Notes to the ACCOUNTS

1. General information

Prime Success International Group Limited (the "Company") and its subsidiaries (collectively referred to as the "Group") is principally engaged in the manufacturing and distribution of footwear products in China with major export market in the United States of America (the "US").

The Company is a company incorporated in the Cayman Islands with limited liability and it shares are listed on The Stock Exchange of Hong Kong Limited. The address of its registered office is Ugland House, South Church Street, P. O. Box 309, George Town, Grand Cayman, Cayman Islands, British West Indies.

These consolidated accounts have been approved for issue by the Board of Directors on 23 April 2007.

2. Principal accounting policies

The principal accounting policies applied in the preparation of these consolidated accounts are set out below. These policies have been consistently applied to all the years presented unless otherwise stated.

(a) Basis of preparation

The consolidated accounts have been prepared in accordance with all applicable Hong Kong Financial Reporting Standards ("HKFRSs") and Hong Kong Accounting Standards ("HKASs") issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA"). The consolidated accounts have been prepared under the historical cost convention, as modified by the revaluation of available-for-sale financial assets, financial assets and financial liabilities (including derivative instruments) at fair value through profit or loss.

The preparation of accounts in conformity with HKFRSs and HKASs requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated accounts, are disclosed in Note 4.

Adoption of new/revised HKFRSs and HKASs

In 2006, the Group adopted the following new/revised HKFRSs and HKASs which are relevant to its operations:

HKAS 21 (Amendment)	Net Investment in a Foreign Operation
HKAS 39 (Amendment)	Cash Flow Hedge Accounting of Forecast Intragroup Transactions
HKAS 39 (Amendment)	The Fair Value Option
HKAS 39 and HKFRS 4 (Amendment)	Financial Guarantee Contracts
HKFRS – Int 4	Determining whether an Arrangement contains a Lease

The adoption of the above new/revised accounting standards has no material impact on the Group's consolidated accounts.

The Group has not early adopted the following new standards, amendments and interpretations that have been issued by the HKICPA but not yet effective in these accounts:

		Effective for accounting periods beginning on or after
HKAS 1 (Amendment)	Capital Disclosures	1 January 2007
HKFRS 7	Financial Instruments: Disclosures	1 January 2007
HKFRS 8	Operating Segments	1 January 2009
HKFRS – Int 7	Applying the Restatement Approach under HKAS 29, Financial Reporting in Hyperinflationary Economies	1 March 2006
HKFRS – Int 8	Scope of HKFRS 2	1 May 2006
HKFRS – Int 9	Reassessment of Embedded Derivatives	1 June 2006
HKFRS – Int 10	Interim Financial Reporting and Impairment	1 November 2006
HKFRS – Int 11	HKFRS 2 – Group and Treasury Share Transactions	1 March 2007
HKFRS – Int 12	Service Concession Arrangements	1 January 2008

2. Principal accounting policies (Continued)

(a) Basis of preparation (Continued)

The Group has already commenced an assessment of the related impact to the Group but is not yet in a position to state whether substantial changes to the Group's accounting policies and presentation of the accounts will be resulted.

(b) Consolidation

The consolidated accounts include the accounts of the Company and all of its subsidiaries made up to 31 December.

(i) Subsidiaries

Subsidiaries are all entities over which the Group has the power to govern the financial and operating policies generally accompanying a shareholding of more than one half of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group controls another entity.

Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are de-consolidated from the date that control ceases.

The purchase method of accounting is used to account for the acquisition of subsidiaries by the Group. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any minority interest. The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognized directly in the consolidated profit and loss account.

Inter-company transactions, balances and unrealized gains on transactions between group companies are eliminated. Unrealized losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group.

In the Company's balance sheet the investments in subsidiaries are stated at cost less provision for impairment losses. The results of subsidiaries are accounted by the Company on the basis of dividend received and receivable.

(ii) Transactions with minority interests

The Group applies a policy of treating transactions with minority interests as transactions with parties external to the Group. Disposals to minority interests result in gains or losses for the Group that are recorded in the consolidated profit and loss account. Purchases from minority interests result in goodwill, being the difference between any consideration paid and the relevant share acquired of the carrying value of net assets of the subsidiary.

(iii) Associated company

An associated company is an entity over which the Group has significant influence but not control, generally accompanying a shareholding of between 20% and 50% of the voting rights. Investment in an associated company is accounted for using the equity method of accounting and are initially recognized at cost.

