1. GENERAL

The Company was incorporated in the Cayman Islands as an exempted company with limited liability on 8 February 2000 under the Companies Law of the Cayman Islands. The Company's shares have been listed on the Main Board of The Stock Exchange of Hong Kong Limited (the "Stock Exchange") since 3 February 2005. The Company's parent company is Foxconn (Far East) Limited (incorporated in the Cayman Islands) and its ultimate holding company is Hon Hai Precision Industry Company Limited ("Hon Hai") (incorporated in Taiwan and its shares are listed on Taiwan Stock Exchange). The addresses of the registered office and principal place of business of the Company are disclosed in the section headed "Corporate Information" to the annual report.

The Company and its subsidiaries (hereinafter collectively referred to as the "Group") are principally engaged in the manufacture of complete mobile phone handset systems and modules for mobile phone handsets.

The consolidated financial statements are presented in United States Dollars ("US$") which is also the functional currency of the Company.

2. ADOPTION OF NEW AND REVISED INTERNATIONAL FINANCIAL REPORTING STANDARDS

In the current year, the Group has applied, for the first time, a number of new standards, amendments and interpretations (hereinafter collectively referred to as "new IFRSs") issued by the International Accounting Standards Board ("IASB") and the International Financial Reporting Interpretations Committee ("IFRIC"), which are either effective for accounting periods beginning on or after 1 December 2005 or 1 January 2006. The adoption of the new IFRSs had no material effect on how the results and financial positions for the current or prior accounting periods have been prepared and presented. Accordingly, no prior period adjustment has been required.

The Group has not early applied the following new IFRSs that have been issued but are not yet effective.

IAS 1 (Amendment)	Capital Disclosures[1]
IFRS 7	Financial Instruments: Disclosures[1]
IFRS 8	Operating Segments[2]
IFRIC 7	Applying the Restatement Approach under IAS 29 *Financial Reporting in Hyperinflationary Economies*[3]
IFRIC 8	Scope of IFRS 2[4]
IFRIC 9	Reassessment of Embedded Derivatives[5]
IFRIC 10	Interim Financial Reporting and Impairment[6]
IFRIC 11	IFRS 2 – Group and Treasury Share Transactions[7]
IFRIC 12	Service Concession Arrangements[8]

[1] Effective for annual periods beginning on or after 1 January 2007
[2] Effective for annual periods beginning on or after 1 January 2009
[3] Effective for annual periods beginning on or after 1 March 2006
[4] Effective for annual periods beginning on or after 1 May 2006
[5] Effective for annual periods beginning on or after 1 June 2006
[6] Effective for annual periods beginning on or after 1 November 2006
[7] Effective for annual periods beginning on or after 1 March 2007
[8] Effective for annual periods beginning on or after 1 January 2008

The directors of the Company anticipate that the application of these new IFRSs will have no material financial impact on the consolidated financial statements of the Group, except for IFRS 8. They have commenced considering the potential impact of IFRS 8 but is not yet in a position to determine whether IFRS 8 would have a significant impact on how its results of operations and financial position are prepared and presented.

3. SIGNIFICANT ACCOUNTING POLICIES

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

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

Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and entities (including special purpose entities) controlled by the Company (its subsidiaries). Control is achieved where the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities.

The results of subsidiaries acquired or disposed of during the year are included in the consolidated income statement from the effective date of acquisition or up to the effective date of disposal, as appropriate.

Where necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies into line with those used by other members of the Group.

All intra-group transactions, balances, income and expenses are eliminated on consolidation.

Minority interests in the net assets (excluding goodwill) of consolidated subsidiaries are presented separately from the Group's equity therein. Minority interests in the net assets consist of the amount of those interests at the date of the original business combination and the minority's share of changes in equity since the date of the combination. Losses applicable to the minority in excess of the minority's interest in the subsidiary's equity are allocated against the interests of the Group except to the extent that the minority has a binding obligation and is able to make an additional investment to cover the losses.

Business combinations

The acquisition of subsidiaries is accounted for using the purchase method. The cost of the acquisition is measured at the aggregate of the fair values, at the date of exchange, of assets given, liabilities incurred or assumed, and equity instruments issued by the Group in exchange for control of the acquiree, plus any costs directly attributable to the business combination. The acquiree's identifiable assets, liabilities and contingent liabilities that meet the conditions for recognition under IFRS 3 "Business Combinations" are recognised at their fair values at the acquisition date, except for non-current assets (or disposal groups) that are classified as held for sale in accordance with IFRS 5 "Non-Current Assets Held for Sale and Discontinued Operations", which are recognised and measured at fair value less costs to sell.

3. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

Business combinations *(Continued)*

Goodwill arising on acquisition is recognised as an asset and initially measured at cost, being the excess of the cost of the business combination over the Group's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities recognised. If, after reassessment, the Group's interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities exceeds the cost of the business combination, the excess is recognised immediately in profit or loss.

The interest of minority shareholders in the acquiree is initially measured at the minority's proportion of the net fair value of the assets, liabilities and contingent liabilities recognised.

Goodwill

Goodwill arising on an acquisition of a subsidiary represents the excess of the cost of acquisition over the Group's interest in the fair value of the identifiable assets, liabilities and contingent liabilities of the relevant subsidiary at the date of acquisition. Such goodwill is carried at cost less any accumulated impairment losses.

Capitalised goodwill arising on an acquisition of a subsidiary is presented separately in the consolidated balance sheet.

For the purposes of impairment testing, goodwill arising from an acquisition is allocated to each of the relevant cash-generating units, or groups of cash-generating units, that are expected to benefit from the synergies of the acquisition. A cash-generating unit to which goodwill has been allocated is tested for impairment annually, and whenever there is an indication that the unit may be impaired. For goodwill arising on an acquisition in a financial year, the cash-generating unit to which goodwill has been allocated is tested for impairment before the end of that financial year. When the recoverable amount of the cash-generating unit is less than the carrying amount of the unit, the impairment loss is allocated to reduce the carrying amount of any goodwill allocated to the unit first, and then to the other assets of the unit pro rata on the basis of the carrying amount of each asset in the unit. Any impairment loss for goodwill is recognised directly in the consolidated income statement. An impairment loss for goodwill is not reversed in subsequent periods.

On subsequent disposal of a subsidiary, the attributable amount of goodwill capitalised is included in the determination of the profit or loss on disposal.

Revenue recognition

Revenue is measured at the fair value of the consideration received or receivable and represents amounts receivable for goods and services provided in the normal course of business, net of discounts and sales related taxes.

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

3. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

Revenue recognition *(Continued)*

Service income is recognised when services are provided.

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

Property, plant and equipment

Property, plant and equipment, other than construction in progress, are stated at cost less accumulated depreciation and any identified impairment loss at the balance sheet date.

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

Construction in progress represents property, plant and equipment in the course of construction for production or for its own use purposes. Construction in progress is carried at cost less any recognised impairment loss. Construction in progress is classified to the appropriate category of property, plant and equipment when completed and ready for intended use. Depreciation of these assets, on the same basis as other assets, commences when the assets are ready for their intended use.

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

Leasing

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

The Group as lessee

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

3. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

Foreign currencies

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

Exchange differences arising on the settlement of monetary items, and on the translation of monetary items, are recognised in profit or loss in the period in which they arise, except for exchange differences arising on a monetary item that forms part of the Company's net investment in a foreign operation, in which case, such exchange differences are recognised in equity in the consolidated financial statements.

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

Goodwill and fair value adjustments arising on an acquisition of a foreign operation on or after 1 January 2005 are treated as assets and liabilities of the foreign operation and translated at the rate of exchange prevailing at the balance sheet date. Exchange differences arising are recognised in the translation reserve.

Borrowing costs

All borrowing costs are recognised in the period incurred.

Retirement benefit costs

Payments to defined contribution retirement benefit plans are charged as an expense when employees have rendered service entitling them to the contributions.

3. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

Retirement benefit costs *(Continued)*

For defined benefit retirement benefit plans, the cost of providing benefits is determined using the projected unit credit method, with actuarial valuations being carried out at each balance sheet date. Actuarial gains and losses which exceed 10% of the greater of the present value of the Group's pension obligations and the fair value of plan assets are amortised over the expected average remaining working lives of the participating employees. Past service cost is recognised immediately to the extent that the benefits are already vested, and otherwise is amortised on a straight-line basis over the average period until the amended benefits become vested.

