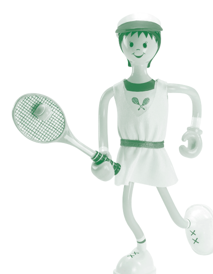
| Name of company | Place of incorporation and operations | Particulars of issued share capital/ registered capital | Effective percentage holding | | Nature of business |
|---|---|---|---|---|---|
| | | | **2006** | 2005 | |
| **Shares/investments held indirectly:** *(Continued)* | | | | | |
| Dongguan L C Technology Co., Ltd. (Note) | Mainland China | HK$3,500,000 | **100** | 100 | Manufacture of consumer electronic products |
| PT. Lung Cheong Brothers Industrial | Republic of Indonesia | Rupiah 5,728,000,000 | **60** | 60 | Manufacture of plastic and electronic products |
| Standard Tooling and Products Co. Ltd. | Hong Kong | Ordinary HK$3,000,000 | **100** | 100 | Engineering services and mould trading |
| Kid Galaxy Corporation | British Virgin Islands | Ordinary US$10 | **100** | 100 | Trading of toys |
| Kid Galaxy Inc. | United States of America | Ordinary US$100,010 | **100** | 100 | Trading of toys |
| Lung Cheong Entertainment Limited | British Virgin Islands | Ordinary US$1 | **100** | 100 | Licensing and development of content |
| Fericle Holdings Limited | British Virgin Islands | Ordinary US$1 | **100** | 100 | Investment holding |

## 19 Investments in subsidiaries *(Continued)*

| Name of company | Place of incorporation and operations | Particulars of issued share capital/ registered capital | Effective percentage holding 2006 | Effective percentage holding 2005 | Nature of business |
|---|---|---|---|---|---|
| **Shares/investments held indirectly:** *(Continued)* | | | | | |
| Liberal Cultural Studies Limited | Hong Kong | Ordinary HK$10,000 | **100** | 100 | Development of animation and publication |
| Inspired Motion Technology Limited | British Virgin Islands | Ordinary US$256,666 | **54** | — | Investment holdings & development of integrated circuit |
| Inspired Motion Technology (HK) Limited | Hong Kong | Ordinary HK$10,000 | **100** | — | Trading of integrated circuit |

Note:

These companies are wholly foreign-owned enterprises established in Mainland China. They adopt 31 December as their accounting year end date pursuant to the local regulations. Accordingly, the management accounts of these subsidiaries as at and for the twelve months ended 31 March have been incorporated in the group financial statements after making adjustments as the directors considered appropriate for compliance with Hong Kong Financial Reporting Standards ("HKFRS"), issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA").



## 20 Available-for-sale financial assets

| | Group | |
|---|---|---|
| | **2006** | 2005 |
| | **HK$'000** | HK$'000 |
| At the beginning of the year (Note) | **28,238** | — |
| Impairment loss | **(135)** | — |
| At the end of the year | **28,103** | — |

Note:

As a result of the adoption of HKAS 38, investments in life insurance contracts amounted to approximately HK$28,238,000 were reclassified from other investments to available-for-sale financial assets at 1 April 2005.

Available-for-sale financial assets included the followings:

| | Group |
|---|---|
| | **2006** |
| | **HK$'000** |
| Investments in life insurance contracts (Note) | **28,103** |

Note:

The Group purchased three life insurance contracts on October 2002 for each of the following three Executive Directors, namely Mr. Leung Lun, Mr. Leung Chung Ming and Mr. Wong Tze On, Andy.

The total insured amount is approximately US$25 million (approximately HK$195 million). Each of the contract will mature on the date when the insured reaches the age of 100 or death of the insured, whichever is earlier. At time of death of the insured, 50% of the insured amount will be payable to the Group and 50% to the beneficiary of the respective insured.

The total premium paid is financed by a renewable bank loan of approximately HK$26,988,000, which is interest-bearing at 1% plus the bank's cost of fund and secured by the three life insurance contracts and a corporate guarantee executed by the Company.