The Group's share of its associated company's post-acquisition profits or losses is recognized in the consolidated profit and loss account, and its share of post-acquisition movements in reserves is recognized in reserves. The cumulative post-acquisition movements are adjusted against the carrying amount of the investment. When the Group's share of losses in the associated company equals or exceeds its interest in the associated company, including any other unsecured receivables, the Group does not recognize further losses, unless it has incurred obligations or made payments on behalf of the associated company.

Unrealized gains on transactions between the Group and its associated company are eliminated to the extent of the Group's interest in the associated company. Unrealized losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of an associated company have been changed where necessary to ensure consistency with the policies adopted by the Group.

Dilution gains and losses in an associated company are recognized in the consolidated profit and loss account.

2. Principal accounting policies (Continued)

(c) Foreign currency translation

(i) Functional and presentation currency

Items included in the accounts of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates (the "functional currency"). The consolidated accounts are presented in Hong Kong dollars, which is different from the Group's functional currency of Renminbi. The directors consider that presentation of consolidated accounts in Hong Kong dollars will facilitate analysis of financial information of the Group.

(ii) Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognized in the profit and loss account.

Changes in the fair value of monetary securities denominated in foreign currency classified as available-for-sale are analysed between translation differences resulting from changes in the amortized cost of the security and other changes in the carrying amount of the security. Translation differences related to changes in the amortized cost are recognized in the profit and loss account, and other changes in the carrying amount are recognized in equity.

Translation differences on non-monetary financial assets and liabilities are reported as part of the fair value gain or loss. Translation differences on non-monetary financial assets and liabilities such as equities held at fair value through profit or loss are recognized in the profit and loss account as part of the fair value gain or loss. Translation differences on non-monetary financial assets such as equities classified as available-for-sale are included in the fair value adjustment reserve in equity.

(iii) Group companies

The results and financial position of all the group entities (none of which has the currency of a hyperinflationary economy) that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

- assets and liabilities for each balance sheet presented are translated at the closing rate at the date of that balance sheet;

- income and expenses for each profit and loss account are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the dates of the transactions); and

- all resulting exchange differences are recognized as a separate component of equity.

On consolidation, exchange differences arising from the translation of the net investment in foreign operations, and of borrowings and other currency instruments designated as hedges of such investments, are taken to shareholders' equity. When a foreign operation is partially disposed of or sold, such exchange differences are recognized in the consolidated profit and loss account as part of the gain or loss on sale.

Goodwill and fair value adjustments arising on the acquisition of a foreign entity are treated as assets and liabilities of the foreign entity and translated at the closing rate.

(d) Operating leases

Leases where substantially all the risks and rewards of ownership of assets remain with the lessor are accounted for as operating leases. Payments made under operating leases net of any incentives received from the lessor are charged to the profit and loss account on a straight-line basis over the lease periods.

2. Principal accounting policies (Continued)

(e) Goodwill

Goodwill represents the excess of the cost of an acquisition over the fair value of the Group's share of the net identifiable assets of the acquired subsidiaries at the date of acquisition. Goodwill on acquisition of subsidiaries is included in intangible assets. Separately recognized goodwill is tested annually for impairment and carried at cost less accumulated impairment losses. Impairment losses on goodwill are not reversed. Gains or losses on the disposal of an entity include the carrying amount of goodwill relating to the entity sold.

Goodwill is allocated to cash-generating units for the purpose of impairment testing. The allocation is made to those cash-generating units or groups of cash-generating units that are expected to benefit from the business combination in which the goodwill arose.

(f) Land use rights

Land use rights are stated at cost less accumulated amortization and accumulated impairment losses if any. Cost mainly represents the consideration paid for the rights to use the land on which various plants and buildings are situated for a period of 10 to 50 years from the date the respective right was granted. Amortization of land use rights is calculated on a straight-line basis over the period of the rights.

(g) Fixed assets

Fixed assets, comprise leasehold buildings, leasehold improvements, construction-in-progress, plant and machinery, furniture, fixtures and equipment and motor vehicles, are stated at historical cost less accumulated depreciation and accumulated impairment losses if any. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Subsequent costs are included in the asset's carrying amount or recognized as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. The carrying amount of the replaced part is derecognized. All other repairs and maintenance are expensed in the profit and loss account during the financial period in which they are incurred.