The amount recognised in the consolidated balance sheet represents the present value of the defined benefit obligation as adjusted for unrecognised actuarial gains and losses and unrecognised past service cost, and as reduced by the fair value of plan assets. Any asset resulting from this calculation is limited to unrecognised actuarial losses and past service cost, plus the present value of available refunds and reductions in future contributions to the plan.

Taxation

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

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

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

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

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

3. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

Taxation *(Continued)*

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

Research and development expenditure

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

An internally-generated intangible asset arising from development expenditure is recognised only if it is anticipated that the development costs incurred on a clearly-defined project will be recovered through future commercial activity. The resultant asset is amortised on a straight-line basis over its useful life, and carried at cost less subsequent accumulated amortisation and any accumulated impairment losses.

The amount initially recognised for internally-generated intangible asset is the sum of the expenditure incurred from the date when the intangible asset first meets the recognition criteria. Where no internally-generated intangible asset can be recognised, development expenditure is charged to profit or loss in the period in which it is incurred.

Subsequent to initial recognition, internally-generated intangible asset is reported at cost less accumulated amortisation and accumulated impairment losses.

Impairment losses (other than goodwill and available-for-sale investments)

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

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

Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is calculated using the first-in, first-out basis.

3. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

Financial instruments

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

Financial assets

The Group's financial assets are classified into one of the three categories, including financial assets at fair value through profit or loss, loans and receivables and available-for-sale financial assets. All regular way purchases or sales of financial assets are recognised and derecognised on a trade date basis. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the time frame established by regulation or convention in the marketplace. The accounting policies adopted in respect of each category of financial assets are set out below.

Financial assets at fair value through profit or loss

The Group's financial assets at fair value through profit or loss are financial assets held for trading.

At each balance sheet date subsequent to initial recognition, financial assets at fair value through profit or loss are measured at fair value, with changes in fair value recognised directly in profit or loss in the period in which they arise.

Loans and receivables

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

3. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

Financial instruments *(Continued)*

Financial assets (Continued)

Available-for-sale financial assets

Available-for-sale equity investments that do not have a quoted market price in an active market and whose fair value cannot be reliably determined are measured at cost less any identified impairment losses at each balance sheet date subsequent to initial recognition. An impairment loss is recognised in profit or loss when there is objective evidence that the asset is impaired. The amount of the impairment loss is measured as the difference between the carrying amount of the asset and the present value of the estimated future cash flows discounted at the current market rate of return for a similar financial asset. Such impairment losses will not reverse in subsequent periods.

Financial liabilities and equity

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

An equity instrument is any contract that evidences a residual interest in the assets of the Group after deducting all of its liabilities. The accounting policies adopted in respect of financial liabilities and equity instruments are set out below.

Financial liabilities

Financial liabilities including bank loans, trade and other payables are subsequently measured at amortised cost, using the effective interest method.

Equity instruments

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

Derivative financial instruments

Derivatives are initially recognised at fair value at the date a derivative contract is entered into and are subsequently remeasured to their fair value at each balance sheet date. The resulting gain or loss is recognised in profit or loss immediately. Derivative financial instruments that are not designated as effective hedging instruments are classified as held for trading.

Derecognition

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

3. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

Financial instruments *(Continued)*

Derecognition (Continued)

Financial liabilities are derecognised when the obligation specified in the relevant contract is discharged, cancelled or expired. The difference between the carrying amount of the financial liability derecognised and the consideration paid and payable is recognised in profit or loss.

Provisions

Provisions are recognised when the Group has a present obligation as a result of a past event, and it is probable that the Group will be required to settle that obligation. Provisions are measured at the directors' best estimate of the expenditure required to settle the obligation at the balance sheet date, and are discounted to present value where the effect is material.

Share-based payment transactions

Equity-settled share-based payment transactions

The fair value of services received determined by reference to the fair value of share options or ordinary shares granted at the grant date is expensed on a straight-line basis over the vesting period or recognised as an expense in full at the grant date when the share options or ordinary shares granted vest immediately, with a corresponding increase in equity (share compensation reserve).

At each balance sheet date, the Group revises its estimates of the number of options or ordinary shares that are expected to ultimately vest. The impact of the revision of the estimates, if any, is recognised in profit or loss with a corresponding adjustment to share compensation reserve.

At the time when the share options are exercised, the amount previously recognised in share compensation reserve will be transferred to share premium. When the share options are forfeited after the vesting date or are still not exercised at the expiry date, the amount previously recognised in share compensation reserve will be transferred to retained profits.

Cash-settled share-based payment transactions

For cash-settled share-based payments, the Group measures the goods or services acquired and the liability incurred at the fair value of the liability. At each balance sheet date, the liability is remeasured at its fair value until the liability is settled, with any changes in fair value recognised in profit or loss.

Government grants

Government grants are recognised as income over the periods necessary to match them with the related costs. Grants related to depreciable assets are presented as deferred income and are released to income over the useful lives of the assets. Grants related to expense items are recognised in the same period as those expenses are charged in the consolidated income statements and are reported separately as other income.

4. KEY SOURCES OF ESTIMATION UNCERTAINTY

The management had made the following estimates and assumptions in the process of applying the Group's accounting policies, which are described in note 3, that have a significant risk of causing a material adjustment to the carrying amounts of the assets and liabilities as discussed below.

Impairment of goodwill

Determining whether goodwill is impaired requires an estimation of the value in use of the cash-generating units to which goodwill has been allocated. The value in use calculation requires the Group to estimate the future cash flows expected to arise from the cash-generating unit and a suitable discount rate in order to calculate the present value. Where the actual future cash flows are less than expected, a material impairment loss may arise. In May 2005, the Company acquired Chi Mei Communications Systems Inc. ("CMCS"), a company which specialises in ODM business, and the carrying amount of goodwill at the balance sheet date was US$63,075,000. Details of the impairment testing are provided in note 18.

Provision

Provision has been made for value-added costs to repair or replace defective goods, such as labour (whether incurred internal or external) and material costs, and also costs that may not be recoverable from suppliers for the rework, either in accordance with contractual terms or the Group's policy. The provision requires the management to estimate the extent of repairs and replacements with reference to past experience, technology needs and industry averages for defective products. The estimation may be adversely affected by many factors, including additional variations to the plans requested by the customers or because of technical needs, and unforeseen problems and circumstances. Any of these factors may affect the extent of repair or replacement required and therefore ultimate repair and replacement costs to be incurred in the future period.

5. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

The Group's financial instruments include investments held for trading, bank loans, trade and other receivables, trade and other payables, bank and bank deposits. Details of these financial instruments are disclosed in the respective notes. The risks associated with these financial instruments and the policies applied by the Group to mitigate these risks are set out below. Management monitors these exposures to ensure appropriate measures are implemented in a timely and effective manner.

5. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES *(Continued)*

Credit risk

The Group's maximum exposure to credit risk in the event of the counterparties' failure to perform their obligations as at 31 December 2006 in relation to each class of recognised financial assets is the carrying amount of those assets as stated in the consolidated balance sheet. A major portion of the Group's trade debts are receivable from industry leaders or multinational customers with solid financial background. Meanwhile, in order to minimise the credit risk, the management of the Group has delegated a team responsible for determination of credit limits and monitoring procedures to ensure that follow-up action is taken to recover overdue debts. In addition, the Group reviews the recoverable amount of each individual trade debt at each balance sheet date to ensure that adequate impairment losses are made for irrecoverable amounts. In this regard, the directors of the Company consider that the Group's credit risk is significantly reduced.

Credit risk in mobile phone handset industry is concentrated on a few global handset manufacturers. However, with the strong financial background and good creditability of the global handset manufacturers, the management considers there is no significant credit risk. In determining whether there is objective evidence of impairment loss, the Group takes into consideration of the estimation of the future cash flows.

The credit risk on liquid funds is limited because the counterparties are banks with higher credit-ratings assigned by international credit-rating agencies and long-term partners of the Group.

Currency risk

Certain subsidiaries of the Company transact in foreign currencies, which expose the Group to foreign currency risk. In order to mitigate the foreign currency risk, the Group manages its foreign currency exposure by non-financial techniques such as managing the transaction currency, and leading and lagging payments and receivable management. In addition, the Group sometimes obtains bank loans in various foreign currencies and enters into short-term foreign currency forward contracts (less than three months) for hedging purpose. Currently the Group does not designate its forward foreign currency contracts as a hedging instrument for the purpose of hedging the currency risk of its foreign operations. However, the management monitors foreign exchange exposure and will consider hedging significant foreign currency exposure should the need arises.

