Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

1. GENERAL

The Company was incorporated in the Cayman Islands as an exempted company with limited liability and its shares are listed on The Stock Exchange of Hong Kong Limited (the "Stock Exchange"). Its ultimate holding company is Talent Crown Investment Limited, incorporated in the British Virgin Islands ("BVI"). The addresses of the registered office and principal place of business of the Company are disclosed in the "Corporate Information" section of the annual report.

The financial statements are presented in Hong Kong dollars, and the functional currency of the Company is Renminbi. The financial statements are present in Hong Kong dollars because the Company is listed in Hong Kong.

The Company is an investment holding company. Particulars of the principal activities of its subsidiaries are set out in note 30.

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

In the current year, the Group has applied, for the first time, a number of new Hong Kong Financial Reporting Standards ("HKFRSs"), Hong Kong Accounting Standards ("HKASs") and Interpretations (hereinafter collectively referred to as "new HKFRSs") issued by The Hong Kong Institute of Certified Public Accountants (the "HKICPA") that are effective for accounting periods beginning on or after 1 January 2005. The adoption of the new HKFRSs has resulted in changes to the Group's accounting policies in the following areas that have an effect on how the results for the current or prior accounting periods are prepared and presented (see Note 3 for the financial impact).

Share-based Payments

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

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

2. CHANGES IN ACCOUNTING POLICIES/APPLICATION OF HONG KONG FINANCIAL REPORTING STANDARDS (continued)

Financial Instruments

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

Convertible notes

Previously, the convertible notes were classified as liabilities and recorded at the proceeds received, net of unamortised deferred expenditures, on the consolidated balance sheet. Upon application of HKAS 32 and HKAS 39, convertible notes are regarded as compound instruments, consisting of a liability component and an equity component, or in the case where the conversion options are not settled by the exchange of a fixed amount for a fixed number of equity instruments, the issuer is required to recognise the convertible notes in the form of financial liability with embedded derivatives. Derivatives embedded in a financial instrument are treated as separate derivatives when their economic risks and characteristics are not closely related to those of the host contract (the liability component) and the host contract is not carried at fair value through profit or loss.

On 1 July 2005, the Group has elected to designate its convertible notes with embedded derivatives as a whole as financial liabilities at fair value through profit or loss.

At each subsequent balance sheet date, the entire convertible notes are measured at fair value, with changes in fair value recognised directly in profit or loss in the period in which they arise. Transaction costs that are directly attributable to the issue of the convertible notes designated as financial liabilities at fair value through profit or loss are recognised in full in retained profits on adoption of HKAS 39. In accordance with relevant transitional provisions of HKAS 39, the carrying amount of the convertible notes as at 1 July 2005 were decreased by approximately HK$1,962,000 with a corresponding increase in retained profits, being the fair value adjustment on 1 July 2005 (see Note 3 for the financial impact).

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

2. CHANGES IN ACCOUNTING POLICIES/APPLICATION OF HONG KONG FINANCIAL REPORTING STANDARDS (continued)

Financial Instruments (continued)

Financial assets and financial liabilities other than debt and equity securities

From 1 July 2005 onwards, the Group classifies and measures its financial assets and financial liabilities other than debt and equity securities (which were previously outside the scope of Statement of Standard Accounting Practice 24 "Accounting for Investments in Securities" issued by the HKICPA) in accordance with the requirements of HKAS 39. Financial assets under HKAS 39 are classified as "financial assets at fair value through profit or loss", "available-for-sale financial assets", "loans and receivables" or "held-to-maturity financial assets". Financial liabilities are generally classified as "financial liabilities at fair value through profit or loss" or "financial liabilities other than financial liabilities at fair value through profit or loss (other financial liabilities)". "Other financial liabilities" are carried at amortised cost using the effective interest method. Except for the convertible notes mentioned above, the adoption of HKAS 39 has had no material effect on the Group's results for current and prior accounting periods.

Owner-occupied Leasehold Interest in Land

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

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

2. CHANGES IN ACCOUNTING POLICIES/APPLICATION OF HONG KONG FINANCIAL REPORTING STANDARDS (continued)

Potential impact on standards, amendments or interpretations not yet effective

The Group has commenced considering the potential impact of the following new standards, amendments or interpretations that have been issued but are not effective, but is not yet in a position to determine whether these standards, amendments or interpretations would have a significant impact on how its results of operations and financial position are prepared and presented. These standards, amendments and interpretations may result in changes in the future as to how the results and financial position are prepared and presented.