Fixed assets are depreciated at rates sufficient to write off their cost less accumulated impairment losses to their residual value over their estimated useful lives on a straight-line basis. The principal annual rates are as follows:

Leasehold buildings	Over the terms of the lease or 50 years, whichever is shorter
Leasehold improvements	Over the terms of the lease or 2 to 5 years, whichever is shorter
Plant and machinery	20%
Furniture, fixtures and equipment	20%
Motor vehicles	20%

Construction-in-progress represents fixed assets under construction and pending installation and is stated at cost less accumulated impairment losses if any. Cost includes the costs of construction of buildings and the costs of plant and machinery. No provision for depreciation is made on construction-in-progress until such time as the relevant assets are completed and are available for intended use. When the assets concerned are brought into use, the costs are transferred to fixed assets and depreciated in accordance with the policy stated above.

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount (Note 2(h)).

The gain or loss on disposal of a fixed asset is the difference between the net sales proceeds and the carrying amount of the relevant asset, and is recognized in the profit and loss account.

2. Principal accounting policies (Continued)

(h) Impairment of assets

Assets that have an indefinite useful life or have not yet available for use are not subject to amortization and are tested annually for impairment. Assets that are subject to amortization are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognized for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). Assets other than goodwill that suffered an impairment are reviewed for possible reversal of the impairment at each balance sheet date.

(i) Financial assets

The Group classifies its financial assets in the following categories: financial assets at fair value through profit or loss, loans and receivables and available-for-sale financial assets. The classification depends on the purpose for which the financial assets were acquired. Management determines the classification of its financial assets at initial recognition.

(i) Financial assets at fair value through profit or loss

Financial assets at fair value through profit or loss are financial assets held for trading. A financial asset is classified in this category if it is acquired principally for the purpose of selling in the short term. Derivatives are also categorized as held for trading unless they are designated as hedges. Assets in this category are classified as current assets.

(ii) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are included in current assets except for maturities greater than 12 months after the balance sheet date which are classified as non-current assets. Loans and receivables are included in trade receivables, other receivables, deposits and prepayments in the balance sheet (Note 2(l)).

(iii) Available-for-sale financial assets

Available-for-sale financial assets are non-derivatives that are either designated in this category or not classified in any of the other categories. They are included in non-current assets unless management intends to dispose of the financial assets within 12 months of the balance sheet date.

Purchases and sales of financial assets are recognized on the trade-date when the Group commits to purchase or sell the asset. Financial assets are initially recognized at fair value plus transaction costs for all financial assets not carried at fair value through profit or loss. Financial assets carried at fair value through profit or loss are initially recognized at fair value, and transaction costs are expensed in the profit and loss account. Financial assets are derecognized when the rights to receive cash flows from the financial assets have expired or have been transferred and the Group has transferred substantially all risks and rewards of ownership. Available-for-sale financial assets and financial assets at fair value through profit or loss are subsequently carried at fair value. Loans and receivables are carried at amortized cost using the effective interest method.

Gains or losses arising from changes in the fair value of financial assets classified under financial assets at fair value through profit or loss are presented in the profit and loss account as fair value gain or loss of financial assets in the period in which they arise. Dividend income from financial assets at fair value through profit or loss is recognized in the profit and loss account as part of other revenues when the Group's right to receive payments is established.

Changes in the fair value of monetary securities denominated in a foreign currency and classified as available-for-sale are analysed between translation differences resulting from changes in amortized cost of the security and other changes in the carrying amount of the security. The translation differences on monetary securities are recognized in profit and loss account; translation differences on non-monetary securities are recognized in equity. Changes in the fair value of monetary and non-monetary securities classified as available-for-sale are recognized in equity.

2. Principal accounting policies (Continued)

(i) Financial assets (Continued)

When securities classified as available-for-sale are sold or impaired, the accumulated fair value adjustments recognized in equity are included in the profit and loss account as gains and losses from available-for-sale financial assets.

Dividends on available-for-sale equity instruments are recognized in the profit and loss account as part of other revenues when the Group's right to receive payments is established.

The fair values of quoted financial assets are based on current bid prices. If the market for a financial asset is not active (and for unlisted securities), the Group establishes fair value by using valuation techniques. These include the use of recent arm's length transactions, reference to other instruments that are substantially the same, discounted cash flow analysis, and option pricing models, making maximum use of market inputs and relying as little as possible on entity-specific inputs.