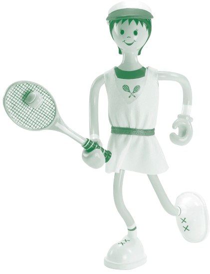
The carrying amount at 31 March 2006 represents the cash surrender value of these insurance contracts as at the balance sheet date.

## 21 Other investments

| | Group 2006 HK$'000 | Group 2005 HK$'000 |
|---|---|---|
| At cost | | |
| Unlisted shares overseas | — | 2,398 |
| Club memberships | — | 2,474 |
| Investments in life insurance contracts | — | 28,238 |
| | — | 33,110 |
| Less: impairment loss | — | (1,174) |
| | — | 31,936 |

## 22 Inventories

| | Group 2006 HK$'000 | Group 2005 HK$'000 |
|---|---|---|
| Raw materials | **100,349** | 159,948 |
| Work-in-progress | **53,880** | 28,394 |
| Finished goods | **34,066** | 36,388 |
| | **188,295** | 224,730 |



## 23 Trade and other receivables

The carrying amounts of trade and other receivables are as follows:

| | Group | | Company | |
|---|---|---|---|---|
| | **2006** | 2005 | **2006** | 2005 |
| | **HK$'000** | HK$'000 | **HK$'000** | HK$'000 |
| Trade receivables | **187,043** | 182,901 | **—** | — |
| Other receivables, deposits and prepayments | **67,379** | 34,651 | **1,553** | 2,210 |
| | **254,422** | 217,552 | **1,553** | 2,210 |

The carrying amounts of trade receivables, other receivables, deposits and prepayments approximate their fair values.

At 31 March 2006, the ageing analysis of the trade receivables was as follows:

| | Group | |
|---|---|---|
| | **2006** | 2005 |
| | **HK$'000** | HK$'000 |
| 0 -30 days | **88,480** | 64,708 |
| 31-60 days | **17,813** | 31,209 |
| 61-90 days | **21,660** | 34,620 |
| 91-180 days | **53,257** | 35,532 |
| 181-365 days | **3,856** | 13,244 |
| Over 365 days | **1,977** | 3,588 |
| | **187,043** | 182,901 |

The Group's sales are on letter of credit or open account terms. Credit terms are reviewed on a regular basis. The normal trade term is between 30 to 90 days but business partners with strong financial background may be offered longer credit terms.

## 23 Trade and other receivables *(Continued)*

Trade receivables were denominated in the following currencies:

| | Group | |
|---|---|---|
| | **2006** | 2005 |
| | **HK$'000** | HK$'000 |
| Hong Kong dollars | **32,310** | 23,578 |
| Chinese Renminbi | **6,347** | 8,904 |
| United States dollars | **148,285** | 149,671 |
| Indonesian Rupiah | **101** | 748 |
| | **187,043** | 182,901 |

## 24 Derivative financial instruments

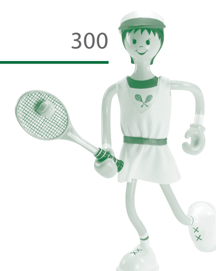
| | Group 2006 | |
|---|---|---|
| | **Assets** | **Liabilities** |
| | **HK$'000** | **HK$'000** |
| Interest-rate swaps — not qualifying as hedges | **—** | **105** |
| Forward foreign exchange contracts — not qualifying as hedges (Note) | **450** | **—** |
| | **450** | **105** |

Note:

Please refer to Note 35(c) for the commitments under these contracts as at 31 March 2006.

## 25 Cash and cash equivalents

| | Group | | Company | |
|---|---|---|---|---|
| | **2006** | 2005 | **2006** | 2005 |
| | **HK$'000** | HK$'000 | **HK$'000** | HK$'000 |
| Cash at bank and in hand | **53,102** | 97,969 | **101** | 300 |
| Short term bank deposits | **36,650** | 70,700 | **—** | — |
| | **89,752** | 168,669 | **101** | 300 |



## 25 Cash and cash equivalents *(Continued)*

Included in cash and cash equivalents of the Group as at 31 March 2006 were approximately HK$75,262,000 (2005: approximately HK$72,224,000) denominated in Renminbi. Renminbi is not a freely convertible currency.

