financial review

FINANCIAL RESULTS

HIGHLIGHTS ON FINANCIAL RESULTS

HK$ million	2006	2005	% increase/ (decrease)
Turnover	4,199	3,980	5.5%
Gross profit	410	454	(9.7%)
Other income and gains	444	175	153.7%
Profit for the year	366	253	44.7%
Attributable to:			
— Equity holders of parent	358	225	59.1%
— Minority interests	8	28	(71.4%)

DISCUSSION ON FINANCIAL RESULTS

The Group reported a record turnover of HK$4,199 million during the year, which represents a slightly increase of 5.5% over last year. The increase in turnover is attributable to contribution from our securities investment business and the growth of our manufacturing businesses.

Gross profit dropped by 9.7% from HK$454 million in 2005 to HK$410 million in 2006. The drop in gross profit is mainly due to the reduction in selling price of some product models due to competition and rise in production costs

Other income and gains amounted to HK$444 million in 2006, up 153.7% from 2005. The significant increase in other income and gains was attributable to (i) the realized gain of approximately HK$316 million from the disposal of our interest in Haier Electronics, (ii) the gain and interest income of HK$48 million derived from the securities investment business and (iii) the unrealized revaluation gain on our investment properties portfolio of HK$39 million recorded in the year 2006.

Profit attributable to equity shareholders of the Company amounted to HK$358 million, up 59.1% from previous reporting year, helped mainly by the rise in other income and gains.

Profit shared by minority interest decreased significantly by 71.4% due to the dilution of the minority interests in CCT Tech in May 2006 upon the full conversion of the convertible notes by the Company into shares in CCT Tech.

ANALYSIS BY BUSINESS SEGMENT

	Turnover				
	2006		2005		
HK$ million	Amount	Relative %	Amount	Relative %	% increase/ (decrease)
Telecom and electronic products	3,882	92.5%	3,846	96.6%	0.9%
Baby products	112	2.7%	124	3.1%	(9.7%)
Securities investment	149	3.5%	—	—	N/A
Property investment and development	3	—	2	—	50%
Corporate and others	53	1.3%	8	0.3%	562.5%
Total	4,199	100.0%	3,980	100.0%	

	Operating profit		
HK$ million	2006	2005	% increase/ (decrease)
Telecom and electronic products	109	189	(42.3%)
Baby products	8	6	33.3%
Securities investment	364	100	264.0%
Property investment and development	39	67	(41.8%)
Corporate and others	(112)	(76)	47.4%
Total	408	286	

During the year, telecom and electronic product business continued to be the principal business of the Group accounting for approximately 92.5% (2005: 96.6%) of the Group's total turnover. The remaining turnover was mainly contributed by the baby product business and securities investment business which accounted for approximately 2.7% (2005: 3.1%) and 3.5% (2005: Nil), respectively, of the Group's turnover.

The telecom and electronic product business contributed HK$109 million in operating profit in the year 2006, representing a decrease of approximately 42.3% as compared to that in 2005. The decrease was due to the reduction in selling prices of certain product models due to price competition and substantial increase in operating costs in 2006. The baby product business reported operating profit of HK$8 million in 2006 despite a difficult operating environment due to successful efforts of the management to improve efficiency and control costs. The operating profit of the securities business segment recorded a significant increase from HK$100 million in 2005 to HK$364 million in 2006, representing an increase of 264.0%. The increase was mainly attributable to the realized gain of HK$316 million from disposal of Haier Electronics shares and the gain and interest income totaling HK$48 million from the trading of listed securities and interest from equity-linked deposits. Corporate and others included the results of the e-commerce business and head office income and administrative expenses.

ANALYSIS BY GEOGRAPHICAL SEGMENT

	Turnover (including bank interest income)				
	2006		2005		
HK$ million	**Amount**	**Relative %**	Amount	Relative %	% increase/ (decrease)
US	**2,142**	**51.0%**	2,360	59.3%	(9.2%)
Asia Pacific Region	**1,424**	**33.9%**	1,160	29.1%	22.8%
Europe	**633**	**15.1%**	460	11.6%	37.6%
Total	**4,199**	**100.0%**	3,980	100.0%	

The US remained the major market of the Group accounting for approximately 51.0% (2005: 59.3%) of the total turnover for the year. The Asia Pacific Region and the European markets accounted for approximately 33.9% (2005: 29.1%) and approximately 15.1% (2005: 11.6%) of the Group's total turnover for the year, respectively. The drop in sales in the US market was mainly attributable to the slow down of the US economy and the delay in shipments caused by shortage in labor of the PRC factories. Our success in the Asia Pacific and European markets, on the other hand, were largely attributable to our aggressive marketing strategy of targeting new customer profiles and successful product diversification.