The Group assesses at each balance sheet date whether there is objective evidence that a financial asset or a group of financial assets is impaired. In the case of equity securities classified as available-for-sale, a significant or prolonged decline in the fair value of the security below its cost is considered an indicator that the securities are impaired. If any such evidence exists for available-for-sale financial assets, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognized in the profit and loss account – is removed from equity and recognized in the profit and loss account. Impairment losses recognized in the profit and loss account on equity instruments are not reversed through the profit and loss account. Impairment test on trade receivables is described in Note 2(l).

(j) Derivative financial instruments and hedging activities

All derivative financial instruments are accounted for at fair value through profit or loss and the gain or loss on changes in fair value is recognized generally in the profit and loss account unless the derivative financial instrument qualifies for hedge accounting. Where a derivative financial instrument qualified for hedge accounting and is designated as a cash flow hedge, the effective part and the ineffective part of any unrealized gain or loss on the instrument is recognized directly in hedging reserve and in the profit and loss account respectively. The cumulative gain or loss associated with the effective part of the cash flow hedge or periods during which the gain or loss arising from the hedged transaction is recognized in the profit and loss account.

(k) Inventories

Inventories comprise raw materials, work-in-progress and finished goods are stated at the lower of cost and net realizable value. Cost, calculated on the weighted average basis, comprises materials, direct labour, other direct costs and related production overheads (based on normal operating capacity) and excludes borrowing costs. Net realizable value is determined on the basis of estimated selling price in the ordinary course of business less applicable variable selling expenses.

(l) Trade and other receivables

Trade and other receivables are recognized initially at fair value and subsequently measured at amortized cost using the effective interest method less provision for impairment. A provision for impairment of trade and other receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of receivables. Significant financial difficulties of the debtor, probability that the debtor will enter bankruptcy or financial reorganization, and default or delinquency in payments are considered indicators that the trade receivable is impaired. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate. The amount of the provision is recognized in the profit and loss account. When a trade receivable is proven uncollectible, it is written off against the provision for impairment of trade and other receivables. Subsequent recoveries of amounts previously written off are credited to the profit and loss account.

2. Principal accounting policies (Continued)

(m) Cash and cash equivalents

Cash and cash equivalents include cash in hand, deposits held at call with banks, time deposits and other short-term highly liquid investments with original maturities of three months or less, and bank overdrafts. Bank overdrafts are shown within borrowings in current liabilities on the balance sheet.

(n) Trade payables

Trade payables are recognized initially at fair value and subsequently measured at amortized cost using the effective interest method.

(o) Borrowings

Borrowings are recognized initially at fair value, net of transaction costs incurred. Borrowings are subsequently stated at amortized cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognized in the profit and loss account over the period of the borrowings using the effective interest method.

Borrowings are classified as current liabilities unless the Group has an unconditional right to defer settlement of the liability for at least 12 months after the balance sheet date.

(p) Deferred taxation

Deferred taxation is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated accounts. However, if the deferred taxation arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transactions affects neither accounting nor taxable profit or loss, it is not accounted for. Tax rates (and laws) enacted or substantively enacted by the balance sheet date are used to determine deferred taxation and it is expected to apply when the related deferred tax asset is realized or the deferred tax liability is settled.

Deferred tax assets are recognized to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilized.

Deferred taxation is provided on temporary differences arising on investments in subsidiaries and an associated company except where the timing of the reversal of the temporary difference can be controlled by the Group and it is probable that the temporary difference will not reverse in the foreseeable future.

(q) Employee benefits

(i) Bonus plans

The expected cost of bonus payments are recognized as a liability when the Group has a present legal or constructive obligation as a result of services rendered by employees and a reliable estimate of the obligation can be made.

Liabilities for bonus plans are expected to be settled within the next twelve months and are measured at the amounts expected to be paid when they are settled.

(ii) Pension obligations

The Group participates in a number of defined contribution retirement schemes in Hong Kong, Taiwan and various cities in China where the Group operates.

A defined contribution plan is a pension plan under which the Group pays fixed contributions to separately administered funds on a mandatory, contractual or voluntary basis. The Group has no legal or constructive obligations to pay further contributions if the funds do not hold sufficient assets to pay all employees the benefits relating to employee service in the current and prior periods. The contributions are recognized as employee benefit expense when they are due and are reduced by contributions forfeited by those employees who leave the scheme prior to vesting fully in the contributions. Prepaid contributions are recognized as an asset to the extend that a cash refund or a reduction in the future payments is available.