The effective interest rate on short-term bank deposits was 1.7% (2005: 1.2%); these deposits have an average maturity of 90 days.

## 26 Share capital

| | **Authorised** | | | |
|---|---|---|---|---|
| | **Convertible cumulative redeemable preference shares of US$100,000 each** | | **Ordinary shares of HK$0.10 each** | |
| | No. of Shares | US$'000 | No. of Shares (thousands) | HK$'000 |
| At 31 March 2005 and 2006 | 40 | 4,000 | 1,000,000 | 100,000 |

| | **Issued and fully paid** | | | |
|---|---|---|---|---|
| | **Convertible cumulative redeemable preference shares of US$100,000 each** | | **Ordinary shares of HK$0.10 each** | |
| | No. of Shares | HK$'000 (equivalent) | No. of Shares (thousands) | HK$'000 |
| At 31 March 2005 and 2006 | — | — | 483,733 | 48,373 |

(a) There are no movements in the authorised share capital of the Company during the year.

(b) On 8 September 1997, a share option scheme (the "Old Scheme") was approved by the shareholders of the Company under which its Directors may, at their discretion, invite employees of the Group including any Executive Directors to take up options to subscribe for ordinary shares of HK$0.1 each in the Company subject to the terms and conditions stipulated therein.

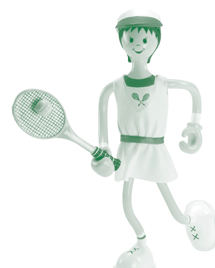
## 26 Share capital *(Continued)*

On 3 September 2002, the shareholders of the Company approved the termination of the Old Scheme and the adoption of a new scheme ("2002 Scheme") as a result of the amendments of Chapter 17 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules"). Upon termination of the Old Scheme, no further options can be granted thereunder but in all other respects, the provisions of the Old Scheme shall remain in force and all share options granted prior to such termination shall continue to be valid and exercisable in accordance therewith.

Under the 2002 Scheme, share options can be exercised at any time during the periods to be determined and notified by the Directors of the Company to the grantees at the time of making offers to grant share options to them, provided that such periods shall not exceed the period of ten years from the date of grant. The maximum number of shares available for issue under the 2002 Scheme is 28,940,000, representing approximately 6% of the issued share capital of the Company as at the date of this report. The subscription price for the shares under the 2002 Scheme shall be a price determined by the Directors at its discretion, provided that it shall not less than the higher of (i) the closing price of the shares stated in the daily quotation sheets of The Stock Exchange of Hong Kong Limited ("Stock Exchange") on the date of grant and (ii) the average closing price of the shares stated in the Stock Exchange's daily quotation sheets for the five business days immediately preceding the date of grant of share options. A nominal consideration of HK$1 is payable for each of the share options granted.

Movements in the number of share options outstanding and their related weighted average exercise prices are as follows:

| | **2006** | | 2005 | |
|---|---|---|---|---|
| | **Average exercise price in HK$ per share** | **Number of Options** | Average exercise price in HK$ per share | Number of Options |
| At 1 April | **0.675** | **10,800,000** | 0.675 | 10,800,000 |
| Lapsed | **0.675** | **(10,800,000)** | — | — |
| At 31 March | **—** | **—** | 0.675 | 10,800,000 |



## 26 Share capital *(Continued)*

Note

Share options outstanding at the end of the year have the following terms:

| Expiry date | Exercise price HK$ | **2006 Number of options** | 2005 Number of options |
|---|---|---|---|
| Directors | | | |
| 30 September 2005 | 0.675 | — | 10,000,000 |
| Other employees | | | |
| 30 September 2005 | 0.675 | — | 800,000 |
| | | — | 10,800,000 |

