

AUDITED FINANCIAL STATEMENTS

NOTES TO FINANCIAL STATEMENTS

31 December 2006

1. CORPORATE INFORMATION

The registered office of Weiqiao Textile Company Limited (the “Company”) is located at No.34, Qidong Road, Weiqiao Town, Zouping County, Shandong Province, the People’s Republic of China (the “PRC”).

The Company and its subsidiaries (collectively, the “Group”) are principally engaged in the manufacture and sale of cotton yarns, grey fabrics and denims in the PRC and overseas.

In the opinion of the directors, the immediate holding company and the ultimate holding company of the Group are Shandong Weiqiao Chuangye Group Company (the “Holding Company”), a limited liability company established in the PRC, and Zouping County Supply and Marketing Corporation Union (“ZCSU”), a collectively-owned enterprise formed in the PRC, respectively.

2.1 BASIS OF PREPARATION

These financial statements have been prepared in accordance with Hong Kong Financial Reporting Standards (“HKFRSs”) (which also include Hong Kong Accounting Standards (“HKASs”) and Interpretations) issued by the Hong Kong Institute of Certified Public Accountants, accounting principles generally accepted in Hong Kong and the disclosure requirements of the Hong Kong Companies Ordinance. They have been prepared under the historical cost convention, except for derivative financial instruments, which have been measured at fair value. These financial statements are presented in Renminbi (“RMB”) and all values are rounded to the nearest thousand except when otherwise indicated.

Basis of consolidation

The consolidated financial statements include the financial statements of the Company and its subsidiaries for the year ended 31 December 2006. The results of subsidiaries are consolidated from the date of acquisition, being the date on which the Group obtains control, and continue to be consolidated until the date that such control ceases. All significant intercompany transactions and balances within the Group are eliminated on consolidation.

The acquisition of subsidiaries during the year has been accounted for using the purchase method of accounting. This method involves allocating the cost of the business combinations to the fair value of the identifiable assets acquired, and the liabilities and contingent liabilities assumed at the date of acquisition. The cost of the acquisition is measured at the aggregate of 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.

Minority interests represent the interests of outside shareholders not held by the Group in the results and net assets of the Company’s subsidiaries.

2.2 IMPACT OF NEW AND REVISED HONG KONG FINANCIAL REPORTING STANDARDS

The Group has adopted the following new and revised HKFRSs for the first time for the current year's financial statements. Except for in certain cases, giving rise to new and revised accounting policies and additional disclosures, the adoption of these new and revised standards and interpretation has had no material effect on these financial statements.

HKAS 21 Amendment	Net Investment in a Foreign Operation
HKAS 27 Amendment	Consolidated and Separate Financial Statements: Amendments as a consequence of the Companies (Amendment) Ordinance 2005
HKAS 39 & HKFRS 4 Amendments	Financial Guarantee Contracts
HKAS 39 Amendment	Cash Flow Hedge Accounting of Forecast Intragroup Transactions
HKAS 39 Amendment	The Fair Value Option
HK(IFRIC)-Int 4	Determining whether an Arrangement contains a Lease

2.3 IMPACT OF ISSUED BUT NOT YET EFFECTIVE HONG KONG FINANCIAL REPORTING STANDARDS

The Group has not applied the following new and revised HKFRSs, that have been issued but are not yet effective, in these financial statements.

HKAS 1 Amendment	Capital Disclosures
HKFRS 7	Financial Instruments: Disclosures
HKFRS 8	Operating Segments
HK(IFRIC)-Int 7	Applying the Restatement Approach under HKAS 29 <i>Financial Reporting in Hyperinflationary Economies</i>
HK(IFRIC)-Int 8	Scope of HKFRS 2
HK(IFRIC)-Int 9	Reassessment of Embedded Derivatives
HK(IFRIC)-Int 10	Interim Financial Reporting and Impairment
HK(IFRIC)-Int 11	HKFRS 2-Group and Treasury Share Transactions
HK(IFRIC)-Int 12	Service Concession Arrangements

The HKAS 1 Amendment shall be applied for annual periods beginning on or after 1 January 2007. The revised standard will affect the disclosures about qualitative information about the Group's objective, policies and processes for managing capital; quantitative data about what the Company regards as capital; and compliance with any capital requirements and the consequences of any non-compliance.

HKFRS 7 shall be applied for annual periods beginning on or after 1 January 2007. The standard requires disclosures that enable users of the financial statements to evaluate the significance of the Group's financial instruments and the nature and extent of risks arising from those financial instruments and also incorporates many of the disclosure requirements of HKAS 32.

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2.3 IMPACT OF ISSUED BUT NOT YET EFFECTIVE HONG KONG FINANCIAL REPORTING STANDARDS (continued)

HKFRS 8 shall be applied for annual periods beginning on or after 1 January 2009 and will replace the existing HKAS 14 “Segment Reporting”. HKFRS requires an entity to adopt the “management approach” to report on the financial performance of its operating segments. Generally, the information to be reported would be that used internally for the purpose of evaluating segment performance and deciding resources allocation to operating segments. Such information may be different from what is used for preparing the income statement and balance sheet. HKFRS 8 therefore requires explanations of the basis on how the segment information is prepared and reconciled to the income statement and balance sheet.

HK(IFRIC)-Int 7, HK(IFRIC)-Int 8, HK(IFRIC)-Int 9, HK(IFRIC)-Int 10, HK(IFRIC)-Int 11 and HK(IFRIC)-Int 12 shall be applied for annual periods beginning on or after 1 March 2006, 1 May 2006, 1 June 2006 and 1 November 2006, 1 March 2007 and 1 January 2008, respectively.

The Group is in the process of making an assessment of the impact of these new and revised HKFRSs upon initial application. So far, it has concluded that while the adoption of the HKAS 1 Amendment, HKFRS 7 and HKFRS 8 may result in new or amended disclosures, these new and revised HKFRSs are unlikely to have a significant impact on the Group's results of operations and financial position.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Subsidiaries

A subsidiary is an entity whose financial and operating policies the Company controls, directly or indirectly, so as to obtain benefits from its activities.

The results of subsidiaries are included in the Company's income statement to the extent of dividends received and receivable. The Company's interests in subsidiaries are stated at cost less any impairment losses.

Joint ventures

A joint venture is an entity set up by contractual arrangement, whereby the Group and other parties undertake an economic activity. The joint venture operates as a separate entity in which the Group and the other parties have an interest.

The joint venture agreement between the venturers stipulates the capital contributions of the joint venture parties, the duration of the joint venture entity and the basis on which the assets are to be realised upon its dissolution. The profits and losses from the joint venture's operations and any distributions of surplus assets are shared by the venturers, either in proportion to their respective capital contributions, or in accordance with the terms of the joint venture agreement.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Joint ventures (continued)

A joint venture company is treated as:

- (a) a subsidiary, if the Group has unilateral control, directly or indirectly, over the joint venture;
- (b) a jointly-controlled entity, if the Group does not have unilateral control, but has joint control, directly or indirectly, over the joint venture;
- (c) an associate, if the Group does not have unilateral or joint control, but holds, directly or indirectly, generally not less than 20% of the joint venture's registered capital and is in a position to exercise significant influence over the joint venture; or
- (d) an equity investment accounted for in accordance with HKAS 39, if the Group holds, directly or indirectly, less than 20% of the joint venture's registered capital and has neither joint control of, nor is in a position to exercise significant influence over, the joint venture.

The Company has unilateral control over the Group's joint ventures, Shandong Luteng Textile Company Limited ("Luteng Textile") and Shandong Binteng Textile Company Limited ("Binteng Textile") since their incorporation on 12 September 2002 and 12 March 2004, respectively.

Goodwill

Goodwill arising on the acquisition of subsidiaries represents the excess of the cost of the business combination over the Group's interest in the net fair value of the acquirees' identifiable assets acquired, and liabilities and contingent liabilities assumed as at the date of acquisition.

Goodwill on acquisitions for which the agreement date is on or after 1 January 2005

Goodwill arising on acquisition is recognised in the consolidated balance sheet as an asset, initially measured at cost and subsequently at cost less any accumulated impairment losses.

The carrying amount of goodwill is reviewed for impairment annually or more frequently if events or changes in circumstances indicate that the carrying value may be impaired.

For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Group's cash-generating units, or groups of cash-generating units, that are expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities of the Group are assigned to those units or groups of units. Each unit or group of units to which the goodwill is so allocated:

- represents the lowest level within the Group at which the goodwill is monitored for internal management purposes; and
- is not larger than a segment based on either the Group's primary or the Group's secondary reporting format determined in accordance with HKAS 14 *Segment Reporting*.

Impairment is determined by assessing the recoverable amount of the cash-generating unit (group of cash-generating units) to which the goodwill relates. Where the recoverable amount of the cash-generating unit (group of cash-generating units) is less than the carrying amount, an impairment loss is recognised.

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2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Goodwill on acquisitions for which the agreement date is on or after 1 January 2005 (continued)

Where goodwill forms part of a cash-generating unit (group of cash-generating units) and part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation. Goodwill disposed of in this circumstance is measured based on the relative values of the operation disposed of and the portion of the cash-generating unit retained.

An impairment loss recognised for goodwill is not reversed in a subsequent period.

Impairment of non-financial assets other than goodwill

Where an indication of impairment exists, or when annual impairment testing for an asset is required (other than inventories, deferred tax assets, financial assets, and non-current assets), the asset's recoverable amount is estimated. An asset's recoverable amount is calculated as the higher of the asset's or cash-generating unit's value in use and its fair value less costs to sell, and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets, in which case, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

An impairment loss is recognised only if the carrying amount of an asset exceeds its recoverable amount. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. An impairment loss is charged to the consolidated income statement in the period in which it arises in those expenses categories consistent with the function of the impaired asset.

An assessment is made at each reporting date as to whether there is any indication that previously recognised impairment losses may no longer exist or may have decreased. If such indication exists, the recoverable amount is estimated. A previously recognised impairment loss of an asset other than goodwill and certain financial assets is reversed only if there has been a change in the estimates used to determine the recoverable amount of that asset, however not to an amount higher than the carrying amount that would have been determined (net of any depreciation/amortisation), had no impairment loss been recognised for the asset in prior years. A reversal of such impairment loss is credited to the consolidated income statement in the period in which it arises.

Related parties

A party is considered to be related to the Group if:

- (a) the party, directly or indirectly through one or more intermediaries, (i) controls, is controlled by, or is under common control with, the Group; (ii) has an interest in the Group that gives it significant influence over the Group; or (iii) has joint control over the Group;
- (b) the party is an associate;
- (c) the party is a jointly-controlled entity;
- (d) the party is a member of the key management personnel of the Group or its parent;
- (e) the party is a close member of the family of any individual referred to in (a) or (d);

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Related parties (continued)

- (f) the party is an entity that is controlled, jointly controlled or significantly influenced by or for which significant voting power in such entity resides with, directly or indirectly, any individual referred to in (d) or (e); or
- (g) the party is a post-employment benefit plan for the benefit of the employees of the Group, or of any entity that is a related party of the Group.

Property, plant and equipment and depreciation

Property, plant and equipment, other than construction in progress, are stated at cost less accumulated depreciation and any impairment losses. The cost of an item of property, plant and equipment comprises its purchase price and any directly attributable costs of bringing the asset to its working condition and location for its intended use. Expenditure incurred after items of property, plant and equipment have been put into operation, such as repairs and maintenance, is normally charged to the consolidated income statement in the period in which it is incurred. In situations where it can be clearly demonstrated that the expenditure has resulted in an increase in the future economic benefits expected to be obtained from the use of an item of property, plant and equipment, and where the cost of the item can be measured reliably, the expenditure is capitalised as an additional cost of that asset or as a replacement.