Interest rate risk

In the past, the Group had applied interest rate swaps to manage its exposure to interest rate fluctuations on its long-term bank borrowings. Currently, a majority of the Group's borrowings are raised on short term basis and therefore the related fair value interest rate risk is considered limited. No additional derivatives were used during the current year for hedging short-term interest rate exposure.

5. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES *(Continued)*

Fair value

The fair value of financial assets and financial liabilities are determined as follows:

(i) the fair value of financial assets and financial liabilities with standard terms and conditions and traded on active liquid markets are determined with reference to quoted market bid prices and ask prices respectively; and

(ii) the fair value of other financial assets and financial liabilities (excluding derivative instruments) are determined in accordance with generally accepted pricing models based on discounted cash flow analysis or using prices from observable current market transactions.

6. BUSINESS AND GEOGRAPHICAL SEGMENTS

The directors consider that the Group is in a single business segment as the turnover and profit are derived entirely from the end-to-end handset manufacturing service to the customers.

Segment information regarding the Group's sales by geographical market, irrespective of the origin of the goods/services, and other analysis by geographical area is presented below.

INCOME STATEMENT

	Year ended 31 December 2006			
	Asia	Europe	America	Consolidated
	US$'000	US$'000	US$'000	US$'000
TURNOVER				
External sales	6,435,691	1,464,947	2,480,598	10,381,236
RESULTS	614,980	114,193	239,502	968,675
Unallocated income				42,838
Unallocated expenses				(212,763)
Unallocated interest expense on bank borrowings				(13,294)
Profit before tax				785,456
Income tax expense				(67,610)
Profit for the year				717,846

6. BUSINESS AND GEOGRAPHICAL SEGMENTS *(Continued)*

INCOME STATEMENT *(Continued)*

	Year ended 31 December 2005			
	Asia	Europe	America	Consolidated
	US$'000	US$'000	US$'000	US$'000
TURNOVER				
External sales	3,276,160	1,012,050	2,076,287	6,364,497
RESULTS	285,782	99,261	182,284	567,327
Unallocated income				29,794
Unallocated expenses				(163,962)
Unallocated interest expense on bank borrowings				(13,901)
Profit before tax				419,258
Income tax expense				(36,324)
Profit for the year				382,934

Segment information regarding the Group's assets and liabilities by locations of customers are as follows:

BALANCE SHEET

	As at 31 December 2006			
	Asia	**Europe**	**America**	**Consolidated**
	US$'000	**US$'000**	**US$'000**	**US$'000**
ASSETS				
Segment assets	**1,014,917**	**366,396**	**669,250**	**2,050,563**
Unallocated assets				**2,451,845**
Consolidated total assets				**4,502,408**
LIABILITIES				
Segment liabilities	**–**	**68,545**	**181,400**	**249,945**
Unallocated liabilities				**1,871,461**
Consolidated total liabilities				**2,121,406**

6. BUSINESS AND GEOGRAPHICAL SEGMENTS *(Continued)*

BALANCE SHEET *(Continued)*

	As at 31 December 2005			
	Asia	Europe	America	Consolidated
	US$'000	US$'000	US$'000	US$'000
ASSETS				
Segment assets	847,318	413,733	587,645	1,848,696
Unallocated assets				1,309,851
Consolidated total assets				3,158,547
LIABILITIES				
Segment liabilities	–	80,143	140,972	221,115
Unallocated liabilities				1,410,415
Consolidated total liabilities				1,631,530

OTHER INFORMATION

	Year ended 31 December 2006				
	Asia	**Europe**	**America**	**Corporate**	**Consolidated**
	US$'000	**US$'000**	**US$'000**	**US$'000**	**US$'000**
Capital additions	**–**	**22,589**	**27,315**	**444,514**	**494,418**
Depreciation and amortisation	**–**	**11,114**	**20,696**	**103,157**	**134,967**
Impairment losses on property, plant and equipment	**–**	**3,892**	**–**	**–**	**3,892**
(Gain) loss on disposal of property, plant and equipment	**–**	**(612)**	**880**	**469**	**737**
(Write back) allowances for doubtful debts	**(1,103)**	**(484)**	**929**	**–**	**(658)**
Write-down of inventories	**–**	**1,887**	**10,020**	**16,200**	**28,107**

6. BUSINESS AND GEOGRAPHICAL SEGMENTS *(Continued)*

OTHER INFORMATION *(Continued)*

	Year ended 31 December 2005				
	Asia	Europe	America	Corporate	Consolidated
	US$'000	US$'000	US$'000	US$'000	US$'000
Capital additions	–	66,185	38,458	236,842	341,485
Depreciation and amortisation	–	15,898	12,941	43,727	72,566
Impairment losses on property, plant and equipment	–	7,966	–	–	7,966
Loss on disposal of property, plant and equipment	–	–	–	244	244
Allowances (write back) for doubtful debts	688	230	(66)	–	852
Write-down of inventories	–	3,447	–	16,881	20,328

The following is an analysis of the carrying amount of segment assets, and additions to property, plant and equipment, analysed by the geographical area in which the assets are located:

	Carrying amount of segment assets as at 31 December		**Additions to property, plant and equipment for the year ended 31 December**	
	2006	2005	**2006**	2005
	US$'000	US$'000	**US$'000**	US$'000
Asia	**3,142,498**	2,002,108	**444,514**	236,842
Europe	**384,937**	435,307	**22,589**	66,185
America	**959,167**	711,038	**27,315**	38,458
	4,486,602	3,148,453	**494,418**	341,485

7. OTHER INCOME

An analysis of the Group's other income is as follows:

	2006	2005
	US$'000	US$'000
Interest income from bank	**10,585**	8,889
Service and subcontracting income	**21,147**	8,691
Sales of materials, scraps and moldings	**14,906**	17,618
Net foreign exchange gain	**8,975**	–
Gain on disposal of certain assets and liabilities of a subsidiary *(Note)*	**1,209**	–
Others	**7,163**	3,287
	63,985	38,485

Note: On 31 July 2006, Dynacept Corporation ("Dynacept"), a wholly-owned subsidiary of the Company, entered into two agreements with MRP Real Estate Holdings, LLC and MRP Brewster, LLC (the "Purchasers") pursuant to which Dynacept disposed certain of its assets and liabilities at a cash consideration of US$8,580,000. The Purchasers are beneficially owned by a director of Dynacept and a relative of that director. The Group recorded a gain, net of costs, of approximately US$1,209,000 as a result of the disposal.

8. RESTRUCTURING COSTS

	2006	2005
	US$'000	US$'000
Impairment losses on property, plant and equipment	**3,892**	6,230
Redundancy costs	**5,767**	2,973
	9,659	9,203

The amount represents those costs incurred and provision made in connection with the Group's restructuring and relocating its European operations during the year.

9. PROFIT BEFORE TAX

	2006 US$'000	2005 US$'000
Profit before tax has been arrived at after charging (crediting):		
(Write back) allowance for doubtful debts	**(658)**	852
Write down of inventories	**28,107**	20,328
Amortisation of prepaid lease payments (included in general and administrative expense)	**337**	132
Auditor's remuneration	**830**	550
Cost of inventories recognised as expense	**9,319,422**	5,741,546
Provision for warranty	**61,323**	22,068
Depreciation of property, plant and equipment	**134,630**	72,434
Impairment losses on property, plant and equipment	**3,892**	7,966
Net foreign exchange (gain) loss	**(8,975)**	5,826
Increase in fair value of investments held for trading	**(310)**	(129)
Staff costs		
Directors' remuneration	**1,457**	1,457
Retirement benefit scheme contributions (excluding directors)	**18,258**	17,710
Equity-settled share-based payments	**53,883**	20,076
Cash-settled share-based payments	**3,429**	–
Other staff costs	**300,016**	259,007
	377,043	298,250
Loss on disposal of property, plant and equipment	**737**	244
Gain on disposal of certain assets and liabilities of a subsidiary	**(1,209)**	–

10. DIRECTORS' REMUNERATION

The emoluments paid or payable to each of the nine (2005: nine) directors were as follows:

		Other emoluments			
	Fees US$'000	**Basic salaries and allowances US$'000**	**Performance related incentive payments US$'000**	**Retirement benefit scheme contributions US$'000**	**Total 2006 US$'000**
Chin Wai Leung, Samuel	**–**	**1,200**	**–**	**–**	**1,200**
Dai Feng Shuh	**–**	**180**	**–**	**–**	**180**
Chang Ban Ja, Jimmy	**–**	**–**	**–**	**–**	**–**
Gou Hsiao Ling	**–**	**–**	**–**	**–**	**–**
Lee Jin Ming	**–**	**–**	**–**	**–**	**–**
Lu Fang Ming	**–**	**–**	**–**	**–**	**–**
Lau Siu Ki	**23**	**8**	**–**	**–**	**31**
Edward Fredrick Pensel	**23**	**–**	**–**	**–**	**23**
Mao Yu Lang	**23**	**–**	**–**	**–**	**23**
	69	**1,388**	**–**	**–**	**1,457**

		Other emoluments			
	Fees US$'000	Basic salaries and allowances US$'000	Performance related incentive payments US$'000	Retirement benefit scheme contributions US$'000	Total 2005 US$'000
Chin Wai Leung, Samuel	–	1,200	–	–	1,200
Dai Feng Shuh	–	180	–	–	180
Chang Ban Ja, Jimmy	–	–	–	–	–
Gou Hsiao Ling	–	–	–	–	–
Lee Jin Ming	–	–	–	–	–
Lu Fang Ming	–	–	–	–	–
Lau Siu Ki	23	8	–	–	31
Edward Fredrick Pensel	23	–	–	–	23
Mao Yu Lang	23	–	–	–	23
	69	1,388	–	–	1,457

Note: The performance related incentive payment is determined by reference to the individual performance of the directors and approved by the Remuneration Committee.

11. EMPLOYEES' EMOLUMENTS

The aggregate emoluments of the five highest paid individuals included one (2005: one) executive director of the Company, whose emoluments are included in note 10 above. The emoluments of the remaining four (2005: four) individuals were as follows:

	2006	2005
	US$'000	US$'000
Salaries and other benefits	**352**	547
Retirement benefits scheme contributions	**–**	–
Performance-related incentive payments	**4,561**	2,152
	4,913	2,699

Their emoluments were within the following bands:

	Number of employees	
	2006	2005
HK$4,500,001 to HK$5,000,000	**–**	1
HK$5,000,001 to HK$5,500,000	**–**	2
HK$6,000,001 to HK$6,500,000	**–**	1
HK$8,000,001 to HK$8,500,000	**1**	–
HK$9,000,001 to HK$9,500,000	**2**	–
HK$11,500,001 to HK$12,000,000	**1**	–
	4	4

12. INCOME TAX EXPENSE

	2006 US$'000	2005 US$'000
Current tax:		
People's Republic of China ("PRC")	**72,867**	38,429
Other jurisdictions	**2,655**	1,963
	75,522	40,392
Overprovision in prior years:		
PRC	**(90)**	–
Other jurisdictions	**(1,208)**	(186)
	(1,298)	(186)
Deferred tax: *(note 19)*:		
Current year	**(6,614)**	(3,992)
Attributable to a decrease in tax rate	**–**	110
	(6,614)	(3,882)
	67,610	36,324

Tax charge mainly consists of income tax in the PRC attributable to the assessable profits of the Company's subsidiaries established in the PRC. The tax charge is calculated at the applicable rates prevailing in the PRC's Economic and Technological Development Zones ranging from 15% to 16.5%. Taxation for other jurisdictions is calculated at the rates prevailing in the respective jurisdictions.

The Company's subsidiaries operating in the PRC are eligible for certain tax holiday and concession. The tax holiday and concession normally are in the form of two years tax exemption from the first profitable year, followed by a 50% reduction of the applicable tax rate in the following three years.

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12. INCOME TAX EXPENSE *(Continued)*

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

	2006 US$'000	2005 US$'000
Profit before tax	**785,456**	419,258
Tax at the PRC income tax rate of 15% for the year	**117,818**	62,889
Effect of different tax rates of subsidiaries	**(338)**	(1,814)
Effect of tax exemptions granted to subsidiaries	**(49,768)**	(32,366)
Tax effect of expenses not deductible for tax purpose	**14,991**	7,141
Tax effect of income not taxable for tax purpose	**(5,098)**	(934)
Tax effect of tax losses not recognised	**244**	1,484
Decrease in opening deferred tax assets (liabilities) resulting from a decrease in applicable tax rate *(note a)*	**–**	110
Tax effect of income tax credits granted to a PRC subsidiary on acquisition of certain qualified equipment *(note b)*	**(6,261)**	–
Tax refund for reinvestment in a PRC subsidiary	**(2,680)**	–
Overprovision in prior years	**(1,298)**	(186)
Tax expense for the year	**67,610**	36,324

Notes:

(a) The decrease in opening deferred tax assets/liabilities was mainly attributable to changes in tax rates in Mexico and certain European countries.

(b) Pursuant to the relevant tax rules and regulations, PRC subsidiaries of the Company can claim PRC income tax credits on 40% of the acquisition cost of certain qualified equipment manufactured in the PRC. Such PRC income tax credits are allowed as deduction from current income tax expenses when relevant conditions are fulfilled and tax approval is obtained from the tax bureau.

13. DIVIDEND

No dividend was paid or proposed during 2006 (2005: Nil), nor has any dividend been proposed since the balance sheet date.

14. EARNINGS PER SHARE

The calculation of basic earnings per share is based on the profit for the year attributable to equity holders of parent of US$718,038,000 (2005: US$385,699,000) and the weighted average number of 6,966,517,747 (2005: 6,843,816,118) shares in issue.

The weighted average number of shares for the purpose of calculating the basic earnings per share for the year ended 31 December 2005 is adjusted for 4,640,000 shares for which their subscriptions have become unconditional on 29 December 2005.

The calculation of the diluted earnings per share attributable to the equity holders of the parent is based on the following data:

	2006	2005
	US$'000	US$'000
Earnings		
Earnings for the purposes of basic and diluted earnings per share (profit for the year attributable to equity holders of the parent)	**718,038**	385,699
Number of shares		
Weighted average number of ordinary shares for the purposes of basic earnings per share	**6,966,517,747**	6,843,816,118
Effect of dilutive potential ordinary shares:		
Share options	**266,877,813**	24,596,130
Weighted average number of ordinary shares for the purposes of diluted earnings per share	**7,233,395,560**	6,868,412,248

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15. PROPERTY, PLANT AND EQUIPMENT

	Land and buildings US$'000	Plant and machinery US$'000	Fixtures and equipment US$'000	Construction in progress US$'000	Total US$'000
COST					
At 1 January 2005	122,585	292,875	18,012	18,935	452,407
Exchange adjustments	(3,695)	(6,757)	(363)	(11)	(10,826)
Acquisition of a subsidiary	16,202	8,188	4,985	–	29,375
Additions	28,512	187,653	19,296	76,649	312,110
Disposals	(6,997)	(29,705)	(3,704)	–	(40,406)
Transfers	9,730	37,921	5,768	(53,419)	–
At 31 December 2005	166,337	490,175	43,994	42,154	742,660
Exchange adjustments	8,626	20,642	1,693	3,880	34,841
Additions	21,019	348,162	58,360	66,877	494,418
Disposals	(10,479)	(86,855)	(2,652)	–	(99,986)
Transfers	18,245	15,193	48	(33,486)	–
At 31 December 2006	**203,748**	**787,317**	**101,443**	**79,425**	**1,171,933**
DEPRECIATION AND IMPAIRMENT					
At 1 January 2005	5,653	20,035	5,046	–	30,734
Exchange adjustments	(633)	(5,052)	(65)	–	(5,750)
Charge for the year	6,719	58,238	7,477	–	72,434
Impairment loss	–	7,966	–	–	7,966
Eliminated on disposals	(2,763)	(19,965)	(1,788)	–	(24,516)
At 31 December 2005	8,976	61,222	10,670	–	80,868
Exchange adjustments	1,235	8,344	653	–	10,232
Charge for the year	10,330	106,079	18,221	–	134,630
Impairment loss	–	3,892	–	–	3,892
Eliminated on disposals	(2,506)	(57,830)	(1,257)	–	(61,593)
At 31 December 2006	**18,035**	**121,707**	**28,287**	**–**	**168,029**
CARRYING VALUES					
At 31 December 2006	**185,713**	**665,610**	**73,156**	**79,425**	**1,003,904**
At 31 December 2005	157,361	428,953	33,324	42,154	661,792

15. PROPERTY, PLANT AND EQUIPMENT *(Continued)*

Included in the land and buildings are freehold land, located in Hungary, Finland, Brazil, the United States of America, Mexico, India and Taiwan, having a cost of approximately US$29,493,000 (2005: US$17,119,000) in aggregate.