2. Principal accounting policies (Continued)

(q) Employee benefits (Continued)

(iii) Share-based compensation

The Group operates an equity-settled, share-based compensation plan. The fair value of the employee services received in exchange for the grant of the options is recognized as an expense. The total amount to be expensed over the vesting period is determined by reference to the fair value of the options granted, excluding the impact of any non-market vesting conditions (for example, profitability and sales growth targets). Non-market vesting conditions are included in assumptions about the number of options that are expected to vest. At each balance sheet date, the entity revises its estimates of the number of options that are expected to vest. It recognizes the impact of the revision of original estimates, if any, in the profit and loss account, and a corresponding adjustment to equity over the remaining vesting period.

The proceeds received net of any directly attributable transaction costs are credited to share capital (nominal value) and share premium when the options are exercised.

(r) Contingent liabilities

A contingent liability is a possible obligation that arises from past events and whose existence will only be confirmed by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the Group. It can also be a present obligation arising from past events that is not recognized because it is not probable that outflow of economic resources will be required or the amount of obligation cannot be measured reliably.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole.

A contingent liability is not recognized but is disclosed in the notes to the accounts. When a change in the probability of an outflow occurs so that the outflow becomes probable, it will then be recognized as a provision. Provisions are not recognized for future operating losses.

(s) Revenue recognition

Revenue comprises the fair value of the consideration received or receivable for sale of goods and services in the ordinary course of the Group's activities. Revenue is shown net of applicable value-added tax, returns, rebates and discounts and after eliminating sales within the Group.

Revenue is recognized when it is probable that future economic benefits will flow to the Group and the amount of revenue can be reliably measured.

Revenue from sales of goods manufactured or traded is recognized on the transfer of significant risks and rewards of ownership, which generally coincides with the time when the goods are delivered to customers and title has passed.

Handling income is recognized when the services are rendered.

Royalty income is recognized on an accrual basis in accordance with the substance of the relevant agreement.

Operating lease rental income is recognized on a straight-line basis over the periods of the leases.

Interest income is recognized on a time-proportion basis, taking account of the principal outstanding and the effective rate over the period to maturity, when it is determined that such income will accrue to the Group.

Dividend income is recognized when the right to receive payment is established.

2. Principal accounting policies (Continued)

(t) Segment reporting

A business segment is a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different from those of other business segments. A geographical segment is engaged in providing products or services within a particular economic environment that are subject to risks and returns that are different from those of segments operating in other economic environments.

In accordance with the Group's internal financial reporting, the Group has determined that the primary segment reporting format is by business segment and the secondary segment reporting format is by geographical segment.

Unallocated expenses represent corporate expenses. Segment assets consist primarily of goodwill, land use rights, fixed assets, deposits paid for acquisition of fixed assets, inventories, receivables and operating cash, and mainly exclude interest in an associated company, available-for-sale financial assets, derivative financial instruments, deferred tax assets and corporate assets. Segment liabilities comprise operating liabilities and exclude items such as corporate taxation and liabilities. Capital expenditure comprises additions to land use rights and fixed assets.

In respect of geographical segment reporting, sales are based on the country in which the customers are located. Total assets and capital expenditure are based on where the assets are located.

(u) Dividend distribution

Dividend distribution to the Company's shareholders is recognized as a liability in the Group's accounts in the period in which the dividends are approved by the board of directors and the Company's shareholders. Dividends proposed or declared after the balance sheet date are disclosed as a post balance sheet event and are not recognized as a liability at the balance sheet date.

3. Financial risk management

The Group's activities expose it to a variety of financial risks: foreign exchange risk, credit risk, liquidity risk and cash flow and fair value interest rate risk.

(a) Foreign exchange risk

The Group operates in various countries and regions and is exposed to foreign exchange risk arising from different currency exposures primarily with respect to Hong Kong dollars, US dollars, Euros and New Taiwanese dollars. Foreign exchange risk arises from future commercial transactions, recognized assets and liabilities and net investments denominated in foreign currencies. The Group has entered into foreign exchange forward contracts to manage the risk arising from certain recognized assets and liabilities. The directors are of the opinion that the Group's remaining exposure to foreign exchange risk would be minimal.