Depreciation is calculated on the straight-line basis to write off the cost of each item of property, plant and equipment to its residual value over its estimated useful lives. The principal estimated useful lives and annual depreciation rates used for this purpose are as follows:

	Estimated useful life	Annual depreciation rate
Buildings	6 - 40 years	2.4% to 16.0%
Machinery and equipment	3 - 33 years	2.9% to 32.0%
Others	4 - 10 years	9.5% to 24.0%

Where parts of an item of property, plant and equipment have different useful lives, the cost of that item is allocated on a reasonable basis among the parts and each part is depreciated separately.

Residual values, useful lives and the depreciation method are reviewed, and adjusted if appropriate, at each balance sheet date.

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss on disposal or retirement recognised in the consolidated income statement in the year the asset is derecognised is the difference between the net sales proceeds and the carrying amount of the relevant asset.

Construction in progress represents a building, which is stated at cost less any impairment losses, and is not depreciated. Cost comprises the direct costs of construction and capitalised borrowing cost on related borrowed funds during the period of construction. Construction in progress is reclassified to the appropriate category of property, plant and equipment when completed and ready for use.

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2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Leases

Leases where substantially all the rewards and risks of ownership of assets remain with the lessor are accounted for as operating leases. Where the Group is the lessor, assets leased by the Group under operating leases are included in non-current assets, and rentals receivable under the operating leases are credited to the consolidated income statement on the straight-line basis over the lease terms. Where the Group is the lessee, rentals payable under such operating leases are charged to the consolidated income statement on the straight-line basis over the lease terms.

Prepaid land lease payments under operating leases are initially stated at cost and subsequently recognised on the straight-line basis over the lease terms.

Intangible assets (other than goodwill)

The useful lives of intangible assets are assessed to be either finite or indefinite. Intangible assets with finite lives are amortised over the useful economic life and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortisation period and the amortisation method for an intangible asset with a finite useful life are reviewed at least at each balance sheet date. Intangible assets are stated at cost less any impairment losses and are amortised on the straight-line basis over their estimated useful lives of 10 years.

Research and development costs

All research costs are charged to the consolidated income statement as incurred.

Expenditure incurred on projects to develop new products is capitalised and deferred only when the Group can demonstrate the technical feasibility of completing the intangible asset so that it will be available for use or sale, its intention to complete and its ability to use or sell the asset, how the asset will generate future economic benefits, the availability of resources to complete the project and the ability to measure reliably the expenditure during the development. Product development expenditure which does not meet these criteria is expensed when incurred.

Investments and other financial assets

Financial assets in the scope of HKAS 39 are classified as either financial assets at fair value through profit or loss, or loans and receivables, as appropriate. When financial assets are recognised initially, they are measured at fair value, plus, in the case of investments not at fair value through profit or loss, directly attributable transaction costs. The Group considers whether a contract contains an embedded derivative when the Group first becomes a party to it. The embedded derivatives are separated from the host contract which is not measured at fair value through profit or loss when the analysis shows that the economic characteristics and risks of embedded derivatives are not closely related to those of the host contract.

The Group determines the classification of its financial assets after initial recognition and, where allowed and appropriate, re-evaluates this designation at the balance sheet date.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Investments and other financial assets (continued)

All regular way purchases and sales of financial assets are recognised on the trade date, that is, the date that the Group commits to purchase or sell the asset. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the period generally established by regulation or convention in the marketplace.

Financial assets at fair value through profit or loss

Financial assets at fair value through profit or loss include financial assets held for trading. Financial assets are classified as held for trading if they are acquired for the purpose of sale in the near term. Derivatives, including separated embedded derivatives, are also classified as held for trading unless they are designated as effective hedging instruments or financial guarantee contracts. Gains or losses on investments held for trading are recognised in the consolidated income statement.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Such assets are subsequently carried at amortised cost using the effective interest method. Amortised cost is calculated taking into account any discount or premium on acquisition and includes fees that are an integral part of the effective interest rate and transaction costs. Gains and losses are recognised in the consolidated income statement when the loans and receivables are derecognised or impaired, as well as through the amortisation process.

Fair value

The fair value of investments that are actively traded in organised financial markets is determined by reference to quoted market bid prices at the close of business at the balance sheet date. For investments where there is no active market, fair value is determined using valuation techniques. Such techniques include using recent arm's length market transactions; reference to the current market value of another instrument which is substantially the same; a discounted cash flow analysis; and option pricing models.

Impairment of financial assets

The Group assesses at each balance sheet date whether there is any objective evidence that a financial asset or a group of financial assets is impaired.

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2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Impairment of financial assets (continued)

Assets carried at amortised cost

If there is objective evidence that an impairment loss on loans and receivables carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate (i.e., the effective interest rate computed at initial recognition). The carrying amount of the asset is reduced either directly or through the use of an allowance account. The amount of the impairment loss is recognised in the consolidated income statement.

The Group first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant. If it is determined that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, the asset is included in a group of financial assets with similar credit risk characteristics and that group is collectively assessed for impairment. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in a collective assessment of impairment.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed. Any subsequent reversal of an impairment loss is recognised in the consolidated income statement, to the extent that the carrying value of the asset does not exceed its amortised cost at the reversal date.

In relation to trade receivables, a provision for impairment is made when there is objective evidence (such as the probability of the insolvency or significant financial difficulties of the debtor) that the Group will not be able to collect all of the amounts due under the original terms of an invoice. The carrying amount of the receivables is reduced through the use of an allowance amount. Impaired debts are derecognised when they are assessed as uncollectible.

Derecognition of financial assets

A financial asset (or, where applicable, a part of a financial asset or part of a group of similar financial assets) is derecognised where:

- the rights to receive cash flows from the asset have expired;
- the Group retains the rights to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a "pass-through" arrangement; or
- the Group has transferred its rights to receive cash flows from the asset and either (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

Where the Group has transferred its rights to receive cash flows from an asset and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the Group's continuing involvement in the asset. Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Group could be required to repay.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Derecognition of financial assets (continued)

Where continuing involvement takes the form of a written and/or purchased option (including a cash-settled option or similar provision) on the transferred asset, the extent of the Group's continuing involvement is the amount of the transferred asset that the Group may repurchase, except in the case of a written put option (including a cash-settled option or similar provision) on an asset measured at fair value, where the extent of the Group's continuing involvement is limited to the lower of the fair value of the transferred asset and the option exercise price.

Financial liabilities at amortised cost (including interest-bearing loans and borrowings)

Financial liabilities including trade and other payables, an amount due to the ultimate holding company and interest-bearing loans and borrowings are initially stated at fair value less directly attributable transaction costs and are subsequently measured at amortised cost, using the effective interest method unless the effect of discounting would be immaterial, in which case they are stated at cost.

Gains and losses are recognised in the consolidated income statement when the liabilities are derecognised as well as through the amortisation process.

Financial guarantee contracts

Financial guarantee contracts in the scope of HKAS 39 are accounted for as financial liabilities. A financial guarantee contract is recognised initially at its fair value plus transaction costs that are directly attributable to the acquisition or issue of the financial guarantee contract, except when such contract is recognised at fair value through profit or loss. Subsequent to initial recognition, the Group measures the financial guarantee contract at the higher of: (i) the amount determined in accordance with HKAS 37 *Provisions, Contingent Liabilities and Contingent Assets*; and (ii) the amount initially recognised less, when appropriate, cumulative amortisation recognised in accordance with HKAS 18 *Revenue*.

Derecognition of financial liabilities

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires.

When an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and a recognition of a new liability, and the difference between the respective carrying amounts is recognised in the consolidated income statement.

Derivative financial instruments and hedging

The Group uses derivative financial instruments such as forward currency contracts and interest rate swaps to hedge its risks associated with interest rate and foreign currency fluctuations. Such derivative financial instruments are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently remeasured at fair value. Derivatives are carried as assets when the fair value is positive and as liabilities when the fair value is negative.

Any gains or losses arising from changes in fair value on derivatives that do not qualify for hedge accounting are taken directly to the consolidated income statement.

The fair value of forward currency contracts is calculated by reference to current forward exchange rates for contracts with similar maturity profiles. The fair value of interest rate swap contracts is determined by reference to the present value of estimated future cash flows.

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2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Derivative financial instruments and hedging (continued)

For the purpose of hedge accounting, hedges are classified as:

- fair value hedges when hedging the exposure to changes in the fair value of a recognised asset or liability or an unrecognised firm commitment (except for foreign currency risk); or
- cash flow hedges when hedging the exposure to variability in cash flows that is either attributable to a particular risk associated with a recognised asset or liability or a highly probable forecast transaction, or a foreign currency risk in an unrecognised firm commitment.

At the inception of a hedge relationship, the Group formally designates and documents the hedge relationship to which the Group wishes to apply hedge accounting, the risk management objective and its strategy for undertaking the hedge. The documentation includes identification of the hedging instrument, the hedged item or transaction, the nature of the risk being hedged and how the Group will assess the hedging instrument's effectiveness in offsetting the exposure to changes in the hedged item's fair value or cash flows attributable to the hedged risk. Such hedges are expected to be highly effective in achieving offsetting changes in fair value or cash flows and are assessed on an ongoing basis to determine that they actually have been highly effective throughout the financial reporting periods for which they were designated.

Hedges which meet the strict criteria for hedge accounting are accounted for as follows:

Fair value hedges

The change in the fair value of a hedging derivative is recognised in the income statement. The change in the fair value of the hedged item attributable to the risk hedged is recorded as a part of the carrying amount of the hedged item and is also recognised in the income statement.

For fair value hedges relating to items carried at amortised cost, the adjustment to carrying value is amortised through the income statement over the remaining term to maturity. Any adjustment to the carrying amount of a hedged financial instrument for which the effective interest method is used is amortised the income statement.

Amortisation may begin as soon as an adjustment exists and shall begin no later than when the hedged item ceases to be adjusted for changes in its fair value attributable to the risk being hedged. If the hedged item is derecognised, the unamortised fair value is recognised immediately in the income statement.

When an unrecognised firm commitment is designated as a hedged item, the subsequent cumulative change in the fair value of the firm commitment attributable to the hedged risk is recognised as an asset or liability with a corresponding gain or loss recognised in the income statement. The changes in the fair value of the hedging instrument are also recognised in the income statement.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Derivative financial instruments and hedging (continued)

Cash flow hedges

The effective portion of the gain or loss on the hedging instrument is recognised directly in equity, while the ineffective portion is recognised immediately in the income statement.

Amounts taken to equity are transferred to the income statement when the hedged transaction affects the income statement, such as when hedged financial income or financial expense is recognised or when a forecast sale occurs. Where the hedged item is the cost of a non-financial asset or non-financial liability, the amounts taken to equity are transferred to the initial carrying amount of the non-financial asset or non-financial liability.

If the forecast transaction or firm commitment is no longer expected to occur, the amounts previously recognised in equity are transferred to the income statement. If the hedging instrument expires or is sold, terminated or exercised without replacement or rollover, or if its designation as a hedge is revoked, the amounts previously recognised in equity remain in equity until the forecast transaction or firm commitment occurs.

Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is determined on the weighted average basis and, in the case of work in progress and finished goods, comprises direct materials, direct labour and an appropriate proportion of overheads. Net realisable value is based on estimated selling prices less any estimated costs to be incurred to completion and disposal.

Cash and cash equivalents

For the purpose of the consolidated cash flow statement, cash and cash equivalents comprise cash on hand and demand deposits, and short term highly liquid investments which are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value, and have a short maturity of generally within three months when acquired, less bank overdrafts which are repayable on demand and form an integral part of the Group's cash management.

For the purpose of the balance sheets, cash and cash equivalents comprise cash on hand and at banks, including term deposits, which are not restricted as to use.