HKAS 1 (Amendment)	Capital disclosures[1]
HKAS 19 (Amendment)	Actuarial gains and losses, group plans and disclosures[2]
HKAS 21 (Amendment)	Net investment in a foreign operation[2]
HKAS 39 (Amendment)	Cash flow hedge accounting of forecast intragroup transactions[2]
HKAS 39 (Amendment)	The fair value option[2]
HKAS 39 & HKFRS 4 (Amendments)	Financial guarantee contracts[2]
HKFRS 6	Exploration for and evaluation of mineral resources[2]
HKFRS 7	Financial instruments: Disclosures[1]
HK(IFRIC)-INT 4	Determining whether an arrangement contains a lease[2]
HK(IFRIC)-INT 5	Rights to interests arising from decommissioning, restoration and environmental rehabilitation funds[2]
HK(IFRIC)-INT 6	Liabilities arising from participating in a specific market, waste electrical and electronic equipment[3]
HK(IFRIC)-INT 7	Applying the restatement approach under HKAS 29 Financial Reporting in Hyperinflationary Economies[4]
HK (IFRIC)-INT 8	Scope of HKFRS 2[5]
HK (IFRIC)-INT 9	Reassessment of embedded derivatives[6]
HK (IFRIC)-INT 10	Interim Financial Reporting and Impairment[7]

[1] Effective for annual periods beginning on or after 1 January 2007.
[2] Effective for annual periods beginning on or after 1 January 2006.
[3] Effective for annual periods beginning on or after 1 December 2005.
[4] Effective for annual periods beginning on or after 1 March 2006.
[5] Effective for annual periods beginning on or after 1 May 2006.
[6] Effective for annual periods beginning on or after 1 June 2006.
[7] Effective for annual periods beginning on or after 1 November 2006.

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

3. SUMMARY OF THE EFFECTS OF THE CHANGES IN ACCOUNTING POLICIES

i) The effects of the changes in the accounting policies described in Note 2 on the Group's results for the current and prior years are as follows:

	For the year ended 30 June	
	2006	2005
	HK$'000	HK$'000
Loss on changes in fair value of convertible notes	**(9,765)**	–
Interest on convertible notes	**590**	–
Amortisation of deferred expenditure	**914**	–
Decrease in profit for the year	**(8,261)**	–

ii) The cumulative effects of the application of the new HKFRSs as at 30 June 2005 and 1 July 2005 are summarised below:

	As at 30.6.2005 (originally stated)	**Effect of HKAS 17**	**As at 30.6.2005 (restated)**	**Effect of HKAS 39**	**As at 1.7.2005 (restated)**
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Property, plant and equipment	171,566	(14,231)	157,335	–	157,335
Lease premium for land					
– non-current portion	–	13,917	13,917	–	13,917
– current portion	–	314	314	–	314
Convertible notes	(75,777)	–	(75,777)	1,962	(73,815)
Total effects on assets and liabilities	95,789	–	95,789	1,962	97,751
Retained profits	252,635	–	252,635	1,962	254,597
Total effects on equity	252,635	–	252,635	1,962	254,597

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

4. CHANGES OF ACCOUNTING ESTIMATES

In previous years, plant and machinery were depreciated at 10% per annum. With effect from 1 July 2005, certain plant and machinery is depreciated at 20% per annum. The decrease in the useful lives of the plant and machinery is as a result of changes in weaving technology. This change in depreciation rate has increased the depreciated charge for the year by HK$5,760,000.

5. SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements has been prepared under the historical cost basis except for certain financial instruments which are measured at fair values, as explained in the accounting policies set out below.

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

Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and its subsidiaries made up to 30 June each year.

All significant inter-company transactions and balances within the Group are eliminated on consolidation.

Revenue recognition

Revenue represents the fair value of the considerations received and receivable for goods sold by the Group, less returns, to outside customers.

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

Interest income from a financial asset is accrued on a time basis, by reference to the principal outstanding and at the effective interest rate applicable, which is the rate that exactly discounts the estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount.

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

5. SIGNIFICANT ACCOUNTING POLICIES (continued)

Property, plant and equipment

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

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

Construction in progress is stated at cost, which includes construction and borrowing costs, as appropriate, less any identified impairment loss. When the construction is completed and the asset is ready for its intended use, the related cost is transferred to an appropriate category of property, plant and equipment and depreciated in accordance with the above policy.

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

Research expenditure

Expenditure on research activities is recognised as an expense in the period in which it is incurred.

Impairment

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

Where an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, such that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset in prior years. A reversal of an impairment loss is recognised as income immediately.

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

5. SIGNIFICANT ACCOUNTING POLICIES (continued)

Operating leases

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

Foreign currencies

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

Exchange differences arising on the settlement of monetary items, and on the translation of monetary items, are recognised in profit or loss in the period in which they arise, except for exchange differences arising on a monetary item that forms part of the Group's net investment in a foreign operation, in which case, such exchange differences are recognised in equity in the consolidated financials statements. Exchange differences arising on the retranslation of non-monetary items carried at fair value are included in profit or loss for the period.