## 27 Reserves

| | Group | | | | | | Company | |
|---|---|---|---|---|---|---|---|---|
| | Other reserves | | | | | | | |
| | Share premium HK$'000 | Exchange fluctuation reserve HK$'000 | Capital reserve HK$'000 | Buildings revaluation reserve HK$'000 | Total HK$'000 | Retained profits HK$'000 | Share Premium HK$'000 | (Accumulated losses)/ Retained profits HK$'000 |
| **At 1 April 2005**, as below | 112,967 | (48,931) | 27,828 | 18,604 | 110,468 | 256,739 | 200,268 | (33,151) |
| Opening adjustment on adoption of HKAS 39 (Note 2 (a)(iii)) | — | — | — | — | — | (396) | — | — |
| **At 1 April 2005, after opening adjustment** | 112,967 | (48,931) | 27,828 | 18,604 | 110,468 | 256,343 | 200,268 | (33,151) |
| Currencies translation difference | — | 6,475 | — | — | 6,475 | — | — | — |
| Surplus on property revaluation | — | — | — | 2,536 | 2,536 | — | — | — |
| Transfer to capital reserve | — | — | 696 | — | 696 | (696) | — | — |
| Profit for the year | — | — | — | — | — | 16,673 | — | 21,216 |
| 2004/05 final dividend paid | (2,419) | — | — | — | (2,419) | — | (2,419) | — |
| At 31 March 2006 | 110,548 | (42,456) | 28,524 | 21,140 | 117,756 | 272,320 | 197,849 | (11,935) |

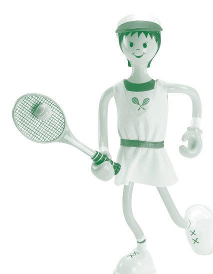
## 27 Reserves *(Continued)*

| | Group | | | | | | Company | |
|---|---|---|---|---|---|---|---|---|
| | Other reserves | | | | | | | |
| | Share premium | Exchange fluctuation reserve | Capital reserve | Buildings revaluation reserve | Total | Retained profits | Share Premium | (Accumulated losses)/ Retained profits |
| | HK$'000 | HK$'000 | HK$'000 | HK$'000 | HK$'000 | HK$'000 | HK$'000 | HK$'000 |
| **At 1 April 2004** | | | | | | | | |
| As previously reported | 112,967 | (52,066) | 27,081 | 22,485 | 110,467 | 230,857 | 200,268 | 18,106 |
| Effect on adoption of HKAS 17 (Note 2(a)(i)) | — | — | — | (3,881) | (3,881) | 12,511 | — | — |
| **At 1 April 2004, as restated** | 112,967 | (52,066) | 27,081 | 18,604 | 106,586 | 243,368 | 200,268 | 18,106 |
| Currencies translation differences | — | 3,135 | — | — | 3,135 | — | — | — |
| Transfer to capital reserve | — | — | 747 | — | 747 | (747) | — | — |
| Profit/(loss) for the year | — | — | — | — | — | 20,165 | — | (45,210) |
| 2003/04 final dividend paid | — | — | — | — | — | (3,628) | — | (3,628) |
| 2004/05 interim dividend paid | — | — | — | — | — | (2,419) | — | (2,419) |
| **At 31 March 2005** | 112,967 | (48,931) | 27,828 | 18,604 | 110,468 | 256,739 | 200,268 | (33,151) |

Note:

(i) Under the Companies Law (Revised) Chapter 22 of the Cayman Islands, share premium of the Company is available for paying distributions and dividends to shareholders subject to the provisions of its Memorandum and Articles of Association and provided that immediately following the distributions or dividend payments, the Company is able to pay its debts as they fall due in the ordinary course of business.

(ii) The capital reserve represents transfers made to the statutory reserve fund set up by subsidiaries, which are wholly foreign-owned investment enterprises in Mainland China, pursuant to the local regulations. According to the regulations, the reserve fund may be used for making up losses, if any, and increasing capital.