FINANCIAL POSITION

Highlights on Financial Position and Major Balance Sheet Items

HK$ million	**31 December 2006**	31 December 2005	% increase/ (decrease)
NON-CURRENT ASSETS			
Property, plant and equipment	**1,222**	1,253	(2.5%)
Investment properties	**490**	257	90.7%
Long term receivable	**312**	—	N/A
Available-for-sale financial assets	**11**	18	(38.9%)
CURRENT ASSETS			
Financial assets at fair value through profit or loss	**226**	24	841.7%
Available-for-sale financial assets	**—**	551	N/A
Cash and cash equivalents	**865**	528	63.8%
EQUITY AND NON-CURRENT LIABILITIES			
Long term payable	**256**	—	N/A
Derivative financial instrument	**71**	—	N/A
Other non-current liabilities	**299**	296	1.0%
Minority interests	**57**	68	(16.2%)
Equity attributable to shareholders' of the Company	**2,752**	2,642	4.2%

FINANCIAL POSITION *(Continued)*

Discussion on Financial Position and Major Balance Sheet Items

The property, plant and equipment represent fixed assets held by the Group for its own use and stated at cost less accumulated depreciation and impairment losses. The decrease in their net book value in the year 2006 was mainly attributable to the combined effect of (i) additions to fixed assets to cope with the needs of production; (ii) reclassification of a property to investment property; and (iii) depreciation provided for the year 2006.

Investment properties in the amount of HK$490 million (31 December 2005: HK$257 million) represents the fair value of properties and their related land lease payment held by the Group for rental and investment purposes. The increase in the balance of investment properties during 2006 was caused by (i) the reclassification of an office premises previously held for own-use to property held for lease; and (ii) acquisitions of two luxury residential properties held for rental.

Long term receivable represents the initial exchange amount which serves as an effective collateral to secure the obligations of the Company under the Put Agreement entered into between CCT Telecom and Deutsche Bank in respect of the put options granted by the Company to Deutsche Bank in relation to the 13.8 billion shares in CCT Tech under the terms of the Put Agreement. The attributable portion of the long term receivable will be refunded to the Company if the shares in CCT Tech are disposed of by Deutsche Bank and the investors to third parties or otherwise will be used to offset the long term payable upon exercise of the put options.

Decrease in non-current available-for-sale financial assets was due to the disposal of one club membership during the year. A gain on disposal of the non-current available-for-sale financial assets amounted to approximately HK$2 million.

Financial assets at fair value through profit or loss (under current assets) as at 31 December 2006 represent our investment in listed securities and equity-linked deposits. To capture the benefit of the blooming Hong Kong Stock Market, the Group has allocated additional funds in the securities investments business in order to generate gains and income for the future.

The available-for-sale financial assets under current asset as at 31 December 2005 in the amount of HK$551 million represent the fair value of the Group's interest in Haier Electronics shares. Following our disposal of all interests in Haier Electronics shares in January 2006, there were no more available-for-sale financial assets (under current assets) recorded as at 31 December 2006.

Cash and cash equivalents increased by 63.8% from HK$528 million as at 31 December 2005 to HK$865 million as at 31 December 2006, mainly due to the receipts of the sales proceeds of approximately HK$551 million from the disposal of Haier Electronics shares and funds from operations minus the funds for capital expenditure for fixed assets, investment properties and funds utilized for the securities investment business.

Long term payable represents the liability of the Company in respect of the repurchase obligations of the CCT Tech Sale Shares under the Put Agreement. If Deutsche Bank or any of the three investors dispose of all or part of the CCT Tech Sale Shares to third parties, the related put options will be recognized in the consolidated income statement and the related long term payable will be included in the calculation of the gain or loss on disposal of the relevant CCT Tech Sale Shares.

FINANCIAL POSITION *(Continued)*

Discussion on Financial Position and Major Balance Sheet Items *(Continued)*

Derivative financial instrument represents the value of put options under the Put Agreement. The derivative financial instrument was initially recognized at fair value at HK$50 million on the date on which the put options were granted and was subsequently re-measured at fair value at the balance sheet date. The fair value of the derivative financial instrument as at 31 December 2006 amounted to HK$71 million. The loss on change in fair value on derivative financial instrument for the year ended 31 December 2006 of HK$21 million was taken directly to the income statement. The put options if not exercised or unwound will expire on 9 May 2008. The long term payable and the derivative financial instrument in relation to the Put Agreement will offset against the long term receivable upon the exercise of the put options and the consequent buy back of CCT Tech Sale Shares from Deutsche Bank. If the CCT Tech Shares are sold by Deutsche Bank and/or the three investors to third parties, the related put options will be unwound and the Company will not need to pay to Deutsche Bank.