Certain property, plant and equipment are pledged to secure banking facilities granted to the Group as at the balance sheet dates (see note 36).

The impairment loss on property, plant and equipment provided during the year ended 31 December 2005 and 2006 mainly arose in connection with the Group's restructuring plan for its plant facilities in Europe. The recoverable amount is determined based on fair value less costs to sell. The fair values of these plant and machinery have been determined by the management by reference to recent market prices for similar plant and machinery.

The above items of property, plant and equipment are depreciated using the straight-line method, after taking into account their estimated residual value, over the following periods:

Freehold land	Nil
Buildings	20-40 years
Plant and machinery	5-10 years
Fixtures and equipment	3-5 years

16. PREPAID LEASE PAYMENTS

The amount represents land use rights in the PRC amortised over their relevant lease term ranging from 40 to 70 years.

17. AVAILABLE-FOR-SALE INVESTMENTS

	2006	2005
	US$'000	US$'000
Unlisted overseas equity investments, at cost	**1,010**	1,028

The above unlisted investments represent investments in unlisted equity securities issued by private entities incorporated in Taiwan and Finland. They are measured at cost less impairment at each balance sheet date because the range of reasonable fair value estimates is so significant that the directors of the Company are of the opinion that their fair values cannot be reliably measured.

18. GOODWILL

	2006	2005
	US$'000	US$'000
At 1 January	**63,075**	–
Arising on acquisition of a subsidiary	**–**	46,469
Arising on acquisition of additional interest in a subsidiary	**–**	16,606
At 31 December	**63,075**	63,075

The amount represents goodwill arising on the acquisition of 56.48% interest in CMCS (see note 28) in May 2005 and an additional 19.86% interest in CMCS subsequently acquired by the Group by end of 2005.

Goodwill has been allocated to one single cash generating unit, CMCS. At the end of 2006, the Group appointed a professional valuer to perform an appraisal of the value in use of CMCS. The recoverable amount has been determined based on a value in use calculation. That calculation uses cash flow projections based on financial budgets approved by management covering a 5-year period, and discount rate of 16.02%. Cash flows beyond the 5-year period has been extrapolated in perpetuity using a steady 5.5% growth rate. This growth rate is based on the relevant industry growth forecasts and does not exceed the average long-term growth rate for the relevant industry. Another key assumption for the value in use calculations is the budgeted gross margin, which is determined based on the unit's past performance and management's expectations for the market development. Management believes that any reasonably possible change in any of these assumptions would not cause the aggregate carrying amount to exceed the aggregate recoverable amount.

19. DEFERRED TAXATION

The following are the major deferred tax liabilities and assets recognised and movements thereon for the year:

	Allowances for inventories, trade and other receivables	Warranty provision	Accelerated tax depreciation	Tax losses	Prepaid expenses	Others	Total
	US$'000	US$'000	US$'000	US$'000	US$'000	US$'000	US$'000
At 1 January 2005	–	–	1,911	(8,961)	8,612	(1,972)	(410)
Acquisition of a subsidiary	–	–	–	(3,121)	–	–	(3,121)
Charge (credit) to income for the year	(279)	–	950	2,968	(8,612)	981	(3,992)
Exchange differences	–	–	5	65	–	–	70
Effect of change in tax rate – charge to the income statement	–	–	57	53	–	–	110
At 31 December 2005	(279)	–	2,923	(8,996)	–	(991)	(7,343)
Charge (credit) to income for the year	(4,237)	(7,483)	(1,114)	6,501	–	(281)	(6,614)
Exchange differences	–	(29)	100	(34)	–	23	60
At 31 December 2006	**(4,516)**	**(7,512)**	**1,909**	**(2,529)**	**–**	**(1,249)**	**(13,897)**

For the purposes of balance sheet presentation, certain deferred tax assets and liabilities have been offset. The following is the analysis of the deferred tax balances (after offset) for financial reporting purposes:

	2006	2005
	US$'000	US$'000
Deferred tax assets	**(15,806)**	(10,094)
Deferred tax liabilities	**1,909**	2,751
	(13,897)	(7,343)

19. DEFERRED TAXATION *(Continued)*

At the balance sheet date, the Group has unused tax losses of US$21,617,000 (2005: US$34,072,000) available for offset against future profits. A deferred tax asset has been recognised in respect of approximately US$10,115,000 (2005: US$24,175,000) of such losses. No deferred tax asset has been recognised in respect of the remaining US$11,502,000 (2005: US$9,897,000) either due to the unpredictability of future profit streams or because it is not probable that the unused tax losses will be available for utilisation before their expiry. The unrecognised tax losses will expire before 2011.

By reference to financial budgets, management believes that there will be sufficient future profits or taxable temporary differences available in the future for the realisation of deferred tax assets which have been recognised in respect of tax losses and other temporary differences.

The Group did not have material temporary differences associated with undistributed earnings of subsidiaries as at the balance sheet date. In addition, the Group is in a position to control the timing of the reversal of the temporary differences and it is probable that such difference will not reverse in the foreseeable future.

20. INVENTORIES

	2006	2005
	US$'000	US$'000
Raw materials	**346,264**	255,383
Work-in-progress	**126,561**	113,970
Finished goods	**271,373**	144,646
	744,198	513,999

21. INVESTMENTS HELD FOR TRADING

The amount represents investment in listed bond funds on the Taiwan Stock Exchange held for trading purpose. The fair values are determined based on the quoted market bid prices available on the Taiwan Stock Exchange as at 31 December 2006.

22. TRADE AND OTHER RECEIVABLES

	2006	2005
	US$'000	US$'000
Trade receivables	**1,814,813**	1,488,078
Other receivables, deposits and prepayments	**62,847**	24,771
	1,877,660	1,512,849

The Group normally allows an average credit period of 30 to 90 days to its trade customers.

22. TRADE AND OTHER RECEIVABLES *(Continued)*

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

	2006 US$'000	2005 US$'000
0-90 days	**1,806,005**	1,485,673
91-180 days	**8,352**	2,042
181-360 days	**385**	288
Over 360 days	**71**	75
	1,814,813	1,488,078

The fair value of the Group's trade and other receivables at the balance sheet dates approximates to the corresponding carrying amount.

23. TRADE AND OTHER PAYABLES

	2006 US$'000	2005 US$'000
Trade payables	**1,540,285**	1,202,338
Accruals and other payables	**326,485**	206,402
	1,866,770	1,408,740

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

	2006 US$'000	2005 US$'000
0-90 days	**1,468,343**	1,192,824
91-180 days	**62,039**	2,055
181-360 days	**7,053**	5,563
Over 360 days	**2,850**	1,896
	1,540,285	1,202,338

The fair value of the Group's trade and other payables at the balance sheet dates approximates to the corresponding carrying amount.

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24. BANK LOANS

	2006	2005
	US$'000	US$'000
Unsecured	139,563	175,548

The loans as at 31 December 2006 are obtained with original maturity of six months, denominated in US$ and carry interest at fixed interest rates at 0.2% plus LIBOR (2005: 0.4% plus LIBOR) per annum at the time the loans are raised.

The fair value of the Group's bank borrowings at the balance sheet dates approximates to the corresponding carrying amount.

25. SHARE CAPITAL

	Number of shares	Amount
		US$'000
Ordinary shares of US$0.04 each, authorised:		
Balance at 31 December 2005 and 31 December 2006	20,000,000,000	800,000
Ordinary shares of US$0.04 each, issued and fully paid:		
Balance at 1 January 2005	5,970,000,025	238,800
Issued on 2 February 2005	869,400,000	34,776
Issued on 28 February 2005	87,101,000	3,484
Issued on 19 August 2005	26,915,000	1,077
Balance at 31 December 2005	6,953,416,025	278,137
Issued on 4 January 2006	4,640,000	185
Exercise of share options *(note 35(a))*	28,731,520	1,149
Issued pursuant to a share scheme *(note 35(c))*	3,168,000	127
Balance at 31 December 2006	6,989,955,545	279,598

Pursuant to the Company's global offering, the Company issued 869,400,000 and 87,101,000 shares of US$0.04 each for consideration of HK$3.88 (equivalent to US$0.5) per share on 2 February 2005 and 28 February 2005, respectively. The Company's shares were listed on the Stock Exchange on 3 February 2005.