## 28 Borrowings

| | Group | | Company | |
|---|---|---|---|---|
| | **2006** | 2005 | **2006** | 2005 |
| | **HK$'000** | HK$'000 | **HK$'000** | HK$'000 |
| **Non-current** | | | | |
| Loans from banks and financial institutions | **—** | 240,000 | **—** | 240,000 |
| **Current** | | | | |
| Trust receipt loans | **57,306** | 95,902 | **—** | — |
| Loans from banks and financial institutions | **414,986** | 133,323 | **300,000** | — |
| **Total borrowings** | **472,292** | 469,225 | **300,000** | 240,000 |

At 31 March 2006, the borrowings were repayable as follows:

| | Group | | Company | |
|---|---|---|---|---|
| | **2006** | 2005 | **2006** | 2005 |
| | **HK$'000** | HK$'000 | **HK$'000** | HK$'000 |
| Within one year | **472,292** | 229,225 | **300,000** | — |
| In the second year | **—** | 81,600 | **—** | 81,600 |
| In the third to fifth years | **—** | 158,400 | **—** | 158,400 |
| | **472,292** | 469,225 | **300,000** | 240,000 |

The current portion of the borrowings included bank loan amounted to approximately HK$218,400,000 repayable on 30 June 2008. Such amount has been reclassified as current liabilities as a result of the Group's breach of certain financial covenants of a long-term bank loan agreement as at 31 March 2006. The Group obtained waivers from the relevant banks in respect of such non-compliance subsequent to the balance sheet date.

## 28 Borrowings *(Continued)*

The effective interest rates at the balance sheet were as follows:

| | 2006 | | 2005 | |
|---|---|---|---|---|
| | **HKD** | **USD** | HKD | USD |
| Bank borrowings | **4.3%** | **4.8%** | 1.9% | 2.8% |

The carrying amounts of the borrowings approximate their fair value.

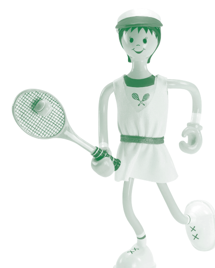
The carrying amounts of the borrowings are denominated in the following currencies:

| | Group | | Company | |
|---|---|---|---|---|
| | **2006** | 2005 | **2006** | 2005 |
| | **HK$'000** | HK$'000 | **HK$'000** | HK$'000 |
| Hong Kong dollars | **445,306** | 432,502 | **300,000** | 240,000 |
| United States dollars | **26,986** | 36,723 | **—** | — |
| | **472,292** | 469,225 | **300,000** | 240,000 |

## 29 Provision for long service payment

| | Group |
|---|---|
| | **HK$'000** |
| At 1 April 2005 | **971** |
| Additional provisions | **225** |
| At 31 March 2006 | **1,196** |

The amount represents provision for long service payment for the Group's employees in Indonesia.



## 30 Deferred income tax

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income taxes relate to the same fiscal authority. The balances shown in the balance sheet are, after appropriate offsetting, as follows:

| | Group | |
|---|---|---|
| | **2006** | 2005 |
| | **HK$'000** | HK$'000 |
| Deferred income tax assets: | | |
| — Deferred income tax assets to be recovered after more than 12 months | **4,872** | 1,055 |
| Deferred income tax liabilities: | | |
| — Deferred income tax liabilities to be settled after more than 12 months | **(13,366)** | (11,427) |
| Net deferred income tax liabilities | **(8,494)** | (10,372) |

The gross movements in deferred income tax assets/(liabilities) are as follow:

| | Group | |
|---|---|---|
| | **2006** | 2005 |
| | **HK$'000** | HK$'000 |
| At 1 April | **(10,372)** | (11,105) |
| Credited to the income statement (Note 9) | **1,878** | 754 |
| Exchange differences | **—** | (21) |
| At 31 March | **(8,494)** | (10,372) |