For the purposes of presenting the consolidated financial statements, the assets and liabilities of the Group's foreign operations are translated into the presentation currency of the Group (i.e. Hong Kong Dollars) at the rate of exchange prevailing at the balance sheet date, and their income and expenses are translated at the average exchange rates for the year, unless exchange rates fluctuate significantly during the period, in which case, the exchange rates prevailing at the dates of transactions are used. Exchange differences arising, if any, are recognised as a separate component of equity (the currency translation reserve). Such exchange differences are recognised in profit or loss in the period in which the foreign operation is disposed of.

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

5. SIGNIFICANT ACCOUNTING POLICIES (continued)

Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, are capitalised as part of the cost of those assets. Capitalisation of such borrowing costs ceases when the assets are substantially ready for their intended use or sale. Investment income earned on the temporary investment of specific borrowings pending their expenditure on qualifying assets is deducted from the borrowing costs eligible for capitalisation.

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

Financial instruments

Financial assets and financial liabilities are recognised on the balance sheet when a group entity becomes a party to the contractual provisions of the instruments. Financial assets and financial liabilities are initially measured at fair value. Transaction costs that are directly attributable to the acquisition or issue of financial assets and financial liabilities (other than financial assets and financial liabilities at fair value through profit or loss) are added to or deducted from the fair value of the financial assets or financial liabilities, as appropriate, on initial recognition. Transaction costs directly attributable to the acquisition of financial assets or financial liabilities at fair value through profit or loss are recognised immediately in profit or loss.

Financial assets

The Group's financial assets are mainly classified as loans and receivables. All regular way purchases or sales of financial assets are recognised and derecognised on a trade date basis. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the time frame established by regulation or convention in the marketplace. The accounting policies adopted in respect of loans and receivables are set out below.

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

5. SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial instruments (continued)

Financial assets (continued)

Loans and receivables

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

Financial liabilities and equity

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

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

Financial liabilities at fair value through profit or loss

Financial liabilities at fair value through profit or loss of the Group are those designated at fair value through profit or loss on initial recognition (including convertible notes). At each balance sheet date subsequent to initial recognition, financial liabilities at fair value through profit or loss are measured at fair value, with changes in fair value recognised directly in profit or loss in the period in which they arise.

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

5. SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial instruments (continued)

Financial liabilities and equity (continued)

Other financial liabilities

Other financial liabilities (including trade and other payables and bank borrowings) are subsequently measured at amortised cost, using the effective interest method.

Equity instruments

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

Derecognition

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

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

Taxation

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

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

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

5. SIGNIFICANT ACCOUNTING POLICIES (continued)

Taxation (continued)

Deferred tax is recognised on differences between the carrying amount of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit, and is accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognised for all taxable temporary differences, and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised. Such assets and liabilities are not recognised if the temporary difference arises from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

Deferred tax liabilities are recognised for taxable temporary differences arising on investments in subsidiaries, except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future.

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

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

Inventories

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

Retirement benefit costs

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

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

6. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

The Group's major financial instruments include trade and other receivables, pledged bank deposits, bank balance and cash, trade and other payables, bank borrowings and convertible notes. Details of these financial instruments are disclosed in respective notes. The risks associated with these financial instruments and the policies on how to mitigate these risks are set out below. Management manages and monitors these exposures to ensure appropriate measures are implemented on a timely and effective manner.

(i) Market Risk

Currency risk

The Group mainly operates in the People's Republic of China (the "PRC") with most of the transactions denominated and settled in RMB. RMB is not freely convertible into other foreign currencies and conversion of RMB into foreign currencies is subject to rules and regulations of foreign exchange control promulgated by the PRC government. The PRC subsidiaries of the Company transact in their own functional currency and therefore no currency risk was noted for the subsidiaries. The convertible notes of the Company are denominated in US dollars. The Group currently does not have a foreign currency hedging policy. However, management monitors foreign exchange exposure closely and consider the usage of hedging instruments when the need arises.

Interest rate risk

The Group's fair value interest rate risk relates primarily to its fixed-rate bank borrowings and convertible notes. It is also exposed to cash flow interest rate risk through the variable-rate bank borrowings.

The Group currently does not have a policy to hedge against the interest rate risk as management believes that changes in the interest rate will not have a significant impact on the Group's financial position. However, management monitors closely the interest rate exposure and will consider using interest rate swap when the need arises.

Price risk

The price at which the convertible notes are converted is dependant on the underlying share price of the Company, therefore the Company is exposed to price risk.

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

6. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (continued)

(ii) Credit Risk

The Group's maximum exposure to credit risk in the event of the counterparties failure to perform their obligations as at 30 June 2006 in relation to each class of recognised financial assets is the carrying amount of those assets as stated in the consolidated balance sheet. In addition, the Group has a concentration of credit risk in certain of its major customers. In order to minimise the credit risk, management of the Group has delegated a team of staff responsible for determination of credit limits, credit approvals and other monitoring procedures to ensure that follow-up action is taken to recover overdue debts. In addition, the Group reviews the recoverable amount of each individual trade debt at each balance sheet date to ensure that adequate impairment losses are made for irrecoverable amounts. In this regard, the directors of the Company consider that the Group's credit risk is significantly reduced.