Provisions

A provision is recognised when a present obligation (legal or constructive) has arisen as a result of a past event and it is probable that a future outflow of resources will be required to settle the obligation, provided that a reliable estimate can be made of the amount of the obligation.

When the effect of discounting is material, the amount recognised for a provision is the present value at the balance sheet date of the future expenditures expected to be required to settle the obligation. The increase in the discounted present value amount arising from the passage of time is included in finance costs in the consolidated income statement.

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2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Income tax

Income tax comprises current and deferred tax. Income tax is recognised in the consolidated income statement or in equity if it relates to items that are recognised in the same or a different period, directly in equity.

Current tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities.

Deferred tax is provided, using the liability method, on all temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred tax liabilities are recognised for all taxable temporary differences, except :

- where the deferred tax liability arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of taxable temporary differences associated with investments in subsidiaries and interests in joint ventures, where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred tax assets are recognised for all deductible temporary differences, carryforward of unused tax credits and used tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carryforward of unused tax credits and unused tax losses can be utilised, except :

- where the deferred tax asset relating to the deductible temporary differences arises from negative goodwill or the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of deductible temporary differences associated with investments in subsidiaries and interests in joint ventures, deferred tax assets are only recognised to the extent that it is probable that temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised.

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 deferred tax asset to be utilised. Conversely, previously unrecognised deferred tax assets are reassessed at each balance sheet date and are recognised to the extent that it is probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the balance sheet date.

Deferred tax assets and deferred tax liabilities are offset, if a legally enforceable right exists to set off current tax assets against current tax liabilities and the deferred taxes relate to the same taxable entity and the same taxation authority.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Revenue recognition

Revenue is recognised when it is probable that the economic benefits will flow to the Group and when the revenue can be measured reliably, on the following bases:

- (a) from the sale of goods, where the significant risks and rewards of ownership have been transferred to the buyer, provided that the Group maintains neither managerial involvement to the degree usually associated with ownership, nor effective control over the goods sold;
- (b) electricity and steam income, when electricity or steam has been supplied;
- (c) rental income, on a time proportion basis over the lease terms; and
- (d) interest income, on an accrual basis using the effective interest method by applying the rate that discounts the estimated future cash receipts through the expected life of the financial instrument to the net carrying amount of the financial asset.

Government grants

Government grants are recognised at their fair value where there is reasonable assurance that the grant will be received and all attaching conditions will be complied with. When the grant relates to an expense item, it is recognised as income over the periods necessary to match the grant on a systematic basis to the costs that it is intended to compensate. Where the grant relates to an asset, the fair value is credited to a deferred income account and is released to the consolidated income statement over the expected useful life of the relevant asset by equal annual instalments.

Retirement benefits schemes

The Company and its subsidiaries participate in defined contribution retirement schemes organised by the local government authorities in the PRC. Employees holding city and township residency are entitled to an annual pension equivalent to a fixed portion of their basic salaries at their retirement dates. The Company and its subsidiaries are required to make contributions to the retirement schemes at a rate of 20% of the total salaries of those employees and have no further obligation for post-retirement benefits. The contributions are charged to the consolidated income statement of the Group as they become payable in accordance with the rules of the schemes.

Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, i.e., assets that necessarily take a substantial period of time to get ready for their intended use or sale, are capitalised as part of the cost of those assets. The capitalisation of such borrowing costs ceases when the assets are substantially ready for their intended use or sale. Where funds have been borrowed generally, and used for the purpose of obtaining qualifying assets, a capitalisation rate of 6.31% is applied to the expenditure on the individual assets.

AUDITED FINANCIAL STATEMENTS

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Dividends

Final dividends proposed by the directors are classified as a separate allocation of retained profits within the equity section of the balance sheet, until they have been approved by the shareholders in a general meeting. When these dividends have been approved by the shareholders and declared, they are recognised as a liability.

Foreign currency transactions

These financial statements are presented in RMB, which is the Company's functional and presentation currency. Each entity in the Group determines its own functional currency and items included in the financial statements of each entity are measured using that functional currency. Foreign currency transactions are initially recorded using the functional currency rates ruling at the date of the transactions. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rates of exchange ruling at the balance sheet date. All differences are taken to the consolidated income statement. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

3. SIGNIFICANT ACCOUNTING ESTIMATES

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

Estimation of fair value of financial derivatives

The Group estimates the fair value of financial derivatives based on the financial modelling which requires various source of information and assumption.

Realisability of deferred tax assets

Deferred tax is provided using the liability method, on all temporary differences at the balance sheet date between the tax base of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred tax assets are recognised for the provision for inventories and trade receivables, difference in depreciation for tax purpose, fair value adjustments of assets and liabilities and government grants recognised as deferred income to the extent that it is probable (i.e. more likely than not) that future taxable profits will be available to utilise deferred tax assets. Recognition primarily involves judgement regarding the future performance of the particular legal entity or tax group in which the deferred tax asset has been recognised. A variety of other factor is also evaluated in considering whether there is convincing evidence that it is probable that some portion or all of the deferred tax assets will ultimately be realised. The carrying amount of deferred tax assets is reviewed at each balance sheet date to assess realisation of deferred tax assets.

4. SEGMENT INFORMATION

The Group has only one business segment, which is the manufacture and sale of cotton yarns, grey fabrics and denims. The Group conducts the majority of its business activities in four geographical areas, namely, Mainland China, Hong Kong, East Asia (principally comprising Japan and South Korea) and others. All of the Group's assets are located in Mainland China.

An analysis by geographical segment, as determined by the location of the Group's operations, is as follows:

Year ended 31 December 2006

	Sales to external customers <i>RMB'000</i>	Cost of sales <i>RMB'000</i>	Gross profit <i>RMB'000</i>
Mainland China	13,001,266	10,675,055	2,326,211
Hong Kong	2,987,167	2,570,974	416,193
East Asia	1,893,886	1,620,638	273,248
Others	1,943,835	1,636,397	307,438
	19,826,154	16,503,064	3,323,090

Year ended 31 December 2005

	Sales to external customers <i>RMB'000</i>	Cost of sales <i>RMB'000</i>	Gross profit <i>RMB'000</i>
Mainland China	7,334,154	5,688,023	1,646,131
Hong Kong	2,372,547	2,123,222	249,325
East Asia	2,138,200	1,959,334	178,866
Others	1,739,488	1,569,680	169,808
	13,584,389	11,340,259	2,244,130

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5. REVENUE, OTHER INCOME AND GAINS

Revenue, which is also the Group's turnover, represents the invoiced value of goods sold, after allowances for trade discounts and returns, and excludes sales taxes and intra-group transactions.

An analysis of revenue, other income and gains is as follows:

	Notes	Group	
		2006 RMB'000	2005 RMB'000
Revenue			
Sale of textile goods		19,826,154	13,584,389
Other income			
Bank interest income		51,177	32,159
Compensation from suppliers on supply of sub-standard goods		70,037	59,208
Penalty income from employees		6,808	6,312
Recognition of deferred income	30	4,148	596
Revenue on plant and equipment leasing		1,000	250
Others		2,228	2,817
		135,398	101,342
Gains			
Sale of electricity and steam		224,490	44,125
Less: cost thereon		(146,810)	(29,491)
Gains on sale of electricity and steam		77,680	14,634
Gains on sale of waste and spare parts		21,905	3,215
Foreign exchange differences, net		109,394	68,206
Realised gains on derivative financial instrument transactions		5,873	—
Fair value gains, net:			
Derivative financial instrument - transactions not qualifying as hedges	27	—	2,139
		214,852	88,194
		350,250	189,536

6. PROFIT BEFORE TAX

The Group's profit before tax is arrived at after charging/(crediting):

	<i>Notes</i>	2006 RMB'000	2005 <i>RMB'000</i>
Cost of goods sold		16,373,711	11,253,204
Staff costs (excluding directors' and supervisors' remuneration (note 8)):			
Wages, salaries and social security costs		2,367,452	1,657,581
Retirement benefits scheme contributions		34,707	30,080
		2,402,159	1,687,661
Depreciation	15	995,255	737,008
Recognition of prepaid land lease payments	16	2,796	2,446
Repairs and maintenance		341,405	296,625
Losses/(gains) on disposal of items of property, plant and equipment		1,967	(94)
Amortisation of intangible assets	17	1,200	1,200
Auditors' remuneration		6,549	5,377
Directors' and supervisors' remuneration	8	4,932	4,214
Foreign exchange differences, net		(109,394)	(68,206)
Provision against inventories		99,859	37,719
Realised (gains)/losses on derivative financial instruments transactions	5	(5,873)	4,271
Fair value losses/(gains), net:			
Derivative financial instruments - transactions not qualifying as hedges	5, 27	6,357	(2,139)
Research and development costs included in:			
Wages and salaries		6,695	5,713
Consumption of consumables		13,184	4,445
		19,879	10,158
Minimum lease payments under operating leases:			
Land and buildings		16,902	9,986

AUDITED FINANCIAL STATEMENTS

7. RETIREMENT BENEFITS

The aggregate contribution of the Group to a retirement benefits schemes was approximately RMB35 million for the year ended 31 December 2006 (2005: RMB30 million). As at 31 December 2006, the Group had no forfeited contributions available to reduce its contributions to the pension scheme in future years (2005: Nil).

8. DIRECTORS' AND SUPERVISORS' REMUNERATION

Directors' and supervisors' remuneration for the year, disclosed pursuant to the Rules Governing The Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules") and Section 161 of the Hong Kong Companies Ordinance, is as follows:

	Group	
	2006 RMB'000	2005 RMB'000
Fees	3,794	4,034
Other emoluments:		
Salaries, allowances and benefits in kind	1,098	152
Retirement benefits scheme contributions	40	28
	1,138	180
	4,932	4,214

There was no arrangement under which a director or a supervisor waived or agreed to waive any remuneration during the year.

There was no emolument paid by the Group to the directors or supervisors as an inducement to join or upon joining the Group or as compensation for loss of office during the year (2005: Nil).

8. DIRECTORS' AND SUPERVISORS' REMUNERATION (continued)

(a) Independent non-executive directors

2006	Fees	Salaries, allowance and benefits in kind	Total
	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB' 000</i>
Mr. Wang Naixin	50	6	56
Mr. Xu Wenying	120	20	140
Mr. Chan Wing Yau, George	613	120	733
	783	146	929

2005	Fees	Salaries, allowance and benefits in kind	Total
	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>
Mr. Wang Naixin	50	—	50
Mr. Xu Wenying	120	—	120
Mr. Chan Wing Yau, George	624	—	624
	794	—	794

There were no other emoluments and benefits payable to the independent non-executive directors in 2005.

AUDITED FINANCIAL STATEMENTS

8. DIRECTORS' AND SUPERVISORS' REMUNERATION (continued)

(b) Executive directors and non-executive directors

	Fees RMB'000	Salaries, allowances and benefits in kind RMB'000	Retirement benefits scheme contributions RMB'000	Total RMB'000
2006				
Executive directors:				
Mr. Zhang Bo*	693	196	6	895
Ms. Zhang Hongxia	1,000	317	8	1,325
Mr. Qi Xingli	600	179	8	787
Ms. Zhao Suwen	400	113	6	519
Ms. Zhang Yanhong**	61	43	6	110
	2,754	848	34	3,636
Non-executive directors:				
Mr. Zhang Shiping	100	18	—	118
Mr. Wang Zhaoting	67	9	—	76
	167	27	—	194
	2,921	875	34	3,830

* Mr. Zhang Bo resigned as an executive director of the Company with effect from 11 September 2006.