The movement in deferred tax assets and liabilities during the year, without taking into consideration the offsetting of balances within the same tax jurisdiction, is as follows,

## 30 Deferred income tax *(Continued)*

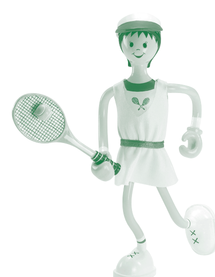
Deferred tax assets:

| | Group |
|---|---|
| | **Cumulative tax losses** |
| | HK$'000 |
| At 1 April 2004 | 2,718 |
| Charged to the income statement | (1,663) |
| At 31 March 2005 and 1 April 2005 | 1,055 |
| Credited to the income statement | 3,817 |
| At 31 March 2006 | 4,872 |

Deferred tax liabilities:

| | Group | | | |
|---|---|---|---|---|
| | **Accelerated depreciation** | **Revaluation of properties** | **Others** | **Total** |
| | HK$'000 | HK$'000 | HK$'000 | HK$'000 |
| At 1 April 2004 | 8,216 | 5,568 | 39 | 13,823 |
| Credited to the income statement | (2,026) | (352) | (39) | (2,417) |
| Exchange differences | 21 | — | — | 21 |
| At 31 March 2005 and 1 April 2005 | 6,211 | 5,216 | — | 11,427 |
| Charged to the income statement | 1,260 | 679 | — | 1,939 |
| At 31 March 2006 | 7,471 | 5,895 | — | 13,366 |

Deferred income tax assets are recognised for tax loss carry-forwards to the extent that the realisation of the related tax benefit through future taxable profits is probable. The Group did not recognise deferred income tax assets of approximately HK$4,787,000 (2005: approximately HK$4,563,000) in respect of losses amounting to approximately HK$14,731,000 (2005: approximately HK$13,421,000) that can be carried forward against future taxable income. Losses amounting to approximately HK$12,425,000 (2005: approximately HK$12,425,000) will expire from 2022 to 2025.



## 31 Trade and other payables and accrued charges

| | Group | | Company | |
|---|---|---|---|---|
| | **2006** | 2005 | **2006** | 2005 |
| | **HK$'000** | HK$'000 | **HK$'000** | HK$'000 |
| Trade payables | **46,592** | 66,920 | **—** | — |
| Other payables and accrued charges | **45,492** | 46,892 | **2,924** | 1,190 |
| | **92,084** | 113,812 | **2,924** | 1,190 |

The carrying amounts of trade payables, other payables and accrued charges approximate their fair values.

At 31 March 2006, the ageing analysis of the trade payables were as follows:

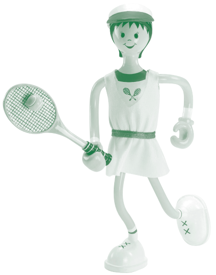
| | Group | |
|---|---|---|
| | **2006** | 2005 |
| | **HK$'000** | HK$'000 |
| 0 -30 days | **18,189** | 21,410 |
| 31-60 days | **10,563** | 14,380 |
| 61-90 days | **6,585** | 13,173 |
| 91-180 days | **10,285** | 16,274 |
| 181-365 days | **853** | 1,324 |
| Over 365 days | **117** | 359 |
| | **46,592** | 66,920 |

Trade payables were denominated in the following currencies:

| | Group | |
|---|---|---|
| | **2006** | 2005 |
| | **HK$'000** | HK$'000 |
| Hong Kong dollars | **25,614** | 36,544 |
| Chinese Renminbi | **11,654** | 15,722 |
| United States dollars | **8,974** | 13,838 |
| Japanese Yen | **307** | 784 |
| Indonesian Rupiah | **43** | 32 |
| | **46,592** | 66,920 |

