MANAGEMENT DISCUSSION AND ANALYSIS

FINANCIAL PERFORMANCE

The Group's revenue for the year ended 30 September 2006 amounted to approximately HK$586 million representing an increase of 13% over last year. However, profit for the year was approximately HK$85 million representing an increase of approximately 30% over last year. There was a significant reduction of other operating expenses of approximately HK$7 million in 2006 due to cost-saving measures and major change in accounting policies namely demolition of annual amortisation of goodwill.

The increase in revenue was mainly due to improved efficiency from the full usage of all dyeing plants. Manufacture and sale of yarns amounted to approximately HK$104 million during the year. The revenue for the provision of fabric processing services and the manufacture of yarns remained stable during the year under review.

The gross profit margin of the Group increased from 24% in 2005 to 26% in 2006, which was mainly attributable to the system enhancement and a steady work force. Profit from operating activities has increased by HK$23 million over 2005.

On finance costs, there was an increase of approximately HK$3 million due to the raising of a HK$250 million syndicated loan. Profit before tax has seen a significant increase of 30% and profit after tax showed an increase of 30% over the previous year.

ANALYSIS BY CUSTOMER GEOGRAPHICAL REGIONS

Sales to customers located in the Greater China region remained stable at 53% of total sales in 2006. The Philippines market continued to be a strong base of customers of the Group, accounted for approximately 37% of the Group's total revenue. The remaining 10% of sales were generated from customers located in Africa, Australia and North America.

MANAGEMENT DISCUSSION AND ANALYSIS

LIQUIDITY AND FINANCIAL RESOURCES

At 30 September 2006, the Group had current assets of approximately HK$429 million (2005: HK$251 million) and current liabilities of approximately HK$188 million (2005: HK$177 million). The current ratio (calculated as current assets to current liabilities) increased from 1.42 as at 30 September 2005 to 2.29 as at 30 September 2006, owing primarily to improved cash position. The gearing ratio (calculated as the total bank borrowings to total shareholders' equity) had risen slightly from 0.39 as at 30 September 2005 to 0.48 as at 30 September 2006. These ratios were at reasonably adequate levels as at 30 September 2006 while the Group had sufficient resources in meeting its short-term and long-term obligations.

During the year under review, the Group principally met its funding requirements by cash flows from operations and bank borrowings. The net cash inflow from operating activities and financing activities were approximately HK$81 million and HK$96 million respectively.

Total bank borrowings increased by around 49% to approximately HK$92 million. The Group successfully raised HK$250 million through a syndication of six banks led by Citic Ka Wah Bank Limited and UOB Asia Limited of which HK$190 million was drawn down in the year ended 30 September 2006. Out of the utilised amount of HK$190 million, HK$90 million was used to repay existing bank debts, HK$28 million was paid as a deposit for the acquisition of United Glory Development Ltd. which owns Huarun Knitting & Dyeing Co. Ltd. in Shishi and the remaining funds were kept for working capital and other capital expenses.

At 30 September 2006, the Group had total bank borrowings of approximately HK$279 million, of which approximately HK$108 million was repayable within one year and approximately HK$171 million was repayable more than one year. Approximately 34% of the total bank borrowings was subject to fixed interest rates while approximately 66% was subject to floating interest rates. The Group's bank borrowings were primarily denominated in Renminbi and Hong Kong dollars. For the Group's total bank borrowings as at 30 September 2006, 34% of the balance was denominated in Renminbi and 66% of the balance was denominated in Hong Kong dollars. There are no seasonal adjustments with respect to the Group's borrowings.

At 30 September 2006, the Group's bank borrowings were secured by (i) certain plant and machinery of the Group; (ii) certain prepaid land lease payments and buildings of the Group; (iii) corporate guarantees given by its subsidiaries; and (iv) charges over the equity of its subsidiaries.

CAPITAL STRUCTURE

At the annual general meeting of the Company held on 24 February 2006, an ordinary resolution was duly passed by the shareholders of the Company with respect to the bonus issue of shares on the basis of 1 bonus share for every 20 existing shares of the Company (the "Bonus Issue"). Upon the granting of listing approval for the Bonus Issue by the Stock Exchange of Hong Kong Limited (the "Stock Exchange"), a total of 38,727,600 bonus shares were issued on 1 March 2006. In May 2006, a total of 67,200,000 shares were issued pursuant to the exercise of the share options by the option holders of the Company at an exercise price of HK$0.395 per share. As a result of the Bonus Issue and the exercise of share options as referred to the above, the total number of issued share capital of the Company as at 30 September 2006 was 880,479,600.