The credit risk on liquid funds is limited because the counter parties are banks and financial institution with good reputation.

7. SEGMENT INFORMATION

No analysis on business segment is provided as substantially all the Group's turnover and segment results were derived from the manufacture and sale of finished woven fabrics. In addition, no geographical market analysis is provided as the Group's turnover and contribution to segment results were substantially derived from the PRC and the assets are substantially located in the PRC.

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

8. OTHER INCOME

	2006 HK$'000	2005 HK$'000
Bank interest income	**3,614**	1,625
Exchange gain	**1,458**	–
Others	**101**	35
	5,173	1,660

9. FINANCE COSTS

	2006 HK$'000	2005 HK$'000
Interest on:		
Bank borrowings wholly repayable within five years	**1,063**	1,770
Convertible notes	**–**	664
Amortisation of deferred expenditure on convertible notes	**–**	518
	1,063	2,952

With the application of HKAS 39, the interest on the convertible notes was included in the fair value change of convertible notes for the year ended 30 June 2006.

10. INCOME TAX EXPENSE

	2006 HK$'000	2005 HK$'000
PRC Enterprise Income Tax ("EIT"):		
Current tax	**42,702**	42,617
Underprovision in the prior year	**2,292**	254
	44,994	42,871

No provision for Hong Kong Profits Tax has been made in the consolidated financial statements as the Group did not generate any assessable profits arising in Hong Kong for both years.

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

10. INCOME TAX EXPENSE (continued)

Fuzhou Huaguan Knitting and Sprining Co., Ltd. ("Fuzhou Huaguan") and Fuzhou Huasheng Textile Co., Ltd. ("Funzhou Huasheng") are subsidiaries established in the PRC which are exempted from the EIT for two years starting from its first profit-making year of operations and thereafter is eligible for 50% relief from EIT for the following three years under the income tax law of the PRC. The first profit-making year of Fuzhou Huaguan and Fuzhou Huasheng were the year ended 31 December 1999 and 31 December 2005 respectively. The tax relief period of Fuzhou Huaguan expired on 31 December 2003 and its applicable tax rate was 27% for the year ended 30 June 2006. Fuzhou Huasheng was in the tax exempted period; accordingly, no provision for income tax has been made in the consolidated financial statements.

The tax charge for the year can be reconciled to the profit per the income statement as follows:

	2006 **HK$'000**	2005 HK$'000
Profit before tax	**137,340**	137,666
Tax at the income tax rate of 27%	**37,082**	37,170
Tax effect of expenses not deductible for tax purpose	**5,228**	3,815
Tax effect of income not taxable for tax purpose	**(899)**	(199)
Effect of tax losses not allowable by Hong Kong tax authority	**1,295**	1,831
Effect of tax exemptions granted to a PRC subsidiary	**(4)**	–
Underprovision in respect of the prior year	**2,292**	254
Tax charge for the year	**44,994**	42,871

No provision for deferred taxation has been recognised in the consolidated financial statements as the amount involved is insignificant.

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

11. PROFIT FOR THE YEAR

	2006 HK$'000	2005 HK$'000
Profit from operating activities is arrived at after charging (crediting):		
Auditors' remuneration	820	730
Staff costs		
– directors' emoluments (note 12)	4,040	5,229
– other staff costs	11,292	10,104
– other staff's retirement benefit scheme contributions	1,491	1,678
	16,823	17,011
Allowance for bad and doubtful debts	187	366
(Write-back of) allowance for inventories	(18)	50
Depreciation on property, plant and equipment	25,984	18,025
Exchange loss	–	137
Loss on disposal of property, plant and equipment	2,478	14
Release of prepaid lease payments	317	308
Research costs	1,738	771

Research costs include staff costs of HK$172,000 (2005: HK$163,000), which are also included in the staff costs disclosed separately above.

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

12. DIRECTORS' AND EMPLOYEES' EMOLUMENTS

The employments paid or payable to each of the six (2005: eight) directors were as follows:

(a) Directors' emoluments

Details of emoluments of individual directors are set out as follows:

2006

	Director's fees HK$'000	Salaries and other benefits HK$'000	Retirement benefit scheme contributions HK$'000	Total HK$'000
Mr. Chen Dong	–	1,800	8	1,808
Mr. Chen Jinyan	–	1,440	8	1,448
Ms. Kong Ping	–	600	12	612
Mr. Huang Yongfeng	36	–	–	36
Mr. Yu Zhong Ming	36	–	–	36
Mr. Lo Kin Chung	100	–	–	100
	172	3,840	28	4,040

2005

	Director's fees HK$'000	Salaries and other benefits HK$'000	Retirement benefit scheme contributions HK$'000	Total HK$'000
Mr. Chen Dong	–	1,800	6	1,806
Mr. Chen Jinyan	–	1,440	6	1,446
Ms. Kong Ping	–	600	12	612
Mr. Chen Qinzhi	–	1,200	6	1,206
Mr. Huang Yongfeng	36	–	–	36
Mr. Yu Zhong Ming	30	–	–	30
Mr. Lo Kin Chung	83	–	–	83
Mr. Tong Lap Hong	10	–	–	10
	159	5,040	30	5,229

No directors waived any emoluments in the year ended 30 June 2006.