Decrease in minority interests was mainly due to the dilution of minority interests arising from the full conversion of convertible notes due to Company by CCT Tech during the year.

The increase in shareholders' funds of approximately 4.2% was mainly due to the carried forward of the retained profits for the year and issue of the new shares from the conversion of convertible bonds during the year 2006.

CAPITAL STRUCTURE AND GEARING RATIO

	31 December 2006		31 December 2005	
HK$ million	Amount	Relative %	Amount	Relative %
Bank loans	450	13.8%	364	11.8%
Convertible notes	49	1.5%	77	2.5%
Finance lease payables	4	0.2%	10	0.3%
Total borrowings	503	15.5%	451	14.6%
Equity	2,752	84.5%	2,642	85.4%
Total capital employed	3,255	100.0%	3,093	100.0%

The Group's gearing ratio was approximately 15.5% as at 31 December 2006 as compared with that of 14.6% as at 31 December 2005. The increase in gearing ratio was mainly due to the aggregate effect of (i) the borrowing of new mortgage loans for the financing of the newly acquired luxury properties; (ii) issue of the 2009 Convertible Bonds; (iii) conversion of part of the 2010 Convertible Bonds; and (iv) the net repayment of the bank borrowings. After taking into account the cash on hand, the Group did not have any net borrowings but was in a net cash position.

Outstanding bank borrowings amounted to HK$450 million at 31 December 2006 (31 December 2005: HK$364 million). Approximately 45.1% of these bank borrowings was arranged on a short-term basis for the ordinary business of the Group and was repayable within one year. The remaining 54.9% of the bank borrowings was of long-term nature, principally comprising mortgage loans on properties held by the Group.

CAPITAL STRUCTURE AND GEARING RATIO *(Continued)*

During the year, the 2009 Convertible Bonds with a nominal value of HK$30 million were issued by the Company to a company controlled by Mr. Mak as part of the consideration to acquire a property by the Company from Mr. Mak in April 2006. In addition, part of the 2010 Convertible Bonds with a nominal value of HK$75 million was converted into approximately 124 million shares of the Company during the year.

Acquisition of certain of the Group's assets were financed by way of finance leases and the total outstanding finance lease payables for the Group as at 31 December 2006 amounted to approximately HK$4 million (31 December 2005: HK$10 million).

As at 31 December 2006, the maturity profile of the bank and other borrowings and convertible notes of the Group falling due within one year, in the second to the fifth year and in the sixth to the tenth year amounted to HK$207 million, HK$208 million and HK$88 million, respectively (31 December 2005: HK$158 million, HK$240 million and HK$53 million, respectively). There was no material effect of seasonality on the Group's borrowing requirements.

LIQUIDITY AND FINANCIAL RESOURCES

HK$ million	31 December 2006	31 December 2005
Current assets	2,293	2,357
Current liabilities	1,295	1,312
Current ratio	177%	180%

Current ratio as at 31 December 2006 was 177% (31 December 2005: 180%). The strong liquid position was attributable to strong cash flow from the operations and the effective financial management of the Group.

As at 31 December 2006, the Group maintained a total cash balance of HK$953 million (31 December 2005: HK$599 million), of which HK$88 million (31 December 2005: HK$71 million) was pledged for general banking facilities.

Almost all of the Group's cash was placed on deposits with licensed banks in Hong Kong. The strong cash balance plus the cash generated from the Group's operations and funds available from the bank facilities are expected to be sufficient to cover all cash requirements, including working capital and capital expenditure needs.

CAPITAL EXPENDITURE AND COMMITMENTS

During the year, the Group incurred capital expenditure amounted to approximately HK$369 million, which was mainly related to the core manufacturing businesses of the Group.

The Group had authorised and contracted capital commitments of approximately HK$69 million (31 December 2005: HK$7 million) as at 31 December 2006, which was mainly related to capital expenditure for the expansion of the manufacturing business of the Group. The outstanding capital commitments will be financed partly by internal resources and partly by bank borrowings.

TREASURY MANAGEMENT

The Group employs a conservative approach to cash management and risk control. To achieve better risk control and efficient fund management, the Group's treasury activities are centralised.