(b) Credit risk

The Group has no significant concentration of credit risk with respect to the retail business as sales are made in cash or via major credit cards. Regarding the wholesale business, the Group has policies in place to ensure that all sales of products are made to customers with appropriate credit history. The management of the Group has delegated a team responsible for determination of credit limits, credit approvals and other monitoring procedures to ensure that follow-up action is taken to recover overdue debts. In addition, the Group reviews the recoverable amount of each individual trade debt at each balance sheet date to ensure that adequate impairment losses are made for irrecoverable amounts. In this regard, the directors consider that the Group's credit risk is significantly reduced.

(c) Liquidity risk

All the bank financing of the Group is in the form of short-term bank loans. Given the Group has a net current assets of HK$434,188,000 and unutilized banking facilities of HK$136,496,000 as at 31 December 2006, the directors believe that sufficient funds are maintained and additional funds can be raised to meet future business operation and development.

3. Financial risk management (Continued)

(d) Cash flow and fair value interest rate risk

The Group is exposed to both cash flow and fair value interest rate risks due to changes in interest rates of interest-bearing financial assets and liabilities. Interest-bearing financial assets mainly comprise bank deposits which are mostly short-term in nature whereas interest-bearing financial liabilities are primarily short-term bank borrowings with primarily floating interest rates. The directors are of the opinion that future interest rates would be relatively stable and the effect on the Group's future financial results will not be significant.

4. Critical accounting estimates and judgements

Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

The Group makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

(a) Estimated impairment of goodwill

The Group determines whether goodwill is impaired on an annual basis. This requires an estimation of the value in use of the cash-generating units to which the goodwill is allocated. Estimating the value in use requires the Group to make an estimate of the expected future cash flows from the cash-generating unit and also to choose a suitable discount rate in order to calculate the present value of those cash flows.

(b) Income taxes

The Group is subject to income taxes in several jurisdictions. Significant judgement is required in determining the provision for income taxes. There are many transactions and calculations for which the ultimate tax determination is uncertain during the ordinary course of business. The Group recognizes liabilities for anticipated tax audit issues based on estimates of whether additional taxes will be due. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the income tax and deferred tax provisions in the period in which such determination is made.

(c) Tangible fixed assets and depreciation

Management determines the estimated useful lives and related depreciation charges for the Group's tangible fixed assets. Management will revise the depreciation charge where useful lives are different to previously estimated, or it will write off or write down technically obsolete or non-strategic assets that have been abandoned or sold.

(d) Estimated write-downs of inventories to net realizable value

The Group writes down inventories to net realizable value based on an assessment of the realizability of inventories. Provisions are made for inventories where events or changes in circumstances indicate that the balances may not be realized. The identification of obsolescence requires the use of judgements and estimates. Where the exception is different from the original estimate, such difference will impact carrying value of inventories and net realizable value for the periods in which such estimate is changed.

(e) Fair value estimation

The fair value of financial instruments that are not traded in an active market (for example, over-the-counter derivatives) is determined by using valuation techniques. The Group uses a variety of methods and makes assumptions that are based on market conditions existing at each balance sheet date. Other techniques, such as estimated discounted cash flows, are used to determine fair value for the remaining financial instruments.

The face values less any estimated credit adjustments for the Group's financial assets and liabilities with a maturity of less than one year, including bank balances and cash, pledged deposits, trade receivables, other receivables, deposits and prepayments, trade payables, other payables and accrued charges and bank loans and overdrafts are assumed to approximate their fair values. The fair value of financial liabilities for disclosure purposes is estimated by discounting the future contractual cash flows at the current market interest rate available to the Group for similar financial instruments.

5. Turnover, other revenues and net gains

An analysis of the Group's turnover, other revenues and net gains for the year is as follows:

	2006 HK$'000	2005 HK$'000
Turnover		
Sales of goods	**3,093,086**	2,622,677
Other revenues		
Tax refund on reinvestment	**8,915**	–
Income derived from an unlisted available-for-sale financial asset (Note 21(a)(i))	**3,000**	3,000
Interest income	**3,830**	1,885
Government incentives	**2,606**	–
Handling income	**2,361**	–
Royalty income	**321**	–
Gross rental income	**267**	286
Dividend income	**57**	88
Others	**2,339**	1,001
	23,696	6,260
Other net gains		
Fair value gain on derivative financial instruments	**85**	268
Gain on disposal of available-for-sale financial assets	**280**	–
Net exchange gain	**6,371**	7,872
	6,736	8,140
Other revenues and net gains	**30,432**	14,400

6. Segment information

(a) Primary reporting format – business segments

The Group is organized into two main business segments:

Brand business – Manufacturing and distribution of footwear products and accessories under "Daphne", "Shoebox" and "adidas Originals" owned by or licensed to the Group.