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

12. DIRECTORS' AND EMPLOYEES' EMOLUMENTS (continued)

(b) Employees' emoluments

The five highest paid individuals of the Group for the year ended 30 June 2006 included three (2005: four) directors of the Company, details of whose emoluments are included above. The emoluments of the remaining two (2005: one) individuals are as follows:

	2006 **HK$'000**	2005 HK$'000
Salaries and other benefits	**1,062**	547
Retirement benefit scheme contributions	**15**	6
	1,077	553

13. DIVIDENDS PAID

	2006 **HK$'000**	2005 HK$'000
Ordinary shares:		
Interim, paid – HK1.0 cent per share (2005: HK1.0 cent per share)	**8,766**	8,766
Final, paid – HK1.5 cents per share (2005: HK1.5 cents per share)	**13,148**	13,107
	21,914	21,873

Of the dividend paid in 2005 approximately HK$41,000 was settled in shares under the Company's scrip dividend scheme announced by the Company on 30 November 2004 in respect of the final dividend of the year ended 30 June 2004.

The final dividend of HK1.0 cent per share (2005: HK1.5 cents per share) has been proposed by the directors and is subject to approval by the shareholders in the annual general meeting.

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

14. EARNINGS PER SHARE

The calculation of the basic and diluted earnings per share is based on the following data:

	2006 HK$'000	2005 HK$'000
Earnings:		
Profit for the year and earnings for the purposes of basic earnings per share	92,346	94,795
Effect of dilutive potential ordinary shares in respect of:		
Convertible notes	9,765	1,182
Earnings for the purpose of diluted earnings per share	102,111	95,977
Number of shares:	'000	'000
Weighted average number of ordinary shares for the purposes of basic earnings per share	876,558	876,529
Effect of dilutive potential ordinary shares in respect of:		
Share options	–	2,573
Convertible notes	194,805	102,608
Weighted average number of ordinary shares for the purpose of diluted earnings per share	1,071,363	981,710

The computation of diluted earnings per share for the year ended 30 June 2006 does not assume the exercise of the Company's outstanding share options as the exercise price of those options is higher than the average market price for share for the year.

The following table summarises the impact on both basic and diluted earnings per share as a result of:

	Year ended 30 June 2006	
	Impact on basic earnings per share cents	Impact on diluted earnings per share cents
Reported figures before adjustments	11.48	9.53
Adjustments arising from changes in accounting policies (see Note 3)	(0.94)	–
Restated	10.54	9.53

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

15. PROPERTY, PLANT AND EQUIPMENT

	Buildings	Plant and machinery	Leasehold improvements	Furniture, fixtures, office equipment and motor vehicles	Construction in progress	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
COST						
At 1 July 2004	61,039	100,293	1,933	3,809	11,132	178,206
Additions	–	6,730	7	184	30,680	37,601
Transfer	23,639	11,098	–	–	(34,737)	–
Disposals	–	(18)	–	(483)	–	(501)
At 30 June 2005	84,678	118,103	1,940	3,510	7,075	215,306
Exchange realignment	2,466	3,440	47	96	206	6,255
Additions	–	887	–	216	11,591	12,694
Transfer	–	4,363	–	–	(4,363)	–
Disposals	–	(30,973)	–	–	–	(30,973)
At 30 June 2006	87,144	95,820	1,987	3,822	14,509	203,282
DEPRECIATION AND AMORTISATION						
At 1 July 2004	13,078	25,035	232	1,991	–	40,336
Provided during the year	6,392	10,511	388	734	–	18,025
Eliminated on disposals	–	(16)	–	(374)	–	(390)
At 30 June 2005	19,470	35,530	620	2,351	–	57,971
Exchange realignment	567	1,035	16	67	–	1,685
Provided during the year	7,889	17,171	397	527	–	25,984
Eliminated on disposals	–	(27,524)	–	–	–	(27,524)
At 30 June 2006	27,926	26,212	1,033	2,945	–	58,116
NET BOOK VALUES						
At 30 June 2006	59,218	69,608	954	877	14,509	145,166
At 30 June 2005	65,208	82,573	1,320	1,159	7,075	157,335

At 30 June 2006, the Group pledged certain of the buildings and plant and machinery with aggregate net book values of HK$871,000 (2005: HK$59,340,000) and HK$37,036,000 (2005: HK$26,572,000), respectively, to banks to secure banking facilities granted to the Group.