During the year, the Group's receipts were mainly denominated in US dollars, with some in Hong Kong dollars and the Euro. Payments were mainly made in Hong Kong dollars, US dollars and Renminbi and some made in Euros. Cash was generally placed in short-term deposits and medium-term deposits denominated in Hong Kong dollars and US dollars and some in European currencies. As at 31 December 2006, the Group's borrowings were mainly denominated in Hong Kong dollars and US dollars. As at 31 December 2006, other than the convertible bonds in an aggregate principal amount of approximately HK$59 million which is interest-free, the Group's borrowings were principally made on a floating rate basis.

The objective of the Group's treasury policies is to minimise risks and exposures due to the fluctuations in foreign currency exchange rates and interest rates. The Group does not have any significant interest rate risk, as both the borrowings of the Group and the interest rates currently remain at low levels. In terms of foreign exchange exposures, the Group is principally exposed to two major currencies, namely the US dollar in terms of receipts and the Renminbi in terms of the production costs (including mainly wages and overhead) in China. For US dollar exposure, since the Hong Kong dollar remains pegged to the US dollar, the exchange fluctuation is not expected to be significant. Above all, as most of the Group's purchases are also made in US dollars, which are to be paid out of our sales receipts in US dollars, the management considers that the net foreign exchange exposure risk for the US dollar is not material.

For Renminbi exposure, the Group entered into forward exchange contracts with banks in China to cover a significant part of our Renminbi expenses for the period up to mid 2006. Our exposure to any Renminbi fluctuation has, therefore, been partly hedged against such risks for the period up to mid 2006 although the appreciation of the Renminbi has increased forward rates which has made hedging more costly. Our future production costs will no doubt be increased by the Renminbi appreciation. Any further appreciation of Renminbi in the future will be of concern to all businesses with manufacturing facilities in China, and to their respective customers. We have invested some of our surplus funds on investments that we believe will benefit from appreciation of the Renminbi. We hope that the returns and gains that we are hoping to derive from these investments will hedge partly against the potential appreciation of the Renminbi.

ACQUISITION AND DISPOSAL OF MATERIAL SUBSIDIARIES AND ASSOCIATES

During the year 2006, we sold 13.8 billion ordinary shares in CCT Tech to Deutsche Bank and three other independent investors for a total consideration of approximately HK$303.6 million. Put options have been granted to Deutsche Bank which give Deutsche Bank the right to sell back the shares to us on the expiration date of the put options or upon occurrence of certain events. The proceeds for the sale of CCT Tech shares were paid to Deutsche Bank to effectively secure the put options. After the disposal, the Group's shareholding interests in CCT Tech are approximately 74.63%. Deutsche Bank and the three other independent investors together held in total approximately 21.44% of the total issued share capital of CCT Tech.

In April 2006, the Group subscribed a total of 550,000,000 shares in Tradeeasy for a total consideration of HK$22 million. Upon completion of the subscription, the Group's shareholding in Tradeeasy has increased from 22.18% to 66.26%. Tradeeasy has become a non-wholly owned subsidiary of the Company since then. Tradeeasy is engaged in provision of e-commerce services.

SIGNIFICANT INVESTMENT

During the year 2006, the Group has further increased its property investment by acquiring two luxury residential properties for a total consideration of HK$177 million. Besides, the Group has invested in aggregate HK$178 million in shares listed on the Stock Exchange. Save as disclosed, there was no significant investment unrelated to the core manufacturing businesses of the Group.

PLEDGE OF ASSETS

As at 31 December 2006, certain of the Group's assets with a net book value of HK$1,004 million (31 December 2005: HK$821 million) and time deposits of HK$88 million (31 December 2005: HK$71 million) were pledged to secure the general banking facilities granted to the Group.

CONTINGENT LIABILITIES

As at 31 December 2006, the banking facilities granted to the subsidiaries subject to the corporate guarantees given to the banks by the Company were utilized to the extent of approximately HK$247 million (31 December 2005: HK$154 million).

As at 31 December 2006, the Group had a contingent liability in respect of possible future long service payments to employees under the Hong Kong Employment Ordinance, with a maximum possible amount of HK$1 million (31 December 2005: HK$1 million). Save as aforesaid, the Group did not have any other significant contingent liabilities as at 31 December 2006.

EMPLOYEES AND REMUNERATION POLICY

The total number of employees of the Group as at 31 December 2006 was 17,820 (31 December 2005: 17,697). Remuneration packages are normally reviewed on an annual basis. Apart from salary payments, there are other staff benefits including provident fund, medical insurance and performance related bonus. Share options may also be granted to eligible employees and persons of the Group. At 31 December 2006, there were no outstanding share options issued by the Company.