** Ms. Zhang Yanhong was appointed as an executive director of the Company with effect from 6 November 2006.

8. DIRECTORS' AND SUPERVISORS' REMUNERATION (continued)

(b) Executive directors and non-executive directors (continued)

	Fees <i>RMB'000</i>	Salaries, allowances and benefits in kind <i>RMB'000</i>	Retirement benefits scheme contributions <i>RMB'000</i>	Total <i>RMB'000</i>
2005				
Executive directors:				
Mr. Zhang Bo	1,000	42	8	1,050
Ms. Zhang Hongxia	1,000	42	8	1,050
Mr. Qi Xingli	600	39	7	646
Ms. Zhao Suwen	400	29	5	434
	3,000	152	28	3,180
Non-executive directors:				
Mr. Zhang Shiping	100	—	—	100
Mr. Wang Zhaoting	50	—	—	50
	150	—	—	150
	3,150	152	28	3,330

AUDITED FINANCIAL STATEMENTS

8. DIRECTORS' AND SUPERVISORS' REMUNERATION (continued)

(c) Supervisors

	Fees <i>RMB'000</i>	Salaries, allowances and benefits in kind <i>RMB'000</i>	Retirement benefits scheme contributions <i>RMB'000</i>	Total <i>RMB'000</i>
2006				
Mr. Liu Mingping	30	35	6	71
Mr. Lu Tianfu	30	3	—	33
Ms. Wang Wei	30	39	—	69
	90	77	6	173
2005				
Mr. Liu Mingping	30	—	—	30
Mr. Lu Tianfu	30	—	—	30
Ms. Wang Wei	30	—	—	30
	90	—	—	90

9. FIVE HIGHEST PAID EMPLOYEES

The five highest paid employees during the year included five directors (2005: five), details of whose remuneration are set out in note 8 above.

10. FINANCE COSTS

	Group	
	2006 <i>RMB'000</i>	2005 <i>RMB'000</i>
Interest on bank loans wholly repayable within five years	676,474	437,867
Less: Interest capitalised	(13,300)	(17,700)
	663,174	420,167
Other finance costs:		
Increase in discounted amounts of long term payable to the immediate holding company	56,829	—
	720,003	420,167

11. TAX

Hong Kong profits tax has not been provided as the Group had no assessable profits arising in Hong Kong during the year (2005: Nil). Taxes on profits assessable elsewhere have been calculated at the rates of tax prevailing in the country in which the Group operates, based on existing legislation, interpretations and practices in respect thereof.

	Group	
	2006 <i>RMB'000</i>	2005 <i>RMB'000</i>
Current – Mainland China	676,667	240,430
Deferred (note 31)	(59,922)	(53,040)
Total tax charge for the year	616,745	187,390

AUDITED FINANCIAL STATEMENTS

11. TAX (continued)

A reconciliation of the tax expense applicable to profit before tax using the statutory rate for the locations in which the Company, its subsidiaries and joint ventures are situated to the tax expense at the effective tax rate, and a reconciliation of the applicable rate (i.e., the statutory tax rate) to the effective tax rate, are as follows:

	Group			
	2006		2005	
	RMB'000	%	RMB'000	%
Profit before tax	2,307,571		1,435,784	
Tax at PRC statutory tax rate	761,498	33.0	473,809	33.0
Expenses not deductible for tax	15,638	0.7	17,992	1.2
Tax loss not recognised	1,997	0.1	6,852	0.5
Tax exemption (note (a))	(3,313)	(0.1)	(7,558)	(0.5)
Tax concessions in respect of purchase of PRC manufactured machinery and equipment (note (b))	(163,378)	(7.1)	(287,689)	(20.0)
Others	4,303	0.2	(16,016)	(1.1)
Tax charge at the Group's effective rate	616,745	26.8	187,390	13.1

Under the PRC income tax law, the companies (except for Shandong Luteng Textile Company Limited ("Luteng Textile") and Shandong Binteng Textile Company Limited ("Binteng Textile")) comprising the Group are subject to corporate income tax ("CIT") at a rate of 33% on the taxable income as reported in their statutory accounts, which are prepared in accordance with PRC GAAP.

Note:

- (a) Being Sino-foreign joint venture enterprises, Luteng Textile and Binteng Textile are subject to a State CIT rate of 30% and a local CIT rate of 3%. With regard to State CIT, they are entitled to a full exemption for the first two years and a 50% reduction in the next three years, commencing from the first profitable year after offsetting all tax losses carried forward from the previous five years. With regard to local CIT, the local tax authority has granted Luteng Textile and Binteng Textile a full exemption commencing from 2002 and 2004, respectively. Luteng Textile and Binteng Textile were entitled to a 50% reduction in State CIT for the current year.
- (b) The amount represents a tax concession, approved by the local tax bureau, in respect of purchases of PRC manufactured machinery and equipment. The tax concession is calculated at 40% of the purchase cost of PRC manufactured machinery and equipment for 2003, 2004 and 2005, and is limited to the amount of increase in income tax for the current year compared with the tax amount of the preceding year.

There are no income tax consequences attaching to the payment of dividend by the Company to its shareholders.

12. PROFIT ATTRIBUTABLE TO EQUITY HOLDERS OF THE PARENT

The consolidated profit attributable to equity holders of the parent for the year ended 31 December 2006 includes a profit of RMB1,606 million (2005: RMB1,154 million) which has been dealt with in the financial statements of the Company (note 33).

13. PROFIT APPROPRIATIONS

- (a) Under the PRC Company Law and the respective companies' articles of association, net profit after tax as determined in accordance with PRC GAAP can only be distributed as dividends after making up prior years' cumulative losses, if any, and making allowance for the following statutory reserve funds, which cannot be used for purposes other than those created and non-distributable as cash dividends:

(i) Statutory surplus reserve

In accordance with the PRC Company Law and the respective companies' articles of association, the Company and its subsidiaries, except for Luteng Textile and Binteng Textile, are required to appropriate 10% of the annual statutory net profit after tax (after offsetting any prior years' losses), determined in accordance with PRC GAAP, to the statutory surplus reserve. When the balance of such reserve fund reaches 50% of each entity's registered capital, any further appropriation is optional. The statutory surplus reserve can be utilised to offset prior years' losses or to increase capital. However, such balance of the statutory surplus reserve must be maintained at a minimum of 25% of the registered capital after such usage.

(ii) Statutory public welfare fund

In 2005, in accordance with the PRC Company Law and the respective companies' articles of association, the Company and its subsidiaries, except for Luteng Textile and Binteng Textile, were required to appropriate 5% to 10% of the annual statutory net profit after tax (after offsetting any prior years' losses), determined in accordance with PRC GAAP, to the statutory public welfare fund, which will be utilised to build or acquire capital items, such as dormitories and other facilities for the employees of the Company and its subsidiaries, and cannot be used to pay for staff welfare expenses. Titles of these capital items remained with the respective companies now comprising the Group.

Pursuant to the revised PRC Company Law which was approved on 27 October 2005 and the Notice of Caiqi [2006]67 dated 15 March 2006 issued by the Ministry of Finance, appropriation to the statutory public welfare fund is no longer needed with effect from 1 January 2006, and the balance of the statutory public welfare fund is required to be transferred to the statutory surplus reserve.

The directors of the respective companies resolved to appropriate 10% of the profit attributable to shareholders, determined in accordance with the PRC GAAP, to the statutory reserve funds for the years ended 31 December 2006 and 2005.

AUDITED FINANCIAL STATEMENTS

13. PROFIT APPROPRIATIONS (continued)

(iii) General reserve fund, employee's bonus and welfare fund and enterprise expansion fund

In accordance with the PRC Joint Venture Law, dividends can be distributed by Luteng Textile and Binteng Textile after allowance has been made by offsetting any prior years' losses out of the annual statutory net profit after tax, determined in accordance with the PRC GAAP, and allocations to the statutory reserve funds, which comprise a general reserve fund, an employee's bonus and welfare fund and an enterprise expansion fund. The amounts of transfer to the various statutory reserve funds are determined at the discretion of the boards of directors of Luteng Textile and Binteng Textile.

(b) Dividend

	2006 <i>RMB'000</i>	2005 <i>RMB'000</i>
Proposed final — RMB0.440 (2005: RMB0.287) per share	525,531	323,005

The proposed final dividend for the year is subject to the approval of the Company's shareholders at the forthcoming annual general meeting. In accordance with the articles of association of the Company, the net profit after tax of the Company for the purpose of profit distribution will be deemed to be the lesser of (i) the net profit determined in accordance with PRC GAAP; and (ii) the net profit determined in accordance with the accounting standards of the overseas place where the Company's shares are listed (i.e. Hong Kong Financial Reporting Standards).

On 4 April 2006, the board of directors resolved to propose a 2005 final dividend of RMB0.287 per share based on the number of ordinary shares in issue of 1,125,452,500 amounting to RMB323 million. During the annual general meeting held on 6 June 2006, the shareholders approved the final dividend of RMB0.287 per share based on the number of ordinary shares in issue of 1,194,389,000 as shown on the Register of Members on 4 May 2006. The final 2005 dividend was then declared and amounted to RMB343 million.

14. EARNINGS PER SHARE ATTRIBUTABLE TO ORDINARY EQUITY HOLDERS OF THE PARENT

The calculation of basic earnings per share amounts is based on the net profit for the year attributable to ordinary equity holders of the parent, and the weighted average number of ordinary shares in issue during the year.

	2006 RMB'000	2005 RMB'000
Earnings		
Profit attributable to ordinary equity holders of the parent, used in the basic earnings per share calculation	1,685,405	1,242,473
		Number of shares
	2006	2005
Shares		
Weighted average number of ordinary shares in issue during the year used in the basic earnings per share calculation	1,181,546,036	920,657,979

The weighted average number of ordinary shares in issue during the year used in the basic earnings per share calculations for 2006 has been adjusted to reflect the issue of 68,936,500 H shares by way of placing on 10 March 2006 whereas the one for 2005 has been adjusted to reflect the issuance of 250,000,000 domestic shares as the purchase consideration for the acquisition of the thermal power assets(note 32(b)).

Diluted earnings per share amounts for the years ended 31 December 2006 and 2005 have not been disclosed as no diluting events existed during these years.