On 19 August 2005, the Company allotted and issued a total of 26,915,000 shares of US$0.04 each to certain employees of CMCS for cash consideration of HK$5.065 (equivalent to US$0.6) per share. These shares rank pari passu in all respects with the then existing shares in issue.

25. SHARE CAPITAL *(Continued)*

On 15 December 2005, the Company entered into subscription agreements (the "Subscription Agreements") with certain employees of CMCS, pursuant to which the Company agreed to allot and issue an aggregate of 4,640,000 new shares of US$0.04 each for cash consideration of HK$12.5 (equivalent to US$1.6) per share. These shares rank pari passu in all respects with the then existing shares in issue. Pursuant to the Subscription Agreements, the subscriptions have become unconditional as at 29 December 2005 and the 4,640,000 new shares were subsequently issued on 4 January 2006. The subscription price received of HK$58,000,000 (equivalent to US$7,480,000) is included as equity of the Company as at 31 December 2005.

During the year, the Company issued 3,168,000 shares pursuant to a share scheme adopted on 12 January 2005. Details of the share scheme are disclosed in note 35 to the consolidated financial statements.

26. RESERVES

The Group's special reserve represents the difference between the paid-in capital of the subsidiaries acquired pursuant to group reorganisation in 2004 and the nominal value of the Company's shares issued in exchange therefrom.

The Group's legal reserve represents statutory reserve attributable to the Company's subsidiaries in the PRC. As required by the laws in the PRC, appropriations are made from the profit of these subsidiaries to the legal reserve until the balance reaches 50% of the registered capital of the subsidiaries. This reserve can only be used to make up losses incurred or to increase capital.

27. DERIVATIVES

Currency derivatives

The Group utilises currency derivatives to hedge significant future transactions and cash flows. The Group is a party of utilising a variety of forward foreign currency contracts in the management of its exchange rate exposures. The instruments adopted are primarily to hedge the currencies used in the Group's principal markets.

At the balance sheet date, total notional amount of outstanding forward foreign exchange contracts that the Group has committed are as below.

	2006	2005
	US$'000	US$'000
Forward foreign exchange contracts	**29,069**	15,152

As at 31 December 2006, the fair value of the Group's currency derivatives is estimated to be approximately US$384,000 liabilities (2005: US$203,000 assets), based on market values provided by the banks of equivalent instruments, and is included as other payables (2005: other receivables) at the balance sheet date. The contracts mainly related to buying of Japanese Yen and Euro with maturities in January 2007.

27. DERIVATIVES *(Continued)*

Interest rate swaps

The Group uses interest rate swaps to manage its exposure to interest rate movements on certain of its bank borrowings.

As at 31 December 2006, contracts with nominal values of US$6,600,000 (2005: US$9,500,000) have fixed interest payments at an average rate of 4 per cent for periods until 2007 (2005: until 2008) and have floating interest receipts based on The Bond Market Association Municipal Swap Index.

The fair value of the swaps is estimated at approximately US$7,000 liabilities (2005: US$188,000 liabilities) and is included as other payables at the balance sheet date. These amounts are based on market values provided by the bank of equivalent instruments at the balance sheet date.

28. ACQUISITION OF SUBSIDIARIES

On 12 May 2005, Transworld Holdings Limited entered into two sale and purchase agreements with two vendors respectively to acquire 56.48% interest in CMCS. The acquisition of CMCS was completed after approval was obtained from the Investment Commission of the Ministry of Economic Affairs of Taiwan on 30 May 2005.

These transactions have been accounted for by the purchase method of accounting. The fair value of net assets acquired in the transactions, and the goodwill arising, are as follows:

	2005 US$'000
Property, plant and equipment	29,375
Available-for-sale investments	955
Deferred tax assets	3,121
Inventories	19,295
Trade and other receivables	25,756
Investments held for trading	13,182
Bank balances and cash	4,678
Trade and other payables	(25,187)
Provision	(5,766)
Tax payable	(1,105)
Bank loans	(5,965)
Net assets acquired	58,339
Minority interests	(25,389)
Goodwill arising on the acquisition	46,469
	79,419
Total consideration, satisfied by:	
Cash	79,419
Net cash outflow arising on acquisition:	
Cash consideration paid	79,419
Bank balances and cash acquired	(4,678)
	74,741

28. ACQUISITION OF SUBSIDIARIES *(Continued)*

The directors had completed an evaluation of the fair value of assets and liabilities acquired pursuant to the acquisition of CMCS and concluded that the carrying amount of the net assets acquired before the combination approximates it fair value.

The goodwill arising on the acquisition of CMCS is attributable to the anticipated future operating synergies from the combination. CMCS is a Taiwan-based original design manufacturer of handsets. The directors believe that the acquisition of CMCS will enhance the Group's design capabilities, reinforce the Group's vertical integration business strategy and strengthen the provision of value-added services to its existing customers.

CMCS contributed approximately US$42,681,000 of turnover and loss for the year attributable to equity holders of the parent of US$4,659,000 for the period between the date of acquisition and 31 December 2005.

If the acquisition of CMCS had been completed on 1 January 2005, total group turnover for 2005 would have been US$6,471,027,000, and the profit for 2005 would have been US$386,320,000. The proforma information is for illustrative purposes only and is not necessarily an indicative turnover and results of the Group that actually would have been achieved had the acquisition been completed on 1 January 2005, nor is it intended to be a projection of future results.

29. BANK DEPOSITS AND BANK BALANCES AND CASH

Bank deposits carry at prevailing market interest rate of 1.98% (2005: 1.94%) per annum with original maturity of over three months.

Bank balances and cash comprise cash held by the Group and short term bank deposits with an original maturity of three months or less. The deposits carry at prevailing market interest rate of 2.43% (2005: 1.70%) per annum.

The fair value of bank deposits and bank balances at balance sheet dates approximates to the corresponding carrying amount.

30. PROVISION

	2006	2005
	US$'000	US$'000
At 1 January	**23,635**	–
Exchange adjustments	**1,366**	–
Acquired on an acquisition of a subsidiary	**–**	5,766
Provision for the year	**61,323**	22,068
Utilisation of provision	**(28,112)**	(4,199)
At 31 December	**58,212**	23,635

The warranty provision represents management's best estimate of the Group's liability under twelve to twenty-four months' warranty granted on handset products, based on prior experience and industry averages for defective products.

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31. CAPITAL COMMITMENTS

	2006 US$'000	2005 US$'000
Commitments for the acquisition of property, plant and equipment contracted but not provided for	**57,389**	17,369

32. OPERATING LEASE ARRANGEMENTS

The Group as lessee

	2006 US$'000	2005 US$'000
Minimum lease payments under operating leases in respect of premises recognised for the year	**12,296**	2,765

At the balance sheet date, the Group had outstanding commitments under non-cancellable operating leases in respect of premises, which fall due as follows:

	2006 US$'000	2005 US$'000
Within one year	**9,018**	2,059
In the second to fifth years inclusive	**4,394**	491
	13,412	2,550

Leases are negotiated, and rentals are fixed, for an average term of one to three years.