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

15. PROPERTY, PLANT AND EQUIPMENT (continued)

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

Buildings	10%
Plant and machinery	10%–20%
Leasehold improvements	20%
Furniture, fixtures, office equipment and motor vehicles	20%

16. PREPAID LEASE PAYMENTS

	2006	2005
	HK$'000	HK$'000
		(Restated)
The Group's prepaid lease payments comprise:		
Leasehold land held under medium-term land use rights in the PRC	**14,329**	14,231
Analysed for reporting purposes as:		
Non-current assets	**14,012**	13,917
Current assets	**317**	314
	14,329	14,231

At 30 June 2006, the Group pledged certain land use rights with a carrying amount of HK$884,000 (2005: HK$14,231,000) to banks to secure banking facilities granted to the Group.

17. INVENTORIES

	2006	2005
	HK$'000	HK$'000
Raw materials	**3,966**	5,956
Work in progress	**10,724**	13,622
Finished goods	**13,473**	9,597
	28,163	29,175

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

18. TRADE AND OTHER RECEIVABLES

The Group allows an average credit period ranges from 45 days to 180 days to its trade customers. The following is an aged analysis of trade receivables at the balance sheet date:

	2006 **HK$'000**	2005 HK$'000
0 – 60 days	**56,761**	59,389
61 – 90 days	**2,072**	222
Over 90 days	**809**	691
Trade receivables	**59,642**	60,302
Other receivables	**1,664**	1,806
	61,306	62,108

The directors consider that the fair values of the Group's trade and other receivables at 30 June 2006 approximate the corresponding carrying amounts.

19. PLEDGED BANK DEPOSITS

The amount of US$5,000,000, equivalent to HK$39,007,000 (2005: US$5,000,000, equivalent to HK$39,000,000) represents deposits held as continuing security for the convertible notes issued. The deposits have been pledged to secure convertible notes which would be repayable on 6 December 2007 and is therefore classified as non-current assets.

The remaining amount represents deposits pledged to lenders to secure facilities granted to the Group. The deposits have been pledged to secure short-term other borrowings and are therefore classified as current assets.

The deposits carry interest rate at ranges, from 0.72% to 3.60% per annum. The pledged bank deposits will be released upon repayment of convertible notes and settlement of relevant borrowings. The fair value of bank deposits at 30 June 2006 approximates to the corresponding carrying amount.

20. BANK BALANCES AND CASH

Bank balances and cash comprises cash held by the Group and bank balances that carry interest rate at ranges, from 0.72% to 3% per annum and have original maturity of three months or less. The carrying amount of these bank balances and cash approximates to their fair value.

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

21. TRADE AND OTHER PAYABLES

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

	2006	2005
	HK$'000	HK$'000
0 – 60 days	**40,001**	43,278
Other payables	**16,591**	14,032
	56,592	57,310

The directors consider that the fair values of the Group's trade and other payables at 30 June 2006 approximate the corresponding carrying amounts.

22. BANK BORROWINGS, SECURED

At 30 June 2006, the Group's bank borrowings are wholly repayable within one year and are secured by the following:

(i) certain buildings and prepaid lease payments as set out in notes 15 and 16, respectively;

(ii) certain plant and machinery as set out in note 15; and

(iii) bank deposits of HK$4,314,000.

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

22. BANK BORROWINGS, SECURED (continued)

The exposure of the Group's fixed-rate borrowings and variable-rate borrowings and the contractual maturity dates or repricing dates are as follows:

	Fixed-rate borrowings HK$'000	**Variable-rate borrowings HK$'000**	**Total HK$'000**
2006:			
Within one year	**6,408**	**9,666**	**16,074**

	Fixed-rate borrowings HK$'000	Variable-rate borrowings HK$'000	Total HK$'000
2005:			
Within one year	15,660	7,840	23,500

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

	2006	2005
Effective interest rate:		
Fixed-rate borrowings	**6.37% to 7.02%**	5.76% to 6.70%
Variable-rate borrowings	**5.03% to 6.71%**	4.91% to 5.94%

The fair values of the Group's borrowings at 30 June 2006 are not significantly different to the corresponding carrying amounts.

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

23. SHARE CAPITAL

	Number of shares	Nominal value HK$'000
Ordinary shares of HK$0.01 each		
Authorised:		
At 1 July 2004, 30 June 2005 and 30 June 2006	2,000,000,000	20,000
Issued and fully paid:		
At 1 July 2004	876,500,000	8,765
Issue of shares as scrip final dividend	57,583	1
At 30 June 2005 and 30 June 2006	876,557,583	8,766

During the year ended 30 June 2005, 57,583 shares had been issued as scrip final dividend for the year ended 30 June 2004. The shares issued rank pari passu with the then existing shares in all respects.

24. CONVERTIBLE NOTES

	2006 HK$'000	2005 HK$'000
Convertible notes–unlisted	**82,990**	75,777

On 6 December 2004, the Company issued the 1.5% original tranche 1 secured convertible notes ("CN") of US$10,000,000 to Credit Suisse (Hong Kong) Limited ("Credit Suisse"), an independent investor.