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15. PROPERTY, PLANT AND EQUIPMENT

Group

	Buildings <i>RMB'000</i>	Machinery and equipment <i>RMB'000</i>	Others <i>RMB'000</i>	Construction in progress <i>RMB'000</i>	Total <i>RMB'000</i>
31 December 2006					
At 1 January 2006:					
Cost	3,844,703	12,044,210	44,720	292,312	16,225,945
Accumulated depreciation	(122,548)	(1,592,809)	(14,697)	—	(1,730,054)
Net carrying amount	3,722,155	10,451,401	30,023	292,312	14,495,891
At 1 January 2006, net of accumulated depreciation					
Cost	3,722,155	10,451,401	30,023	292,312	14,495,891
Additions	43,339	312,750	26,498	2,066,511	2,449,098
Disposals	—	(2,070)	(188)	—	(2,258)
Depreciation provided during the year	(103,587)	(884,930)	(6,738)	—	(995,255)
Transfers	818,718	1,395,024	—	(2,213,742)	—
At 31 December 2006, net of accumulated depreciation	4,480,625	11,272,175	49,595	145,081	15,947,476
At 31 December 2006:					
Cost	4,706,760	13,747,693	70,960	145,081	18,670,494
Accumulated depreciation	(226,135)	(2,475,518)	(21,365)	—	(2,723,018)
Net carrying amount	4,480,625	11,272,175	49,595	145,081	15,947,476

15. PROPERTY, PLANT AND EQUIPMENT (continued)

Group

	Buildings RMB'000	Machinery and equipment RMB'000	Others RMB'000	Construction in progress RMB'000	Total RMB'000
31 December 2005					
At 1 January 2005:					
Cost	2,071,928	7,649,999	32,102	739,406	10,493,435
Accumulated depreciation	(73,717)	(914,080)	(5,725)	—	(993,522)
Net carrying amount	1,998,211	6,735,919	26,377	739,406	9,499,913
At 1 January 2005, net of accumulated depreciation					
Additions	126,576	944,811	8,094	1,654,654	2,734,135
Purchase from the Holding Company (note 34)	1,425,180	1,570,296	4,524	—	3,000,000
Disposals	—	(1,149)	—	—	(1,149)
Depreciation provided during the year	(48,831)	(679,205)	(8,972)	—	(737,008)
Transfers	221,019	1,880,729	—	(2,101,748)	—
At 31 December 2005, net of accumulated depreciation	3,722,155	10,451,401	30,023	292,312	14,495,891
At 31 December 2005:					
Cost	3,844,703	12,044,210	44,720	292,312	16,225,945
Accumulated depreciation	(122,548)	(1,592,809)	(14,697)	—	(1,730,054)
Net carrying amount	3,722,155	10,451,401	30,023	292,312	14,495,891

AUDITED FINANCIAL STATEMENTS

15. PROPERTY, PLANT AND EQUIPMENT (continued)

Company

	Buildings <i>RMB'000</i>	Machinery and equipment <i>RMB'000</i>	Others <i>RMB'000</i>	Construction in progress <i>RMB'000</i>	Total <i>RMB'000</i>
31 December 2006					
At 1 January 2006:					
Cost	3,005,988	9,035,268	35,476	29,377	12,106,109
Accumulated depreciation	(102,797)	(1,190,094)	(10,721)	—	(1,303,612)
Net carrying amount	2,903,191	7,845,174	24,755	29,377	10,802,497
At 1 January 2006, net of accumulated depreciation					
	2,903,191	7,845,174	24,755	29,377	10,802,497
Additions	31,748	189,159	24,595	1,875,369	2,120,871
Disposals to subsidiaries	—	(11,996)	—	—	(11,996)
Disposals	—	(2,070)	—	—	(2,070)
Depreciation provided during the year	(80,614)	(663,209)	(5,007)	—	(748,830)
Transfers	645,573	1,209,702	—	(1,855,275)	—
At 31 December 2006, net of accumulated depreciation					
	3,499,898	8,566,760	44,343	49,471	12,160,472
At 31 December 2006:					
Cost	3,683,309	10,417,450	60,071	49,471	14,210,301
Accumulated depreciation	(183,411)	(1,850,690)	(15,728)	—	(2,049,829)
Net carrying amount	3,499,898	8,566,760	44,343	49,471	12,160,472

15. PROPERTY, PLANT AND EQUIPMENT (continued)

Company

	Buildings RMB'000	Machinery and equipment RMB'000	Others RMB'000	Construction in progress RMB'000	Total RMB'000
31 December 2005					
At 1 January 2005:					
Cost	1,410,628	5,962,120	22,946	98,891	7,494,585
Accumulated depreciation	(59,045)	(696,150)	(3,638)	—	(758,833)
Net carrying amount	1,351,583	5,265,970	19,308	98,891	6,735,752
At 1 January 2005, net of accumulated depreciation					
Additions	128,315	529,575	8,006	1,024,077	1,689,973
Purchase from the					
Holding Company	1,425,180	1,570,296	4,524	—	3,000,000
Disposal to subsidiaries	—	(76,422)	—	—	(76,422)
Disposals	—	(692)	—	—	(692)
Depreciation provided during the year					
Transfers	(43,752)	(495,279)	(7,083)	—	(546,114)
	41,865	1,051,726	—	(1,093,591)	—
At 31 December 2005, net of accumulated depreciation					
	2,903,191	7,845,174	24,755	29,377	10,802,497
At 31 December 2005:					
Cost	3,005,988	9,035,268	35,476	29,377	12,106,109
Accumulated depreciation	(102,797)	(1,190,094)	(10,721)	—	(1,303,612)
Net carrying amount	2,903,191	7,845,174	24,755	29,377	10,802,497

At 31 December 2006, certain of the Group's buildings, machinery and equipment with a value of approximately RMB8,219 million (2005: RMB7,938 million) were pledged to secure certain of the Group's bank loans (note 28).

The carrying amount of construction in progress included capitalised interest of RMB13.3 million (2005: RMB17.7 million) in the current year (note 10) prior to being transferred to buildings, and machinery and equipment.

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16. PREPAID LAND LEASE PAYMENTS

Group

	2006 <i>RMB'000</i>	2005 <i>RMB'000</i>
Carrying amount at 1 January	133,087	123,533
Additions	1,566	12,000
Recognised during the year	(2,796)	(2,446)
Carrying amount at 31 December	131,857	133,087
Current portion included in prepayments, deposits and other receivables	(2,816)	(2,782)
Non-current portion	129,041	130,305

The leasehold lands are held under long term leases and are situated in the PRC.

At 31 December 2006, certain of the Group's land use rights with a net carrying amount of approximately RMB93 million (2005: RMB83 million) were pledged to secure certain of the Group's bank loans (note 28).

17. OTHER INTANGIBLE ASSETS

The intangible assets of the Group represent technology rights of US\$1,450,000 (equivalent to approximately RMB12 million) injected by a minority shareholder to a subsidiary of the Company as its capital contribution in September 2002.

	2006 <i>RMB'000</i>	2005 <i>RMB'000</i>
At 1 January:		
Cost	12,001	12,001
Accumulated amortisation	(3,900)	(2,700)
Net carrying amount	8,101	9,301
At 1 January, net of accumulated amortisation	8,101	9,301
Amortisation provided during the year	(1,200)	(1,200)
At 31 December, net of accumulated amortisation	6,901	8,101
At 31 December:		
Cost	12,001	12,001
Accumulated amortisation	(5,100)	(3,900)
Net carrying amount	6,901	8,101

18. INVESTMENTS IN SUBSIDIARIES

Details of the interests in subsidiaries of the Company are set out below:

	2006 <i>RMB'000</i>	2005 <i>RMB'000</i>
Unlisted investments, at cost	1,200,891	1,200,891
Amounts due from subsidiaries	1,245,392	1,660,119
Amounts due to subsidiaries	(130,125)	(146,635)
	2,316,158	2,714,375

The amounts due from/to subsidiaries are unsecured, interest-free and have no fixed repayment. The carrying amounts of these amounts due from/to subsidiaries approximate to their fair values.

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18. INVESTMENTS IN SUBSIDIARIES (continued)

Particulars of the subsidiaries and joint ventures of the Company as at 31 December 2006 are as follows:

Company name	Place and date of incorporation/ registration and operations	Legal status	Paid-up capital/ registered capital	Percentage of equity interests directly attributable to the Company	Principal activities
<i>Subsidiaries</i>					
Weihai Weiqiao Textile Company Limited ("Weihai Weiqiao")	Weihai, the PRC 25 July 2001	Limited liability company	RMB148,000,000	87.2	Production and sale of cotton yarns and fabrics
Binzhou Industrial Park	Binzhou, the PRC 26 November 2001	Limited liability company	RMB600,000,000	98.5	Production and sale of cotton yarns and fabrics
Shandong Weiqiao Mianye Company Limited	Zouping, the PRC 30 September 2003	Limited liability company	RMB5,000,000	92	Purchase, processing and sale of raw cotton, cotton seeds and lint cotton
Weihai Weiqiao Industrial Park Company Limited ("Weihai Industrial Park")	Weihai, the PRC 30 January 2004	Limited liability company	RMB260,000,000	99.8	Production and sale of cotton yarns and fabrics
<i>Joint ventures</i>					
Luteng Textile	Zouping, the PRC 12 September 2002	Sino-foreign equity joint venture	US\$9,790,000	75	Production and sale of polyester yarns and related products
Binteng Textile	Zouping, the PRC 12 March 2004	Sino-foreign equity joint venture	US\$15,430,000	75	Production and sale of compact yarns and related products

19. INVENTORIES

	Group	
	2006 RMB'000	2005 RMB'000
Raw materials	1,373,129	791,186
Work in progress	736,605	644,315
Semi-finished goods	610,217	636,778
Finished goods	616,999	1,098,061
Consumables	72,926	71,657
Raw materials in transit	167,688	403,231
	3,577,564	3,645,228

	Company	
	2006 RMB'000	2005 RMB'000
Raw materials	1,151,577	620,494
Work in progress	563,694	491,680
Semi-finished goods	370,548	455,238
Finished goods	426,100	892,660
Consigned materials for processing	15,929	22,699
Consumables	53,531	59,447
Raw materials in transit	167,688	403,231
	2,749,067	2,945,449

As at 31 December 2006, there was no raw material in transit secured for the Group's bank loans.

Certain of the Group's raw materials in transit of approximately RMB141 million as at 31 December 2005 were utilised to secure certain of the Group's bank loans, as further detailed in note 28 to the financial statements.

AUDITED FINANCIAL STATEMENTS

20. TRADE RECEIVABLES

An aged analysis of the trade receivables as at the balance sheet date, based on the invoice date, is as follows:

	Group	
	2006 RMB'000	2005 RMB'000
Within 3 months	686,039	546,539
3 to 6 months	2,745	7,610
6 months to 1 year	674	3,765
1 to 2 years	4,380	4,358
	693,838	562,272

	Company	
	2006 RMB'000	2005 RMB'000
Within 3 months	651,966	524,442
3 to 6 months	2,745	7,564
6 months to 1 year	674	3,765
1 to 2 years	4,380	4,358
	659,765	540,129

The Group normally allows a credit period of not more than 45 days to its customers, although an extension of the credit period is not uncommon for customers with a long term relationship. The Group seeks to maintain strict control over its outstanding receivables. Overdue balances are reviewed regularly by senior management. In view of the aforementioned and the fact that the Group's trade receivables relate to a large number of diversified customers, there is no significant concentration of credit risks. Trade receivables are non-interest-bearing.

As at 31 December 2006, there was no trade receivables secured for the Group's bank loans.

Certain of the Group's trade receivables of approximately RMB111 million at 31 December 2005 were pledged to secure general bank loans granted to the Group(note 28).

21. PREPAYMENTS, DEPOSITS AND OTHER RECEIVABLES

	Group	
	2006 RMB'000	2005 RMB'000
Prepayments to suppliers	52,725	446,216
Prepaid land lease payments, current portion	2,816	2,782
Export value-added tax refundable	—	63
Other receivables and prepayments	505	9,534
	56,046	458,595

	Company	
	2006 RMB'000	2005 RMB'000
Prepayments to suppliers	45,484	445,687
Other receivables and prepayments	85	8,969
	45,569	454,656

22. AMOUNTS DUE FROM/TO THE IMMEDIATE HOLDING COMPANY/RELATED PARTIES

The balances with the immediate holding company are unsecured, interest-free and have no fixed repayment terms. The balances with related parties are unsecured, interest-free and have specific repayment terms.