OEM business – Manufacturing and distribution of footwear products under original-equipment manufacturing arrangements ("OEM").

There were no material transactions between the business segments.

	2006 Brand business HK$'000	2006 OEM business HK$'000	2006 Group HK$'000	2005 Brand business HK$'000	2005 OEM business HK$'000	2005 Group HK$'000
Turnover	**2,316,310**	**776,776**	**3,093,086**	1,827,341	795,336	2,622,677
Segment results	**330,203**	**69,851**	**400,054**	209,471	112,849	322,320
Income derived from an unlisted available-for-sale financial asset			**3,000**			3,000
Fair value gain on derivative financial instruments			**85**			268
Unallocated revenues			**344**			374
Unallocated expenses			**(2,877)**			(2,558)
Operating profit			**400,606**			323,404
Segment assets	**1,333,896**	**311,702**	**1,645,598**	1,058,723	312,264	1,370,987
Interest in an associated company			**2,418**			2,346
Available-for-sale financial assets			**33,624**			33,437
Derivative financial instruments			**353**			268
Other unallocated assets			**36,845**			27,586
Total assets			**1,718,838**			1,434,624
Segment liabilities	**507,884**	**186,624**	**694,508**	412,882	189,163	602,045
Other unallocated liabilities			**11,118**			8,963
Total liabilities			**705,626**			611,008
Amortization	**644**	**643**	**1,287**	516	523	1,039
Depreciation	**56,002**	**10,098**	**66,100**	40,997	7,906	48,903
Provision for/(write-back of) bad and doubtful debts	**177**	**(2)**	**175**	–	46	46
Provision for/(write-back of) slow-moving inventories	**13,819**	**8,460**	**22,279**	7,682	(4,757)	2,925
Capital expenditure	**146,450**	**23,056**	**169,506**	127,898	29,047	156,945

(b) Secondary reporting format – geographical segments

The Group's two business segments operate in two main geographical areas, China and the US. In presenting information on the basis of geographical segments, segment turnover is based on the geographical location of customers.

	2006 HK$'000	2005 HK$'000
China	**2,303,778**	1,827,341
The US	**718,585**	770,238
Others	**70,723**	25,098
	3,093,086	2,622,677

As the Group's assets are mainly located in China, no segment assets and segment capital expenditures are presented.

7. Operating profit

Operating profit is stated after charging the following:

	2006 HK$'000	2005 HK$'000
Amortization of land use rights	**1,287**	1,039
Auditors' remuneration	**2,919**	2,182
Cost of inventories sold	**1,407,303**	1,214,091
Depreciation of fixed assets	**66,100**	48,903
Employee benefits expense (Note 13)	**408,829**	374,140
Loss on disposal of fixed assets	**4,595**	5,020
Operating lease rentals in respect of land and buildings	**364,366**	255,250
Provision for bad and doubtful debts, net	**175**	46
Provision for slow-moving inventories, net	**22,279**	2,925

8. Finance costs

	2006 HK$'000	2005 HK$'000
Interest on bank loans and overdrafts	**9,199**	4,441

9. Taxation

No provision for Hong Kong profits tax has been made in the accounts as the Group does not have any assessable profit arising in Hong Kong. Taxation on profits arising outside Hong Kong has been calculated on the estimated assessable profit for the year at the rates of taxation prevailing in the countries/places in which the Group operates.

Certain subsidiaries of the Company operating in China are eligible for certain tax exemptions and concessions including tax holiday and reduced enterprise income tax rate. Accordingly, the China enterprise income tax for such subsidiaries has been provided for after taking account of these tax exemptions and concessions.