33. RELATED PARTY TRANSACTIONS

(a) During the year, the Group entered into the following transactions with related parties, including Hon Hai, the Company's ultimate holding company, and subsidiaries and associates of Hon Hai other than members of the Group:

	2006	2005
	US$'000	US$'000
Hon Hai		
Sales of goods	**6,006**	359
Purchase of goods	**51,466**	11,322
Purchase of property, plant and equipment	**10,592**	2,952
Sales of property, plant and equipment	**975**	2,141
Subcontracting income	**10,614**	2,638
Lease expense	**8**	68
Research and development expense	**–**	18
Subcontracting expense	**525**	41
General service expense	**190**	–
Design service	**5,435**	–
Subsidiaries and associates of Hon Hai		
Sales of goods	**247,327**	74,618
Purchase of goods	**1,012,846**	433,503
Purchase of property, plant and equipment	**12,745**	14,446
Sales of property, plant and equipment	**34,590**	6,698
Lease expense	**4,451**	1,683
Subcontracting income	**41,880**	994
Subcontracting expense	**26,743**	16,802
General service expense	**32,535**	17,103
Research and development expense	**2,250**	4,724

33. RELATED PARTY TRANSACTIONS *(Continued)*

(b) At the balance sheet date, the Group has the following balances due from/to related parties included in:

	2006	2005
	US$'000	US$'000
Trade receivables:		
Hon Hai	**14,802**	344
Subsidiaries and associates of Hon Hai	**92,130**	47,203
	106,932	47,547
Other receivables:		
Hon Hai	**5**	27
Subsidiaries and associates of Hon Hai	**587**	768
	592	795
	107,524	48,342
Trade payables:		
Hon Hai	**46,328**	2,476
Subsidiaries and associates of Hon Hai	**255,473**	202,427
	301,801	204,903
Other payables:		
Hon Hai	**5,479**	184
Subsidiaries and associates of Hon Hai	**6,873**	10,367
	12,352	10,551
	314,153	215,454

Balances due from/to related parties are unsecured, interest free and are repayable within one year.

(c) Compensation of key management personnel

The remuneration of directors and other members of key management during the year was as follows:

	2006	2005
	US$'000	US$'000
Short-term benefits	**2,173**	2,102
Share-based payments	**7,039**	2,645
	9,212	4,747

34. RETIREMENT BENEFITS PLANS

Majority of the employees of the Company's subsidiaries are members of state-managed retirement benefit schemes operated by the government in the PRC. These subsidiaries in the PRC are required to contribute a specified percentage ranging from 5% to 20% of their payroll costs to the retirement benefit schemes to fund the benefits. The only obligation of the Group with respect to the retirement benefit schemes is to make the specified contributions.

Certain subsidiaries of the Company operate defined benefit plans in Taiwan and Korea. Under the schemes, the employees are entitled to retirement benefits on attainment of a retirement age ranging from 55 to 60. The most recent actuarial valuations of plan assets and the present value of the defined benefit obligation were carried out at 31 December 2006 by 徐茂欽精算師, 中華民國精算師協會 (Hsu Mao-Chin Actuary, The Actuarial Institute of the Republic of China), 蔡惠玲精算師, 中華民國精算師協會 (Tsai Hui-Ling, The Actuarial Institute of the Republic of China) and Watson Wyatt Philippines Inc., respectively. The present value of the defined benefit obligation, the related current service cost and past service cost were measured using the projected unit credit method.

The main actuarial assumptions used were as follows:

	2006	2005
Discount rate	**2.5% – 5.0%**	3.5%
Expected return on plan assets	**2.5% – 5.0%**	3.5%
Expected rate of salary increases	**2.0% – 5.0%**	3.0%
Future pension increases	**–**	–

The actuarial valuation showed that the market value of plan assets was US$1,954,000 (2005: US$582,000) and that the actuarial value of these assets represented 39% (2005: 95%) of the benefits that had accrued to members.

Amounts recognised in the consolidated income statement in respect of the defined benefit plans are as follows:

	2006 **US$'000**	2005 US$'000
Current service cost	**265**	150
Interest cost	**121**	23
Expected return on plan assets	**(41)**	(15)
Net actuarial (gains)/losses	**–**	–
Past service cost	**165**	15
	510	173

Of the charge for the year, US$433,000 (2005: US$75,000) has been included in cost of sales and US$77,000 (2005: US$98,000) has been included in administrative expenses.

The actual return on plan assets was US$14,000 (2005: US$4,000) as at 31 December 2006.

34. RETIREMENT BENEFITS PLANS *(Continued)*

The amount included in the consolidated balance sheet arising from the Group's obligation in respect of its defined benefit retirement benefit plans is as follows:

	2006 US$'000	2005 US$'000
Present value of funded defined benefit obligations	**4,989**	610
Fair value of plan assets	**(1,954)**	(582)
	3,035	28
Present value of unfunded defined benefit obligations	–	–
Deficit	**3,035**	28
Net actuarial gains and losses not recognised	**90**	208
Past service cost not recognised	**(3,373)**	(206)
Net (asset) liability arising from defined benefit obligations	**(248)**	30

The Group also operates a number of defined contribution schemes in other overseas locations. Arrangements for these staff retirement benefits vary from country to country and are made in accordance with local regulations and custom.

35. SHARE-BASED PAYMENT TRANSACTIONS

(a) Equity-settled share option scheme

On 12 January 2005, the Company adopted a share option scheme (the "Option Scheme") for the primary purpose of attracting skilled and experienced personnel and incentivizing them to remain with the Group. Under the Option Scheme, the board of directors of the Company may grant options to eligible employees, including directors of the Company and its subsidiaries, to subscribe for shares in the Company. Additionally, the Company may, from time to time, grant share options to third party service providers for services provided by them to the Group. The Option Scheme will expire on 3 February 2015.

Under the Option Scheme, the directors of the Company may at their discretion grant options to any eligible person to subscribe for shares in the Company. The directors may at their discretion determine the specific exercise period which should expire in any event no later than ten years from the effective date of the Option Scheme.

35. SHARE-BASED PAYMENT TRANSACTIONS *(Continued)*

(a) Equity-settled share option scheme *(Continued)*

The total number of shares which may initially be issued upon the exercise of all options to be granted under the Option Scheme and any other share option scheme(s) adopted by the Company must not in aggregate exceed 10% of the total number of issued shares of the Company as of the date of listing its shares on the Stock Exchange, i.e. must not exceed 683,940,003 shares. Subject to the approval of the shareholders of the Company in general meeting, the limit may be refreshed to 10% of the total number of shares in issue as at the date of approval of the refreshed limit. Notwithstanding the foregoing, the maximum number of shares which may be issued upon exercise of all outstanding options granted and yet to be exercised under the Option Scheme and any other share option scheme(s) of the Company must not in aggregate exceed 30% of the number of issued shares of the Company from time to time. Pursuant to an ordinary resolution passed at the Company's annual general meeting held on 8 June 2006, the 10% scheme limit was refreshed to 695,805,602 shares, representing 10% of the total number of issued shares of the Company as at the date of passing of the resolution. The maximum number of shares of the Company in respect of which options granted and to be granted to each eligible person under the Option Scheme of the Company in any 12-month period up to the date of the latest grant shall not exceed 1% of the total number of issued shares of the Company from time to time. The maximum number of shares issued and to be issued upon exercise of options granted and to be granted (including options exercised, cancelled and outstanding) to a substantial shareholder and/or an independent non-executive director, or their respective associates, in the 12-month period up to and including the date of such grant in aggregate over 0.10% of total number of issued shares of the Company from time to time and have an aggregate value exceeding HK$5,000,000 must be approved by the shareholders of the Company in general meeting.

Options granted must be taken up within 30 days after the date of grant, upon payment of HK$1.0 per offer. The Option Scheme does not contain any minimum period for which an option must be held before it can be exercised, though such minimum period may be specified by the board of directors of the Company at the time of grant. The exercise price is determined by the board of directors of the Company, and will not be less than the higher of (i) the closing price of the Company's shares on the date of grant; (ii) the average closing price of the shares for the five business days immediately preceding the date of grant; and (iii) the nominal value of the Company's share.

On 25 July 2005, 435,599,000 share options were granted at an exercise price of HK$6.06. The options are granted with vesting period ranging from one to six years from the date of grant. The share options are exercisable from the vesting date to 31 December 2011, the maturity date for these options, subject to the terms and conditions of the Option Scheme. The estimated fair value of the options granted on 25 July 2005 was US$104,038,000.

The closing price of the shares immediately before 25 July 2005, the date of grant of options, was HK$5.75.

35. SHARE-BASED PAYMENT TRANSACTIONS *(Continued)*

(a) Equity-settled share option scheme *(Continued)*

The following table discloses movements of the Company's share options held by employees during the year ended 31 December 2006:

Option type	Outstanding at 1/1/2006	Granted during year	Exercised during year	Lapsed during year	Expired during year	Outstanding at 31/12/2006
2005	**435,290,000**	**–**	**(28,731,520)**	**(3,644,200)**	**–**	**402,914,280**

The following table discloses movements of the Company's share options held by employees during the year ended 31 December 2005:

Option type	Outstanding at 1/1/2005	Granted during year	Exercised during year	Lapsed during year	Expired during year	Outstanding at 31/12/2005
2005	–	435,599,000	–	(309,000)	–	435,290,000

44,795,010 share options are exercisable as at 31 December 2006 (2005: Nil).

