

BUSINESS REVIEW

For the six months ended 30 June 2006, the Group's turnover and net loss were approximately HK\$33.3 million (2005: HK\$20.3 million) and HK\$4.4 million (2005: HK\$5.8 million), respectively. Basic loss per share for the period was HK0.20 cent (2005: HK0.26 cent). The Board has resolved not to pay any interim dividend for the period (2005: Nil).

For the period under review, revenue from toys and decorative gift items was approximately HK\$18.2 million and HK\$15.1 million (2005: approximately HK\$11.5 million and HK\$8.8 million), respectively, accounting for approximately 55% and 45% of the Group's total turnover, respectively.

For the first half of 2006, the Group continues to engage in the design, manufacture and sale of toys and decorative gift items on an OEM and ODM basis and under the Group's own brandnames KCARE and KITECH. During the period, the Group has experienced improved sales of its toy and gift products as compared with the same period in 2005. Such increase in sales is a result of the improvement of the global economy and the increased marketing effort of the Group. In addition, as Miracles For Fun (HK) Limited ("MFF") has become a subsidiary of the Group in December 2005, the consolidation of the results of MFF has also contributed to the increase in revenue for the period.

The Group generally finances its operations with internally generated cash flow and facilities provided by its principal bankers in Hong Kong and in the PRC. The Group had cash and bank balances of approximately HK\$56.5 million as at the balance sheet date. The Group's cash and bank balances were mostly held in Hong Kong dollars and Renminbi.

The Group's bank and other borrowings were made in Hong Kong dollars and Renminbi, approximately 70% of such borrowings bore interest at fixed lending rate. At 30 June 2006, the Group's bank and other borrowings amounted to approximately HK\$37.6 million, out of which approximately 95% was repayable within one year. The gearing ratio of the Group calculated as a ratio of total bank and other borrowings to total assets was approximately 24% as at 30 June 2006. Net current assets at 30 June 2006 was approximately HK\$30.2 million and the current ratio was approximately 153%. The Group had not used any financial instruments for hedging during the period.

At 30 June 2006, certain of the Group's buildings and leasehold land and buildings with carrying values of approximately HK\$9.9 million and HK\$9.2 million, respectively, were pledged to secure general banking facilities granted to the Group.

As at 30 June 2006, the Group did not have any contingent liabilities (2005: Nil).

At 30 June 2006, the Group had a total of 1,075 employees. The Group always maintains good working relations with its employees and has committed itself to staff training and development. Remuneration packages are maintained at a competitive level and are being reviewed on a periodical basis. Bonus and share options are awarded to employees according to the assessment of individual performance and industrial practice.

Subsequent to the period under review, on 6 July 2006, the Group has announced its proposal to issue 774,837,000 offer shares at a price of HK\$0.05 per offer share by way of open offer of new shares, on the basis of seven offer shares for every twenty existing shares held on the record date. The estimated net proceeds from the open offer will be approximately HK\$37 million. The Board intends to apply the net proceeds as to (i) approximately HK\$2 million towards upstream and downstream integration in the principal line of business of the Group to enhance its profitability, including but not limited to the distribution of fabrics or chemical products or the production of packaging materials; (ii) approximately HK\$25 million towards possible diversified investments in the agricultural, energy and/or resources industries or other projects which have earning potentials to diversify its business; and (iii) the remaining balance of approximately HK\$10 million for general working capital of the Group. Further details of the open offer are set out in the Company's announcement dated 6 July 2006.

The Directors are optimistic about the performance of the Group for the full year as the global economy continues to flourish. Moving forward, the Group will continue to invest in research and development and to develop new series of products with add-on features and functions. The Group will continue to develop its business by expanding its sales team and distribution channels in North America, Europe and the PRC. In addition, the Group will apply part of the net proceeds from the open offer to explore other investment opportunities in the agricultural, energy and/or resources industries or other projects that have earning potentials to expand its operations and to diversify its business.

The proceeds from the Company's issue of new shares at the time of its listing on The Stock Exchange of Hong Kong Limited (the "Stock Exchange") on 22 January 2001, after deduction of related expenses, amounted to approximately HK\$43 million. As of 30 June 2006, the net proceeds were applied in accordance with the proposed applications set out in the Company's prospectus dated 9 January 2001, as follows:

- approximately HK\$5 million was used for developing new models and new products;
- approximately HK\$5 million was used for the acquisition of new machinery and auxiliary equipment;
- approximately HK\$10 million was used for establishing retail outlets and developing distribution channels in major cities in the PRC; and
- approximately HK\$18 million was used as general working capital of the Group.

The Group has placed the unused balance of the net proceeds with licensed banks in Hong Kong and the PRC. These deposits have been receiving reasonable and steady interest income which preserves the best interests of the Group and the shareholders.

DIRECTORS' INTERESTS IN SHARES

As at 30 June 2006, the interests and short positions of the Directors and chief executive of the Company in the shares, underlying shares and debentures of the Company and its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance (the "SFO")) which had been notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests and short positions in which they are deemed or taken to