AUDITED FINANCIAL STATEMENTS

23. CASH AND CASH EQUIVALENTS, PLEDGED DEPOSITS AND TIME DEPOSITS MATURING OVER THREE MONTHS

	Group	
	2006 RMB'000	2005 RMB'000
Cash and bank balances	3,953,465	3,134,935
Time deposits	1,644,689	1,717,178
	5,598,154	4,852,113
Less: Pledged time deposits:		
Pledged for letter of credit facilities	(106,526)	(470,000)
Pledged for bank loans (note 28)	—	(42,138)
	(106,526)	(512,138)
Non-pledged time deposits maturing over three months	(1,281,914)	(1,154,040)
Cash and cash equivalents	4,209,714	3,185,935

	Company	
	2006 RMB'000	2005 RMB'000
Cash and bank balances	3,703,444	2,872,886
Time deposits	1,632,890	1,717,178
	5,336,334	4,590,064
Less: Pledged time deposits:		
Pledged for letter of credit facilities	(94,727)	(470,000)
Pledged for bank loans (note 28)	—	(42,138)
	(94,727)	(512,138)
Non-pledged time deposits maturing over three months	(1,281,914)	(1,154,040)
Cash and cash equivalents	3,959,693	2,923,886

23. CASH AND CASH EQUIVALENTS, PLEDGED DEPOSITS AND TIME DEPOSITS MATURING OVER THREE MONTHS (continued)

Cash at banks earn interest at floating rates based on daily bank deposit rates. Short term time deposits are made for varying periods of one day to six months depending on the immediate cash requirements of the Group, and earn interest at the respective short term time deposit rates. The carrying amounts of the cash and cash equivalents, the pledged time deposits and the non-pledged time deposits maturing over three months approximate to their fair values.

24. TRADE PAYABLES

An aged analysis of the trade payables as at the balance sheet date, based on the date of transferring the significant risks and rewards of ownership of raw materials and items of property, plant and equipment to the Group, is as follows:

	Group	
	2006 RMB'000	2005 RMB'000
Within 3 months	627,038	1,944,107
3 to 5 months	50,139	99,186
5 months to 1 year	78,536	200,798
Over 1 year	32,830	—
	788,543	2,244,091

	Company	
	2006 RMB'000	2005 RMB'000
Within 3 months	553,676	1,802,599
3 to 5 months	46,553	98,068
5 months to 1 year	78,336	199,119
Over 1 year	31,632	—
	710,197	2,099,786

Trade payables are non-interest-bearing.

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25. BILLS PAYABLE

	Group	
	2006 RMB'000	2005 RMB'000
Within 3 months	290,000	499,300
3 to 6 months	370,000	90,000
	660,000	589,300

	Company	
	2006 RMB'000	2005 RMB'000
Within 3 months	210,000	449,300
3 to 6 months	290,000	—
	500,000	449,300

Certain of the Group's bills payable amounting to RMB160 million as at 31 December 2006 were drawn by Weihai Industrial Park in favour of the Company and were discounted with banks by the Company prior to 31 December 2006.

Certain of the Group's bills payable amounting to RMB430 million as at 31 December 2006 were drawn by the Company in favour of Binzhou Industrial Park and were discounted with banks by Binzhou Industrial Park prior to 31 December 2006.

Certain of the Group's bills payable amounting to RMB140 million as at 31 December 2005 were drawn by Weihai Weiqiao and Weihai Industrial Park in favour of the Company and were discounted with banks by the Company prior to 31 December 2005.

26. OTHER PAYABLES AND ACCRUALS

	Group	
	2006 RMB'000	2005 RMB'000
Payroll payable	206,288	171,832
Welfare payable	549,046	326,005
Other taxes payable	183,022	128,470
Accruals	77,145	16,784
Other payables	374,807	198,267
	1,390,308	841,358

	Company	
	2006 RMB'000	2005 RMB'000
Payroll payable	150,926	134,610
Welfare payable	418,993	252,718
Other taxes payable	139,455	97,770
Accruals	74,714	16,500
Other payables	237,026	130,485
	1,021,114	632,083

Other payables are non-interest-bearing.

AUDITED FINANCIAL STATEMENTS

27. DERIVATIVE FINANCIAL INSTRUMENTS

	Group and Company			
	Assets		Liabilities	
	2006 <i>RMB'000</i>	2005 <i>RMB'000</i>	2006 <i>RMB'000</i>	2005 <i>RMB'000</i>
Forward currency contract	—	—	—	1,323
Interest rate swaps	5,524	8,243	9,742	4,781
	5,524	8,243	9,742	6,104

The carrying amounts of the forward currency contract and interest rate swap of the Group and the Company are the same as their fair values.

The Company has entered into one forward currency contract and various interest rate swap contracts to manage its exchange rate exposures and interest rate exposures, respectively, which did not meet the criteria for hedge accounting.

During the year, the increase and decrease in the fair values of non-hedging currency derivatives and interest rate swap derivatives amounting to RMB1,323,000 and RMB7,680,000, respectively, were credited and charged to the consolidated income statement, respectively. During the prior year, the decrease and increase in the fair values of non-hedging currency derivatives and interest rate swap derivatives amounting to RMB1,323,000 and RMB3,462,000, respectively, were charged and credited to the consolidated income statement respectively.

28. INTEREST-BEARING BANK LOANS

	Effective interest rat	Maturity	Group		Company	
			2006 RMB'000	2005 RMB'000	2006 RMB'000	2005 RMB'000
Current:						
Unsecured	(1)	2007	1,667,945	2,893,584	1,350,431	2,670,514
Secured	(2)	2007	2,272,297	2,241,828	1,633,995	1,864,828
			3,940,242	5,135,412	2,984,426	4,535,342
Non-current:						
Unsecured	(3)	2008-2009	2,832,453	326,281	2,622,453	32,281
Secured	(4)	2008-2010	2,956,931	4,229,229	2,588,931	3,971,229
			5,789,384	4,555,510	5,211,384	4,003,510
			9,729,626	9,690,922	8,195,810	8,538,852

- (1) The interest rates of these loans range from 5.3100% to 8.2872% per annum, at three-month LIBOR+1.4%, at three-month LIBOR+1.5%, at six-month LIBOR+1.1% and at one-year SIBOR+1.75%.
- (2) The interest rates of these loans range from 5.3100% to 7.9560% per annum, at three-month LIBOR+2%, and at three-month LIBOR+2.5%.
- (3) The interest rates of these loans range from 5.3010% to 7.3440% per annum, at three-month LIBOR+1.4%, at six-month LIBOR+1.1%, and at three-month SIBOR+1.75%.
- (4) The interest rates of these loans range from 5.3100% to 8.7350% per annum, at three-month LIBOR+2.2%, at three-month LIBOR+2.5% and at one-year LIBOR+3%.

	Group		Company	
	2006 RMB'000	2005 RMB'000	2006 RMB'000	2005 RMB'000
Analysed into:				
Bank loans repayable:				
Within one year	3,940,242	5,135,412	2,984,426	4,535,342
In the second year	2,458,388	2,342,780	2,146,388	2,102,781
In the third to fifth years, inclusive	3,330,996	2,212,730	3,064,996	1,900,729
	9,729,626	9,690,922	8,195,810	8,538,852

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28. INTEREST-BEARING BANK LOANS (continued)

- (i) Other than certain of the Group's bank loans in the aggregate amount of US\$485 million equivalent to RMB3,787 million at 31 December 2006 (2005: US\$431 million and HK\$110 million), all of the Group's bank loans are denominated in RMB.
- (ii) On 8 September 2004, the Company entered into a loan agreement (the "First Syndicate Loan Agreement") with a syndicate of banks for a three-year term loan facility of up to US\$78 million (equivalent to approximately RMB629 million) and RMB183 million. On 1 August 2005, the Company entered into another syndicate loan agreement (the "Second Syndicate Loan Agreement") for a three-year term loan facility of up to US\$125 million (equivalent to approximately RMB1,009 million).

On 11 August 2006, the Company entered into a three-year term loan facility (the "Third Syndicate Loan Agreement") with a syndicate of banks. The facility provides that the Company may borrow up to US\$280 million. According to the terms of the Third Syndicate Loan Agreement, the Company firstly used the proceeds borrowed under the Third Syndicate Loan Agreement to repay in full all outstanding borrowings under the First Syndicate Loan Agreement and the Second Syndicate Loan Agreement and apply the remaining balance for general funding purposes. In addition, the Third Syndicate Loan Agreement contains certain undertakings and financial covenants including, but not limited to a minimum level of consolidated tangible net worth, a maximum level of consolidated total debts and consolidated total secured debts, and the maintenance of net consolidated current assets and certain financial ratios. As of 18 August 2006, an aggregate of US\$280 million (equivalent to approximately RMB2,233 million) has been drawn down under the facility of the Third Syndicate Loan Agreement. The outstanding balance under the First Syndicate Loan Agreement of RMB109.8 million and US\$46.8 million (equivalent to approximately RMB373.2 million) and the Second Syndicate Loan Agreement of US\$111.1 million (equivalent to approximately RMB886 million) were repaid subsequently in August 2006.

- (iii) Certain of the Group's bank loans amounting to approximately RMB5,229 million (2005: RMB6,205 million) were secured by certain of the Group's buildings, machinery and equipment, and land use rights (prepaid land lease payments) of an aggregate net carrying value of approximately RMB8,312 million (2005: RMB8,021 million) as at 31 December 2006.
- (iv) Certain of the Group's bank loans amounting to approximately RMB40 million were secured by certain of the Group's pledged deposits of approximately RMB42 million as at 31 December 2005.
- (v) Certain of the Group's bank loans of RMB85 million were secured by its trade receivables of RMB111 million as at 31 December 2005.
- (vi) Certain of the Group's bank loans up to approximately RMB141 million were secured by certain of the Group's raw materials in transit of approximately RMB141 million as at 31 December 2005.
- (vii) Weihai Civil Aviation Industrial Company Limited, the minority shareholder of Weihai Weiqiao, guaranteed bank loans of Weihai Weiqiao of up to approximately RMB10 million (2005: RMB10 million) as at 31 December 2006.
- (viii) Liu Guangmin, the minority shareholder of Weiqiao Industrial Park, guaranteed bank loans of Weihai Industrial Park of up to approximately RMB1 million (2005: RMB1 million) as at 31 December 2006.
- (ix) The Company guaranteed bank loans of certain of its subsidiaries up to approximately RMB344 million (2005: RMB506 million) as at 31 December 2006.
- (x) Given the non-compliance with the Listing Rules (as fully described in Note 37(d) below), the Company has obtained the waivers for breach of loan covenants from a commercial bank and the Agent of the Third Syndicate Loan Agreement on 27 December 2006 and 30 December 2006, respectively.

28. INTEREST-BEARING BANK LOANS (continued)

Other interest rate information:

	Group			
	2006		2005	
	Fixed rate RMB'000	Floating rate RMB'000	Fixed rate RMB'000	Floating rate RMB'000
Bank loans:				
Unsecured	783,396	3,717,002	967,641	2,252,224
Secured	2,312,603	2,916,625	2,368,135	4,102,922
	3,095,999	6,633,627	3,335,776	6,355,146

	Company			
	2006		2005	
	Fixed rate RMB'000	Floating rate RMB'000	Fixed rate RMB'000	Floating rate RMB'000
Bank loans:				
Unsecured	403,396	3,569,488	695,571	2,007,224
Secured	1,594,301	2,628,625	1,907,135	3,928,922
	1,997,697	6,198,113	2,602,706	5,936,146

The carrying amounts of the Group's and the Company's current bank loans approximate to their fair values. The carrying amounts and fair value of the Group's non-current bank loans are as follows:

	Carrying amounts		Fair value	
	2006 RMB'000	2005 RMB'000	2006 RMB'000	2005 RMB'000
Fixed rate bank loans	1,218,800	1,469,825	1,195,358	1,426,865
Floating rate bank loans	4,570,584	3,085,685	4,570,584	3,085,685
	5,789,384	4,555,510	5,765,942	4,512,550

The fair value of the Company's secured bank loans (non-current portion) with a carrying amount of RMB888,800,000 (2005: RMB1,075,825,000) was RMB868,556,000 (2005: RMB1,045,031,000) at the balance sheet date.

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29. LONG TERM PAYABLE TO THE IMMEDIATE HOLDING COMPANY

	Group and Company	
	2006 RMB'000	2005 RMB'000
Amounts repayable:		
Within one year	137,103	50,000
In the second year	—	368,927
Portion classified as current liabilities	137,103 (137,103)	418,927 (50,000)
Non-current portion	—	368,927

The Group made repayments in the aggregate amount of RMB273,927,000 to the immediate holding company in 2006, including repayments of RMB223,927,000 ahead of the due date in 2007.