The CN bears interest at 1.5% per annum, which is payable semi-annually in arrears and is repayable on 6 December 2007.

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

24. CONVERTIBLE NOTES (continued)

Credit Suisse has an option to convert the CN into ordinary shares of the Company at the option of the bondholder, at any time between the date of issue of the CN to the maturity dates of 6 December 2007 at either of the following options:

(i) fixed conversion price of HK$0.8579 or

(ii) floating conversion price being 91% of the average of any 4 consecutive closing prices per share as selected by the bondholder during the 30 consecutive business days immediately prior to the date on which the conversion notice is received by the Company.

Details of the CN are set out in an announcement made by the Company on 8 December 2004. The ordinary shares to be issued upon such conversion rank pari passu in all respects with the ordinary shares of the Company in issue on the relevant conversion date.

Pursuant to a deed of assignment dated 3 December 2004, Credit Suisse will deposit the subscription funds for the CN into an account of DB Trustees (Hong Kong) Limited (the "Account"). The Company will charge the Account and all moneys (including interest) from time to time standing to the credit of the Account, by way of fixed charge, in favour of DB Trustees (Hong Kong) Limited (who acts as security trustee for Credit Suisse) as continuing security for the payment and discharge of all moneys owing by the Company to Credit Suisse. At 30 June 2006, an amount of US$5,000,000, equivalent to HK$39,007,000 (2005: US$5,000,000, equivalent to HK$39,000,000) was maintained in the Account.

Following the adoption of HKAS 39 on 1 July 2005, the CN were designated as financial liabilities through profit or loss.

The CN is measured at fair value at each balance sheet date. Its fair value of the conversion option of the CN is determined with reference to the quoted market prices of the Company's shares at the balance sheet date. During the year ended 30 June 2006, the fair value (excluding changes attributable to the benchmark interest rate) of the CN decreased by HK$11,768,000.

Unless previously redeemed, converted or purchased and cancelled, the CN will be redeemed by the Company at its principal amount of US$10,000,000, equivalent to HK$78,000,000 on 6 December 2007.

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

25. SHARE-BASED PAYMENT TRANSACTIONS

The Company's share option scheme (the "Scheme") was adopted for the purpose of providing incentives and rewards to eligible participants for their contribution to the Group and/or to enable the Group to recruit and retain high-calibre employees and attract human resources that are valuable to the Group and any entity in which the Group holds any equity interest ("Invested Entity"). Eligible participants of the Scheme include the directors and employees of the Company, its subsidiaries or any Invested Entity, suppliers and customers, of the Group or any Invested Entity, any person or entity that provides research, development or other technological support to the Group or any Invested Entity, and any shareholder of any members of the Group or any Invested Entity or any holder of any securities issued by any members of the Group or any Invested Entity. The Scheme became effective on 10 September 2003 (the "Listing date") and, unless otherwise terminated or amended, will remain in force for 10 years.

At 30 June 2006, the number of shares in respect of which options had been granted and remained outstanding under the Scheme was 38,250,000, representing approximately 4% of the shares of the Company in issue at that date. The maximum number of shares which may be issued upon exercise of all outstanding share options granted and yet to be exercised under the Scheme and any other share option schemes adopted by the Group shall not exceed such number of Company's shares as equal to 30% of the issued share capital of the Company from time to time. The total number of shares which may be issued upon exercise of all share options to be granted under the Scheme and any other share option schemes of the Group must not in aggregate exceed 10% of the Company's shares in issue as at the Listing date. The number of shares in respect of which options may be granted to any individual in any one year is not permitted to exceed 1% of the shares of the Company in issue at any point in time, without prior approval from the Company's shareholders. Options granted to substantial shareholders or independent non-executive directors in excess of 0.1% of the Company's share capital or with a value in excess of HK$5,000,000 must be approved in advance by the Company's shareholders.

Options granted must be taken up within 28 days of the date of grant, upon payment of HK$1 per option. Options may be exercised at any time from the date of grant of the share option to the 10th anniversary of the date of grant. The exercise price is determined by the directors of the Company, and will not be less than the higher of the closing price of the Company's shares on the date of grant, and the average closing price of the shares for the five business days immediately preceding the date of grant.