## 32 Cash generated from operations

| | Group | |
|---|---|---|
| | **2006** | 2005 |
| | **HK$'000** | HK$'000 |
| | | (Restated) |
| Profit before income tax | **15,244** | 24,337 |
| Adjustments for: | | |
| — Interest income | **(617)** | (472) |
| — Interest expense | **22,947** | 9,514 |
| — Arrangement fees on bank loans | **754** | 1,942 |
| — Loss on disposal of property, plant and equipment | **—** | 121 |
| — Depreciation of property, plant and equipment | **43,474** | 45,755 |
| — Provision for long service payment | **225** | — |
| — Amortisation of goodwill | **—** | 1,633 |
| — Amortisation of leasehold land and land use rights | **1,120** | 1,057 |
| — Write-off/impairment loss of other investments | **1,224** | 1,174 |
| — Loss on disposal of trading securities | **1,386** | 1,357 |
| — Unrealised loss on trading securities | **—** | 1,515 |
| — Decrease in cash surrender value of life insurance contracts | **135** | 25 |
| — Fair value gain on derivative financial instruments | **(741)** | — |
| Changes in working capital: | | |
| — Inventories | **36,435** | (33,422) |
| — Trade and other receivables | **(36,870)** | (34,244) |
| — Trade and other payables and accrued charges | **(21,728)** | 19,672 |
| — Trust receipt bank loans | **(38,596)** | 12,099 |
| Cash generated from operations | **24,392** | 52,063 |



## 33 Contingent liabilities

At 31 March 2006, the Group had no contingent liabilities. At 31 March 2005, the Group had contingent liabilities not provided for in the financial statements as follows:

| | Group | |
|---|---|---|
| | **2006** | 2005 |
| | **HK$'000** | HK$'000 |
| Shipping guarantee | **—** | 318 |

## 34 Banking and other facilities

At 31 March 2006, the Group had a total banking and other facilities of approximately HK$861,000,000 (2005: approximately HK$787,967,000), of which the following had been utilised:

(a) an outstanding bank loan of US$3,460,000 (approximately HK$26,988,000) (2005: US$3,753,000 (approximately HK$29,277,000)) for financing the lump sum payments for premiums of the three life insurance contracts. The bank loan is secured by the three life insurance contracts with a combined death benefit of approximately US$25 million (approximately HK$195 million) and a corporate guarantee executed by the Company;

(b) a syndication loan of HK$300,000,000 (2005: HK$240,000,000); and

(c) general banking facilities of approximately HK$145,304,000 (2005: approximately HK$170,671,000).

These general banking facilities are all supported by a corporate guarantee executed by the Company.

## 35 Commitments

### (a) Capital commitment for leasehold land and buildings

| | Group | |
|---|---|---|
| | **2006** | 2005 |
| | **HK$'000** | HK$'000 |
| Contracted but not provided for | **109** | 17,398 |

### (b) Commitments under operating leases

At 31 March 2006, the Group had future aggregate minimum lease payments under non-cancellable operating leases in respect of land and buildings as follows:

| | Group | |
|---|---|---|
| | **2006** | 2005 |
| | **HK$'000** | HK$'000 |
| Not later than one year | **3,812** | 4,224 |
| Later than one year and not later than five years | **12,673** | 12,651 |
| Over five years | **5,291** | 4,362 |
| | **21,776** | 21,237 |

### (c) Commitments under forward foreign currency contracts

As at 31 March 2006, the Group had maximum outstanding forward foreign currency contracts to purchase approximately US$109,500,000 (2005: approximately US$58,500,000) for approximately HK$854,100,000 (2005: approximately HK$456,300,000).

## 36 Related party transactions

Key management compensation

The aggregate amounts of emoluments paid or payable to key management of the Company are as follows:

| | **2006** | 2005 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| Fees | **240** | 210 |
| Other emoluments: | | |
| Basis salaries, bonus, housing allowances, other allowances and benefits in kind | **6,416** | 6,487 |
| Provident fund scheme contributions | **84** | 84 |
| | **6,740** | 6,781 |

## 37 Ultimate holding company

The Directors regard Rare Diamond Limited, a company incorporated in the British Virgin Islands, as being the ultimate holding company.