The long term payable balances to the immediate holding company as at 31 December 2006 and 31 December 2005 were unsecured and interest-free.

30. DEFERRED INCOME

Deferred income recognised in the consolidated balance sheet, arising from the government grants received by Binzhou Industrial Park, is as follows:

	Group	
	2006 RMB'000	2005 RMB'000
At 1 January	83,567	—
Addition	22,072	84,163
Recognised as income during the year	(4,148)	(596)
At 31 December	101,491	83,567
Portion classified as current liabilities	(5,151)	(3,574)
Non-current portion	96,340	79,993

Binzhou Industrial Park received government grants during prior years and the current year amounting to RMB84 million and RMB22 million, respectively. The grants were provided by the Finance Bureau of the Binzhou City for the purpose of providing support for the development of Binzhou Industrial Park and product development. Since Binzhou Industrial Park fulfilled the conditions attaching to the government grants in 2006 and 2005, which were confirmed by the Finance Bureau of the Binzhou City, the Group recognised the government grants as deferred income over the expected useful lives of the relevant fixed assets to which the grants related by equal annual instalments.

AUDITED FINANCIAL STATEMENTS

31. DEFERRED TAX

The movements in the deferred tax assets and liabilities during the year are as follows:

	Group		Company	
	2006 RMB'000	2005 RMB'000	2006 RMB'000	2005 RMB'000
Deferred tax assets				
At 1 January	61,422	—	19,655	—
Credited to the consolidated income statement during the year	59,622	61,422	52,261	19,655
At 31 December	121,044	61,422	71,916	19,655
Deferred tax liabilities				
At 1 January	8,381	—	—	—
Credited to the consolidated income statement during the year	(300)	8,382	—	—
At 31 December	8,082	8,382	—	—
Credited to the consolidated income statement, net (note 11)	59,922	53,040	52,261	19,655

31. DEFERRED TAX (continued)

The principal components of the Group's and the Company's deferred tax are as follows:

	Group		Company	
	2006 RMB'000	2005 RMB'000	2006 RMB'000	2005 RMB'000
Deferred tax assets				
Provision against inventories	60,413	27,460	45,474	13,758
Impairment of trade receivables	7,626	7,831	7,138	7,343
Net fair value losses/(gains) of derivative financial instruments	1,392	(706)	1,392	(706)
Government grants recognised as deferred income	33,492	27,577	—	—
Difference in depreciation for tax purposes	12,480	(7,623)	12,271	(7,623)
Fair value adjustment to the long term payable to the immediate holding company	(2,606)	—	(2,606)	—
Others	8,247	6,883	8,247	6,883
At 31 December	121,044	61,422	71,916	19,655
Deferred tax liabilities				
Difference in depreciation for tax purposes	8,082	8,382	—	—
At 31 December	8,082	8,382	—	—

There was no material unprovided deferred tax during the year.

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32. SHARE CAPITAL

	2006 RMB'000	2005 RMB'000
Shares		
Registered, issued and fully paid:		
780,770,000 (2005: 780,770,000) domestic shares of RMB1.00 each	780,770	780,770
413,619,000 (2005: 344,682,500) H shares of RMB1.00 each	413,619	344,683
	1,194,389	1,125,453

The Company does not have any share option scheme.

During the current and prior years, the movements in share capital were as follows:

- (a) In 2006, 68,936,500 H shares of the Company with a par value of RMB1.00 each were issued to the public by way of placing at a price of HK\$12.05 (equivalent to approximately RMB12.49) per H Share. These H shares were listed on the Hong Kong Stock Exchange in March 2006.
- (b) In 2005, 250,000,000 domestic shares of the Company with a par value of RMB1.00 each were issued to the Holding Company as part of the consideration for the acquisition of the thermal power assets at a price of RMB10.84 (equivalent to approximately HK\$10.40) per domestic share.

A summary of the transactions during the current and prior year with reference to the above movements of the Company's ordinary share capital is as follows:

	Number of shares in issue	Issued share capital RMB'000	Capital reserve account RMB'000	Total RMB'000
At 1 January 2005	875,452,500	875,453	3,424,199	4,299,652
Issue of domestic shares (b)	250,000,000	250,000	2,460,000	2,710,000
At 1 January 2006	1,125,452,500	1,125,453	5,884,199	7,009,652
Issue of H shares (a)	68,936,500	68,936	791,174	860,110
	1,194,389,000	1,194,389	6,675,373	7,869,762
Share issue expenses	—	—	(1,994)	(1,994)
At 31 December 2006	1,194,389,000	1,194,389	6,673,379	7,867,768

33. RESERVES

Group

The amounts of the Group's reserves and the movements therein for the current and prior year are presented in the consolidated statement of changes in equity on pages 54 to 55 of this annual report.

Company

	Capital reserve <i>RMB'000</i>	Statutory surplus reserve <i>RMB'000</i>	Statutory public welfare fund <i>RMB'000</i>	Retained profits <i>RMB'000</i>	Proposed final dividend <i>RMB'000</i>	Total <i>RMB'000</i>
At 1 January 2005	3,424,199	184,082	184,082	1,067,231	218,863	5,078,457
Final 2004 dividend declared	—	—	—	—	(218,863)	(218,863)
Issue of domestic shares (note 32(b))	2,460,000	—	—	—	—	2,460,000
Profit for the year (note 12)	—	—	—	1,154,290	—	1,154,290
Transfer from/(to) reserves	—	117,937	117,937	(235,874)	—	—
Proposed final 2005 dividend (note 13(b))	—	—	—	(323,005)	323,005	—
At 1 January 2006	5,884,199	302,019	302,019	1,662,642	323,005	8,473,884
Final 2005 dividend declared	—	—	—	—	(342,790)	(342,790)
Dividend relating to additional issuance of shares	—	—	—	(19,785)	19,785	—
Issue of H Shares (note 32(a))	791,174	—	—	—	—	791,174
Share issue expense	(1,994)	—	—	—	—	(1,994)
Transfer of the statutory public welfare fund to the statutory surplus reserve	—	302,019	(302,019)	—	—	—
Profit for the year (note 12)	—	—	—	1,606,166	—	1,606,166
Transfer from/(to) reserves	—	167,909	—	(167,909)	—	—
Proposed final 2006 dividend (note 13(b))	—	—	—	(525,531)	525,531	—
At 31 December 2006	6,673,379	771,947	—	2,555,583	525,531	10,526,440

34. NOTE TO THE CONSOLIDATED CASH FLOW STATEMENT

Major non-cash transactions

During 2005, the Company acquired certain thermal power assets from the Holding Company at an aggregate consideration of RMB3,000 million which was satisfied as to RMB2,710 million (equivalent to approximately HK\$2,601 million) by way of the allotment and issue of 250,000,000 domestic shares and RMB290 million (equivalent to approximately HK\$278 million) by two cash instalments payable in 2007.

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35. CONTINGENT LIABILITIES

At the balance sheet date, the Group's and the Company's contingent liabilities not provided for in the financial statements were as follows:

	Group	
	2006 <i>RMB'000</i>	2005 <i>RMB'000</i>
Letters of credit issued	128,342	497,740
	Company	
	2006 <i>RMB'000</i>	2005 <i>RMB'000</i>
Letters of credit issued	128,342	497,740
Guarantees given to banks in connection with facilities granted to subsidiaries	344,210	506,199
	472,552	1,003,939

36. COMMITMENTS

(a) Capital commitments

At the balance sheet date, the Group and the Company had the following capital commitments, principally for construction in progress, the acquisition of items of property, plant and equipment and equity investments:

	Group	
	2006 RMB'000	2005 RMB'000
Contracted, but not provided for	573,534	65,451
Authorised, but not contracted for	89,914	270,570
	663,448	336,021

	Company	
	2006 RMB'000	2005 RMB'000
Contracted, but not provided for	548,534	40,451
Authorised, but not contracted for	89,914	40,000
	638,448	80,451

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36. COMMITMENTS (continued)

(b) Operating lease commitments

At the balance sheet date, the Group and the Company had the following total future minimum lease payments under non-cancellable operating leases in respect of land and buildings:

	Group	
	2006 RMB'000	2005 RMB'000
Within one year	19,237	12,235
In the second to fifth years, inclusive	75,800	48,395
After five years	238,048	149,332
	333,085	209,962

	Company	
	2006 RMB'000	2005 RMB'000
Within one year	19,176	12,175
In the second to fifth years, inclusive	75,558	48,152
After five years	237,399	148,622
	332,133	208,949

37. RELATED PARTY TRANSACTIONS

The Group is part of a larger group of companies under ZCSU and has extensive transactions and relationships with the members of ZCSU. As such, it is possible that the terms of these transactions are not the same as those that would result from transactions among the wholly unrelated parties. Related parties refer to entities of which ZCSU is a shareholder and is able to exercise control or significant influence. The transactions were made on terms agreed between the parties.

In addition to the transactions and balances disclosed in notes 22, 28 and 29 to these financial statements during the year, the Group had the following transactions with related parties:

(a) Transactions with related parties

Name of related parties	Relationship with the Company	Nature of transactions	2006 RMB'000	2005 RMB'000
The Holding Company	The immediate holding company	Expenses on provision of electricity and steam	75,051	701,925
		Expenses on property leasing	16,902	9,986
		Revenue on supply of electricity	206,372	36,816
		Settlement of liabilities by the Holding Company on behalf of the Group	—	27,835
		Settlement of liabilities by the Group on behalf of the Holding Company	—	46,531
Shandong Weiqiao Dyeing and Weaving Co., Ltd.	A fellow subsidiary	Sale of cotton yarns	205,544	242,315
		Revenue on plant and equipment leasing	1,000	250
Shandong Weilian Printing and Dyeing Co., Ltd.	A fellow subsidiary	Sale of grey fabrics	257,677	126,870
Shandong Weiqiao Bleaching-Dyeing Co., Ltd.	An associate of the Holding Company	Sale of cotton yarns	19,594	8,713
Shandong Hengfu Knitting Co., Ltd.	A fellow subsidiary	Sale of cotton yarns	58,807	33,646

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37. RELATED PARTY TRANSACTIONS (continued)

(a) Transactions with related parties (continued)

Name of related parties	Relationship with the Company	Nature of transactions	2006 RMB'000	2005 RMB'000
Shandong Weiqiao Hongyuan Home Textile, Ltd.	A fellow subsidiary	Sale of grey fabrics	14,408	531
Shandong Weiqiao Tekuanfu Co., Ltd.	A fellow subsidiary	Sale of grey fabrics	77,156	4,882
Shandong Weiqiao Clothes Co., Ltd.	A fellow subsidiary	Sale of denims	1,146	83
Shandong Weiqiao Elite Garment Co., Ltd.	A fellow subsidiary	Sale of grey fabrics	582	—

In preparation for listing of the Company, the Company and the Holding Company entered into a supply agreement (the "Old Supply Agreement") on 25 August 2003, pursuant to which (i) the Company has agreed to supply or procure its subsidiaries to supply cotton yarns and grey fabrics to the Holding Company and its subsidiaries other than the companies now comprising the Group (collectively referred to as the "Holding Group"); and (ii) the Holding Company has agreed to supply cotton to the Group and to provide, or procure its subsidiaries and/or associates to provide, cotton yarns and grey fabrics downstream processing services to the Group, for a term of three years commencing from 25 August 2003. On 25 August 2006 the Old Supply Agreement was renewed based on the same terms and conditions for a period of three years commencing from 25 August 2006 in accordance with the automatic renewal mechanism set out in the Old Supply Agreement. Pursuant to the renewed supply agreement, the Group has supplied and will continue to supply cotton yarns and grey fabrics to the Holding Group; however, the Holding Group has not and will not supply cotton to the Group, and has not and will not provide downstream processing services to the Group.