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

25. SHARE-BASED PAYMENT TRANSACTIONS (continued)

The following table discloses details of the Company's share options held by directors and employees and movements in such holdings during the two years:

Category	Date of grant	Exercise period	Exercise price HK$	Outstanding at 1.7.2004	Granted during the year	Lapsed during the year	Outstanding at 30.6.2005 and 30.6.2006
Directors	23.12.2003	23.12.2003–22.12.2013	0.612	8,000,000	–	(4,000,000)	4,000,000
Employees	23.12.2003	23.12.2003–22.12.2013	0.612	34,250,000	–	–	34,250,000
				42,250,000	–	(4,000,000)	38,250,000

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

26. BALANCE SHEET OF THE COMPANY

	Notes	2006 HK$'000	2005 HK$'000
NON-CURRENT ASSETS			
Property and equipment		**302**	395
Interests in subsidiaries		**172,770**	172,770
Pledged bank deposits		**39,007**	39,000
		212,079	212,165
CURRENT ASSETS			
Amounts due from subsidiaries		**144,036**	140,972
Other receivables		**124**	102
Bank balances and cash		**940**	2,014
		145,100	143,088
CURRENT LIABILITIES			
Other payables		**820**	1,394
Amounts due to subsidiaries		**9,115**	2,041
		9,935	3,435
NET CURRENT ASSETS		**135,165**	139,653
		347,244	351,818
CAPITAL AND RESERVES			
Share capital		**8,766**	8,766
Dividend reserve	(a)	**8,766**	13,148
Other reserves	(a)	**246,722**	254,127
		264,254	276,041
NON-CURRENT LIABILITIES			
Convertible notes		**82,990**	75,777
		347,244	351,818

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

26. BALANCE SHEET OF THE COMPANY (continued)

Note:

(a) RESERVES

	Share premium HK$'000	Capital reserve HK$'000	Dividend reserve HK$'000	Retained profits HK$'000	Total HK$'000
At 1 July 2004	69,329	172,750	13,148	161	255,388
Issue of shares as scrip final dividend	40	–	(41)	–	(1)
Profit for the year	–	–	–	33,761	33,761
Final dividend paid	–	–	(13,107)	–	(13,107)
Proposed interim dividend	–	–	8,766	(8,766)	–
Interim dividend paid	–	–	(8,766)	–	(8,766)
Proposed final dividend	–	–	13,148	(13,148)	–
At 30 June 2005	69,369	172,750	13,148	12,008	267,275
Effect of changes in accounting polices (note 3)	–	–	–	1,962	1,962
At 1 July 2005 (restated)	69,369	172,750	13,148	13,970	269,237
Profit for the year	–	–	–	8,165	8,165
Final dividend paid	–	–	(13,148)	–	(13,148)
Proposed interim dividend	–	–	8,766	(8,766)	–
Interim dividend paid	–	–	(8,766)	–	(8,766)
Proposed final dividend	–	–	8,766	(8,766)	–
At 30 June 2006	69,369	172,750	8,766	4,603	255,488

Capital reserve of the Company represents the difference between underlying net assets of the subsidiaries which were acquired by the Company and the nominal value of the share capital issued by the Company to acquire the assets under a group reorganisation on 15 August 2003.

27. OPERATING LEASE ARRANGEMENTS

The Group as lessees

	2006 HK$'000	2005 HK$'000
Minimum lease payments paid under operating leases during the year in respect of rented premises	**2,559**	2,569

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

27. OPERATING LEASE ARRANGEMENTS (continued)

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

	2006 HK$'000	2005 HK$'000
Within one year	1,428	1,587
In the second to fifth years, inclusive	2,180	2,455
	3,608	4,042

Operating lease payments represent rentals payable by the Group for certain of its office premises. Leases are negotiated for an average term of two years with fixed rentals.

28. COMMITMENTS

	The Group	
	2006 HK$'000	2005 HK$'000
Capital expenditure contracted for but not provided in the financial statements in respect of construction of land and buildings	1,902	3,679
Capital expenditure authorised but not contracted for in respect of land and plant and machinery	–	17,218

At 30 June 2006, the Group had commitments for future research costs of HK$400,000 (2005: HK$531,000) payable under a non-cancellable consultancy agreement which will expire on 31 March 2009.

29. RELATED PARTY TRANSACTIONS

Compensation of key management personnel

The remuneration of key management during the year were as follows:

	2006 HK$'000	2005 HK$'000
Short-term benefits	4,040	5,229

The remuneration of key management is determined by the remuneration committee of the Company having regard to the performance of individuals and market trends.

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

30. PRINCIPAL SUBSIDIARIES

Details of the Company's principal subsidiaries at 30 June 2006 are as follows:

Name of subsidiary	Place of incorporation or registration/ operations	Paid up issued/ registered capital	Proportion of nominal value of issued/registered capital held by the Company		Principal activities
			Directly %	Indirectly %	
Fuzhou Huaguan *	PRC	RMB41,280,530	–	100	Manufacture and sale of finished woven fabrics
Fuzhou Huasheng *	PRC	US$4,000,000	–	100	Manufacture and sale of finished woven fabrics
Global Art International Limited	BVI	US$1 Ordinary share	–	100	Investment holding
Good Fame Group Limited	BVI	US$1 Ordinary share	–	100	Investment holding
Right Lane International Limited	BVI	US$30,000 Ordinary shares	100	–	Investment holding

* Fuzhou Huaguan and Fuzhou Huasheng are established as wholly foreign-owned enterprises under the relevant PRC law and regulations with an operating period up to 26 July 2010 and 6 December 2054, respectively.

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