MANAGEMENT DISCUSSION AND ANALYSIS

CAPITAL EXPENDITURE AND MATERIAL ACQUISITION

During the year under review, the total capital expenditure of the Group was approximately HK$75 million, which was incurred as follows:

— approximately HK$47 million for the expansion of various plants and erection of new buildings;

— approximately HK$28 million for the deposit on the acquisition of United Glory Development Ltd., to cope with the increase in production and sales volume.

FOREIGN EXCHANGE EXPOSURE

Most assets, liabilities and transactions of the Group are denominated in Renminbi ("RMB"), except overseas sales which are denominated in United States dollars ("USD") and Hong Kong dollars ("HKD"). In view of the currency peg between HKD and USD and a relatively stable RMB at HKD1.00 equal to RMB1.02 (as at 30 September 2006), the fluctuations of foreign currencies did not have a significant impact on the performance of the Group.

CONTINGENT LIABILITIES

The Group did not have any significant contingent liabilities as at 30 September 2006 (2005: HK$Nil).

PLEDGE OF ASSETS

The Group's bank borrowings are secured by certain subsidiaries of the Group's prepaid land lease payments, buildings and plant and machinery with a total carrying value of approximately HK$91 million at 30 September 2006 (2005: HK$101,127,000), and corporate guarantees given by subsidiaries of the Company.

EMPLOYMENT INFORMATION

At 30 September 2006, the Group had a total of 2,017 (2005: 2,031) employees in Hong Kong, Macau and the PRC. The Group's emoluments policies are formulated on the performance of individual employees and on the basis of the salary trends in various regions, and are reviewed periodically.

For the year ended 30 September 2006, the total staff costs (including Directors' emoluments) amounted to approximately HK$46 million (2005: HK$39 million). The upsurge was due to employee share option benefits.

The Company also maintains a share option scheme for the purpose of providing incentives and rewards to the eligible participants for their contributions to the Group.

MANAGEMENT DISCUSSION AND ANALYSIS

BUSINESS DEVELOPMENT AND OUTLOOK

All plants and other business expansions have contributed greatly to the Group's turnover. The management expects to see further growth with future acquisition and expansion of plant facilities.

Existing plants include:

— Huafeng Knitting (99.24% owned subsidiary of the Company): specializes in fabric manufacturing and processing with an annual production capacity of 55,000 tonnes.

— Fenghua Textile (wholly-owned subsidiary of the Company): principally engages in yarn spinning (65,000 spindles) with an annual production capacity of approximately 14,000 tonnes.

— Lingfeng (wholly-owned subsidiary of the Company): principally engages in fabric processing with an annual processing capacity of approximately 38,000 tonnes.

— Shenyang Huafeng (53.6% owned subsidiary of the Company): principally engages in fabric processing of corduroy; fabric processing and printing of muslin. Total annual processing capacity reaches approximately 36 million meters.

— Lianyungang Huafeng (wholly-owned subsidiary of the Company): the factory has been leased out to a third party at an annual rental of HK$2.5 million.

On technology transfer, the Group has been acquiring latest technical know-how from external resources on the improvement of operation efficiency, reduction of manufacturing cost and better quality control. The aggregate value of six types of technology know-how with 8 to 10 years of remaining economic useful life amounted to about HK$19 million was assessed by an independent professional valuer, BMI Appraisals Limited, in January 2007. Since much of the latest technology is new to the industry, an amount of HK$10 million was considered as research & development cost. As such, the HK$10 million research & development cost was included in cost of services provided and cost of sales in the financial year ended 30 September 2006.

The Group reported increasingly bullish turnover in 2006. Boosted by increasing surges in production capacity and improved efficiencies from the full use of all dyeing plants, the Group has an aggressive strategy for growth and is carving out a leadership role in the industry.

The future sees the Group continuing to deliver strong and consistent profitable growth through its expansion of presence in China and globally. We intend to invest substantially in capacity expansion of existing operations and our ambitions are to diversify into new vertical industry areas that compliment and enhance our fabric processing resources and capabilities.