37. RELATED PARTY TRANSACTIONS (continued)

(a) Transactions with related parties (continued)

Also, in the preparation for listing of the Company, the Company and the Holding Company entered into a supply of electricity and steam agreement on 25 August 2003. Pursuant to the agreement, the Holding Company agreed to supply electricity and steam to the Group, at the lower of the market price and RMB0.35 per kWh (including VAT at the rate of 17%) for electricity, and at the lower of the market price and RMB60 per ton (including VAT at the rate of 13%) for steam. Pursuant to the supplemental agreement of the supply of electricity and steam dated 31 May 2005, it was agreed that if the aggregate amount of electricity and steam to be purchased by the Group from the Holding Company in any financial year of the Company were equal to or less than that purchased for the financial year ended 31 December 2004 (the "Planned Electricity and Steam Purchase"), the price for the Planned Electricity and Steam Purchase shall be either the lower of RMB0.35 per kWh (including VAT at the rate of 17%) and RMB60 per ton (including VAT at the rate either of 13%) or the then prevailing market price. The price for any excess purchase shall be adjusted, but must not be higher than the then prevailing market price.

On 13 August 2005, the Company entered into an asset transfer agreement (the "Assets Transfer Agreement") with the Holding Company to acquire the thermal power assets at an aggregate consideration of RMB3,000,000,000 (equivalent to approximately HK\$2,879,000,000) (note 34). On 27 October 2005, the Company obtained the new business licence indicating the increased registered capital of the Company from the Shandong Provincial Administration Bureau for Industry and Commerce, entering the completion of the Asset Transfer Agreement (the "Completion").

Upon the Completion, the Company and the Holding Company entered into a supply of excess electricity agreement on 2 November 2005, pursuant to which the Company has the right to supply electricity which is in excess of the Group's actual consumption, to the Holding Company for a term commencing from the date of Completion and ending on 31 December 2007. The price at which the excess electricity is supplied to the Holding Company by the Group shall be RMB0.45 per kWh (including VAT at the rate of 17%) or the price then at which a power plant in Shandong Province would sell its electricity produced to the relevant power grid (such price is currently ranging from RMB0.37 per kWh to RMB0.40 per kWh), whichever is higher. However, if any applicable mandatory price for the electricity is announced by the PRC government, such mandatory price would be adopted instead.

Up to 31 December 2006, the Group has entered into twelve property lease agreements with the Holding Company, with a right of renewal exercisable by the Group. The significant terms of such agreements are summarised as follows:

- (i) Land use rights lease agreement dated 27 December 2000 with the commencement date and expiry date on 27 December 2000 and 27 December 2020, respectively, at an annual rental of RMB454,900 for the land relating to Weiqiao First Production Area.
- (ii) Land use rights lease agreement dated 10 May 2001 with the commencement date and expiry date on 10 May 2001 and 10 May 2021, respectively, at an annual rental of RMB868,000 for the land relating to Weiqiao First Production Area.

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37. RELATED PARTY TRANSACTIONS (continued)

(a) Transactions with related parties (continued)

- (iii) Land use rights lease agreement dated 30 September 2002 with the commencement date and expiry date on 30 September 2002 and 30 September 2022, respectively, at an annual rental of RMB888,700 for the land relating to Weiqiao Second Production Area.
- (iv) Land use rights lease agreement dated 14 May 2003 with the commencement date and expiry date on 14 May 2003 and 14 May 2023, respectively, at an annual rental of RMB1,503,000 for the land relating to Weiqiao Third Production Area.
- (v) Land use rights lease agreement dated 13 September 2002 with the commencement date and expiry date on 13 September 2002 and 13 September 2022, respectively, at an annual rental of RMB60,700 for the land relating to a production plant of Luteng Textile.
- (vi) Operating lease agreement related to a building dated 10 May 2000 with the commencement date and expiry date on 10 May 2000 and 10 May 2006, respectively, at an annual rental of RMB600,000 for a building located at No. 34 Qidong Road, Weiqiao Town, Zouping County, Shandong Province, the PRC. The Company and the Holding Company terminated this agreement on 31 January 2005.
- (vii) Land use rights lease agreement dated 17 October 2003 with the commencement date and expiry date on 17 October 2003 and 17 October 2023, respectively, at an annual rental of RMB2,167,000 for the land relating to the Zouping Industrial Park Area.
- (viii) Land use rights lease agreement dated 17 October 2003 with the commencement date and expiry date on 17 October 2003 and 17 October 2023, respectively, at an annual rental of RMB994,100 for the land relating to the Zouping Industrial Park Area.
- (ix) Land use rights lease agreement dated 17 October 2003 with the commencement date and expiry date on 17 October 2003 and 17 October 2023, respectively, at an annual rental of RMB2,000,000 for the land relating to the Zouping Industrial Park Area.
- (x) Operating lease agreement dated 31 January 2005 with the commencement date and expiry date on 1 February 2005 and 1 February 2010, respectively, at an annual rental of RMB600,000 for a building located at No. 1, Weifang Road, Economic Development Zone, Zouping County, Shandong Province, the PRC.
- (xi) Land use rights lease agreement dated 2 November 2005 with the commencement date and expiry date on 31 October 2005 and 31 October 2025, respectively, at an annual rental of RMB2,699,000, which is subject to annual adjustment, for the land relating to the thermal power assets acquired from the Holding Company.
- (xii) Land use rights lease agreement dated 1 May 2006 with the commencement date and expiry date on 1 May 2006 and 1 May 2026, respectively, at an annual rental of RMB7,001,000 for the land relating to the Zouping Industrial Park Area .

37. RELATED PARTY TRANSACTIONS (continued)

(b) *Outstanding balances with related parties included in the consolidated balance sheet*

	Due from related parties		Due to related parties	
	2006 RMB'000	2005 RMB'000	2006 RMB'000	2005 RMB'000
The Holding Company	—	—	299,901	720,221
Fellow subsidiaries	5,044	480,814	7,980	864
An associate of the Holding Company	—	1,782	1,280	—

(c) *Compensation of key management personnel of the Group:*

	2006 RMB'000	2005 RMB'000
Short term employee benefits	5,100	4,306
Post-employment benefits	68	28
Share-based payments	—	—
Total compensation paid to key management personnel	5,168	4,334

Further details of directors' and supervisor's remuneration are included in note 8 to the financial statements.

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37. RELATED PARTY TRANSACTIONS (continued)

- (d) On 28 December 2006 and 15 January 2007, the Company made an announcement and a circular, respectively, on “Continuing Connected Transactions (Supply of Cotton Yarn and Cotton Fabric)”. According to the announcement and the circular (collectively, the “Announcements”), the Company announced, among others, that on 25 August 2006, it has renewed the Old Supply Agreement dated 25 August 2003 on the same terms and conditions for a period of three years commencing from 25 August 2006 in accordance with the automatic renewal mechanism set out in the Old Supply Agreement (the “Renewed Supply Agreement”). According to the terms of the Old Supply Agreement, the renewal of the Old Supply Agreement applies to the supply of cotton yarn and cotton fabric by the Group to Holding Group as well as the provision of cotton yarn and grey fabric downstream processing activities by Holding Group to the Group but does not apply to the supply of cotton (including lint cotton and tailings) by the Holding Company to the Group. In the Announcements, the Company also disclosed that it has complied with the reporting requirements but not the announcement and independent shareholders’ approval requirements under the Listing Rules in respect of the transactions under the Renewed Supply Agreement. Pursuant to an ordinary resolution in an extraordinary general meeting on 2 March 2007, among others, the continuing connected transactions carried out by the Company during the year ended 31 December 2006 under the Renewed Supply Agreement with the Holding Company on 25 August 2006 for a period of three years commencing from 25 August 2006 on the same terms and conditions as the Old Supply Agreement and also, the estimated maximum values of the annual aggregate supply of cotton yarn and cotton fabric by the Group to the Holding Group as set out in the Announcements for each of the three years ending 31 December 2008 were approved, ratified and confirmed by the independent shareholders.

The related party transactions mentioned above also constitute connected transactions or continuing connected transactions as defined in Chapter 14A of the Listing Rules.

38. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

The main risks arising from the Group’s financial assets and liabilities are cash flow interest rate risk, foreign currency risk, credit risk and liquidity risk. The Group does not have written risk management policies and guidelines. However, the Company’s management periodically analyses and formulates strategies to manage the Group’s exposure to financial risk. Generally, the Group introduces conservative strategies on its risk management. The Group’s accounting policies in relation to derivative financial instruments are set out in note 2.4 to the financial statements.

Cash flow interest rate risk

The Group’s exposure to the risk of changes in market interest rates relates primarily to the Group’s long term debt obligations with floating interest rates.

The Group’s policy is to manage its interest cost using a mix of fixed and variable rate debts. To manage this mix in a cost-effective manner, the Group enters into interest rate swaps, in which the Group agrees to exchange, at specified intervals, the difference between fixed and variable rate interest amounts calculated by reference to an agreed-upon notional principal amount. These interest rate swaps can reduce part of interest rate risk of the underlying debt obligations to some extent.

38. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (continued)

Foreign currency risk

The Group has transactional currency exposures. Such exposures arise from sales, purchases and borrowings of the Group in United States dollars (“US\$”). The Group is exposed to foreign currency risk arising from the fluctuation of the exchange rate of US\$. Considering that the fluctuation of exchange rate between US\$ and RMB is not significant, the Group believes its exposure to exchange rate risk is not significant. The Group has also entered into one foreign forward contract to reduce part of the foreign currency exposure to some extent.

Credit risk

Credit risk arises from the possibility that the counterparty of a transaction is unwilling or unable to fulfil its obligation and the Group thereby suffers financial loss.

The credit limits of trade receivable are determined and monitored by management on an ongoing basis. In addition, at each balance sheet date, the Group reviews the recoverable amount of each individual trade debt to ensure that adequate impairment losses are made for irrevocable amounts. Therefore, the Group's exposure to bad debt is not significant.

The credit risk of the Group's other financial assets, which comprises cash and cash equivalents and certain derivative instruments, arises from default of the counterparty with a maximum exposure equal to the carrying amounts of these instruments.

Liquidity risk

The objective of liquidity management is to ensure sufficient cash flows to meet all financial commitments and to capitalise on opportunities for business expansion. This includes the Group's ability to meet operation demand, to repay borrowings as they mature, and to make new loans and investments as opportunities arise. Liquidity is managed on a daily basis by the finance department under the direction of the general manager and financial controller. The finance department is responsible for ensuring that the Group has adequate liquidity for all operations. The Group manages liquidity risk by holding sufficient liquid assets (mainly cash) of appropriate quality to ensure that short term funding requirements are covered within prudent limits. Adequate standby facilities are maintained to provide strategic liquidity to meet unexpected and material cash outflows in the ordinary course of business.

39. POST BALANCE SHEET EVENT

During the 5th Session of the 10th National People's Congress, which was concluded on 16 March 2007, the PRC Corporate Income Tax Law (“the New Corporate Income Tax Law”) was approved and will become effective on 1 January 2008. The New Corporate Income Tax Law introduces a wide range of changes which include, but are not limited to, the unification of the income tax rate for domestic-invested and foreign-invested enterprises at 25%. Since the detailed implementation and administrative rules and regulations have not yet been announced, the financial impact of the New Corporate Income Tax Law to the Group and the Company cannot be reasonably estimated at this stage.

40. APPROVAL OF THE FINANCIAL STATEMENTS

The financial statements were approved and authorised for issue by the board of directors of the Company on 30 March 2007.