In respect of the share options exercised during the year, the weighted average share price at the dates of exercise is US$3.01 (equivalent to HK$23.41).

The Group recognised total expense of US$32,448,000 (2005: US$17,274,000) for the year ended 31 December 2006 in relation to the share options granted by the Company.

The fair value of the share options was calculated using the Black-Scholes option pricing model. The inputs into the model were as follows:

Share price on date of grant	US$0.76 (equivalent to HK$5.95)
Exercise price	US$0.76 (equivalent to HK$6.06)
Expected volatility	30%
Expected life	Vesting period plus 1.5 years
Risk free rate	3.3925%
Dividend yield	0%

Because the Black-Scholes option pricing model requires the input of highly subjective assumptions, including the volatility of share prices, changes in subjective input assumptions can materially affect the fair value estimate.

Expected volatility was determined by calculating the historical volatility of the Company's share price over the period from 3 February 2005 (date of listing) to grant date. The expected life in the model has been adjusted, based on management's best estimate, for the effect of non transferability, exercise restrictions and behavioral considerations.

35. SHARE-BASED PAYMENT TRANSACTIONS *(Continued)*

(b) Cash-settled share-based payments

During the year ended 31 December 2006, the Group issued to certain employees share appreciation rights ("SAR") at exercise prices ranging from HK$12.00 to HK$26.05 with vesting period ranging from one to three years from the grant date. The SARs require the Group to pay the intrinsic value of the SAR to the employee at the date of exercise. At 31 December 2006, the Group has recorded liabilities of US$3,429,000 (2005: Nil) and recorded total expenses of US$3,429,000 (2005: Nil) for the year then ended. The fair value of the SARs is determined using the Black-Scholes pricing model with expected volatility of 44.27%, risk free rate of 4.33% and dividend yield of 0%. The SARs granted have not been vested up to 31 December 2006.

(c) Other share-based payment plan

Pursuant to a share scheme adopted by the Company on 12 January 2005 (the "Share Scheme"), the Company may grant free shares to the directors, employees of the Company or its subsidiaries or third party service providers including employees of Hon Hai and its other subsidiaries.

On 29 December 2006, the Company awarded 5,748,145 ordinary shares to certain employees pursuant to the share scheme, of which 3,010,427 shares awarded were vested immediately, while the remaining shares are granted with lock-up periods ranging from one to three years from the grant date. No consideration is payable on the grant of the shares and the shares were subsequently issued on 2 February 2007.

On 31 December 2005, the Company awarded 3,273,000 shares to its employees pursuant to the share scheme, of which 1,723,000 shares awarded were vested immediately, while the remaining shares are granted with lock-up periods ranging from one to three years from the grant date. No consideration is payable on the grant of the shares. During the current year, the rights to 105,000 shares awarded are waived by employees upon their termination of employment, and the remaining 3,168,000 ordinary shares are issued on 26 September 2006.

The Group recognised total expense of US$21,435,000 (2005: US$2,802,000) for the year ended 31 December 2006 in relation to the ordinary shares awarded by the Company under the Share Scheme.

36. PLEDGE OF ASSETS

As at the balance sheet date, the Group pledged property, plant and equipment having a carrying value of approximately US$4,603,000 (2005: US$19,727,000) to secure general banking facilities granted to the Group. The bank facilities were unutilised as at 31 December 2006.

37. PRINCIPAL SUBSIDIARIES

The Company has the following principal subsidiaries as at 31 December 2006:

Name of subsidiary	Form of business structure	Place of incorporation/ establishment	Issued and fully paid share capital/ registered capital	Attributable equity interest held by the Company		Principal activities
				Directly	Indirectly	
CMCS	Limited company	Taiwan	NT$1,500,000,000	–	76.332%	Design and manufacture of handsets
S&B USA Inc. (formerly Dynacept Corporation)	Limited company	United States of America ("USA")	US$1,000	–	100%	Inactive
Foxconn Pecs Kft	Limited company	Hungary	EUR735,000	–	100%	Inactive
FIH Co., Limited	Limited company	Taiwan	NT$1,000,000	100%	–	Provision of services to group companies
Foxconn Beijing Trading Co., Ltd.	Limited company	British Virgin Islands ("BVI")	US$1	100%	–	Trading of handsets
Foxconn DK ApS	Limited Company	Denmark	DKK2,100,000	–	100%	Research development and project management
Foxconn Hungary Kft	Limited company	Hungary	HUF10,039,000,000	–	100%	Manufacture of handsets
Foxconn Mexico Precision Industry, Co. SA de CV.	Limited company	Mexico	MXN969,094,000	–	100%	Manufacture of handsets
Foxconn Oy	Limited company	Finland	EUR1,558,800	–	100%	Manufacture of handsets
富士康精密組件(北京)有限公司 (Foxconn Precision Component (Beijing) Co., Ltd.)	Wholly foreign owned enterprise	PRC	US$68,800,000	–	100%	Manufacture of handsets
宏訊電子工業(杭州)有限公司 (Honxun Electrical Industry (Hangzhou) Co., Ltd.)	Wholly foreign owned enterprise	PRC	US$68,800,000	–	100%	Manufacture of handsets

37. PRINCIPAL SUBSIDIARIES *(Continued)*

Name of subsidiary	Form of business structure	Place of incorporation/ establishment	Issued and fully paid share capital/ registered capital	Attributable equity interest held by the Company Directly	Attributable equity interest held by the Company Indirectly	Principal activities
S&B Industry, Inc.	Limited company	USA	US$31,594,767	–	100%	Plastics manufacturing
S&B Industry Technologies Limited Partnership	Limited company	USA	US$7,218,280	–	100%	Repair Center
深圳富泰宏精密工業有限公司 (Shenzhen Futaihong Precision Industrial Co., Ltd.)	Wholly foreign owned enterprise	PRC	US$178,520,000	–	100%	Manufacture of handsets
Success World Holdings Limited	Limited company	Hong Kong	HK$388,525,000	100%	–	Investment holding
Sutech Industry Inc.	Limited company	USA	US$10,000	–	100%	Provision of logistics services to group companies
Sutech Trading Limited	Limited company	BVI	US$1	–	100%	Trading of handsets
富士康(天津)精密工業有限公司 (Foxconn (Tianjin) Precision Industry Co., Ltd.)	Wholly foreign owned enterprise	PRC	US$19,800,000	–	100%	Manufacture of handsets
Foxconn do Brasil Indústria e Comércio de Electrônicos Ltda. (formerly Triple S Cosmoplast da Amazonia, Ltda.)	Limited company	Brazil	BRL$23,828,402	–	100%	Manufacture of handsets
Foxconn India Private Limited	Limited company	India	INR19,999,900	–	100%	Manufacturing, import, export distribution and assembly
富士康精密電子(烟台)有限公司 (Foxconn Precision Electronics (Yantai) Co., Ltd.)	Wholly foreign owned enterprise	PRC	USD8,000,000	–	100%	Manufacture of handsets

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37. PRINCIPAL SUBSIDIARIES *(Continued)*

Name of subsidiary	Form of business structure	Place of incorporation/ establishment	Issued and fully paid share capital/ registered capital	Attributable equity interest held by the Company Directly	Attributable equity interest held by the Company Indirectly	Principal activities
富士康精密電子(太原)有限公司 (Foxconn Precision Electronics (Taiyuan) Co., Ltd.)	Wholly foreign owned enterprise	PRC	USD52,500,000	–	100%	Manufacture of handsets
富泰京精密電子(北京)有限公司 (Futaijing Precision Electronics (Beijing) Co., Ltd.)	Wholly foreign owned enterprise	PRC	USD15,000,000	–	100%	Manufacture of handsets
廊坊全義電子有限公司	Wholly foreign owned enterprise	PRC	RMB190,000,000	–	100%	Manufacture of handsets
Foxconn Reynosa S.A. De C.V.	Limited company	Mexico	MXN50,000	–	100%	Inactive
FIH Technology Korea Ltd.	Limited company	Korea	KRW51,700,000	–	100%	Research development and project management

None of the subsidiaries had issued any debt securities at the end of the year.

The above table lists the subsidiaries of the Company which, in the opinion of the directors, principally affected the results for the year or formed a substantial portion of the net assets of the Group. To give details of other subsidiaries would, in the opinion of the directors, result in particulars of excessive length.