The amount of taxation charged/(credited) to the consolidated profit and loss account represents:

	2006 HK$'000	2005 HK$'000
Current taxation		
– Taxation outside Hong Kong	**114,597**	62,479
– (Over)/under provision in prior years	**(420)**	159
Deferred taxation (Note 30)	**(17,664)**	522
	96,513	63,160

9. Taxation (Continued)

The tax on the Group's profit before tax differs from the theoretical amount that would arise using the applicable domestic tax rates of the consolidated entities as follows:

	2006 HK$'000	2005 HK$'000
Profit before taxation	**391,617**	319,216
Less: Share of profit of an associated company	**(210)**	(253)
	391,407	318,963
Tax calculated at domestic tax rates of 12% to 33% applicable to profits in the respective countries/places	**111,445**	76,827
Income not subject to taxation	**(48,762)**	(71,108)
Expenses not deductible for taxation purposes	**37,910**	56,019
Deferred tax assets previously not recognized	**(7,077)**	–
Tax losses for which no deferred tax assets recognized	**3,462**	2,230
Utilization of previously unrecognized tax losses	**(62)**	(701)
(Over)/under provision in prior years	**(420)**	159
Temporary differences not recognized	**17**	(266)
Taxation charge	**96,513**	63,160

The weighted average applicable tax rate was 28% (2005: 24%).

10. Profit attributable to shareholders of the Company

The profit attributable to shareholders of the Company is dealt with in the accounts of the Company to the extent of HK$36,607,000 (2005: HK$97,185,000).

11. Dividends

	2006 HK$'000	2005 HK$'000
Interim dividend, paid, of HK2.0 cents (2005: HK2.5 cents) per ordinary share	**32,758**	40,947
Final dividend, proposed, of HK2.5 cents (2005: HK2.5 cents) per ordinary share	**40,947**	40,947
	73,705	81,894

At a meeting held on 23 April 2007, the board of directors recommended a final dividend of HK2.5 cents per ordinary share for the year ended 31 December 2006. This proposed dividend is not reflected as a dividend payable in these accounts, but will be reflected as an appropriation of retained profits for the year ending 31 December 2007.

12. Earnings per share – basic and diluted

The calculation of basic and diluted earnings per share is based on the Group's profit attributable to shareholders of HK$291,566,000 (2005: HK$254,593,000) and the weighted average number of 1,637,892,384 (2005: 1,619,097,863) ordinary shares in issue during the year.

There were no dilutive potential ordinary shares in existence during the years ended 31 December 2006 and 31 December 2005.

13. Employee benefits expense

Employee benefits expense including directors' emoluments represents:

	2006 HK$'000	2005 HK$'000
Wages, salaries and bonuses	**389,745**	361,779
Defined contribution pension costs (Note (a))	**19,084**	12,361
	408,829	374,140

(a) Defined contribution pension costs

All Hong Kong employees of the Group have joined a Mandatory Provident Fund Scheme (the "MPF Scheme") registered with the Mandatory Provident Fund Schemes Authority under the Mandatory Provident Fund Schemes Ordinance in Hong Kong. The assets of the MPF Scheme are held separately from those of the Group in funds under the control of an independent trustee. Under the rule of the MPF Scheme, both the employer and employees are required to contribute 5% of the employee's relevant income or HK$1,000 per month, whichever is lower, as mandatory contributions.

The Group is also required to make contributions to pension schemes operated by the municipal governments of various cities in China and Taiwan at certain percentages of the salaries of its domestic employees. The governments are responsible for the entire pension obligations payable to retired employees. The Group does not have other obligations under these pension schemes in China and Taiwan other than the contribution payments.

As at both 31 December 2006 and 31 December 2005, no forfeited contribution is available to reduce the contribution payable in the future.

Contributions payable to the funds as at 31 December 2006 of approximately HK$1,375,000 (2005: HK$1,135,000) are included in other payables and accrued charges.

(b) Directors' emoluments

The remuneration of each director of the Company for the year ended 31 December 2006 is set out below:

	Fees HK$'000	Salaries and bonuses HK$'000	Defined contribution pension costs HK$'000	Total HK$'000
Name of director				
Mr Chen Ying-Chieh	–	1,162	30	1,192
Mr Chen Hsien Min	–	1,406	–	1,406
Mr Chang Chih-Kai	–	637	–	637
Mr Hsiao Hsi-Ming	72	–	–	72
Mr Huang Shun-Tsai	72	–	–	72
Mr Kuo Jung-Cheung	72	–	–	72
	216	3,205	30	3,451

13. Employee benefits expense (Continued)

(b) Directors' emoluments (Continued)

The remuneration of each director of the Company for the year ended 31 December 2005 is set out below:

	Fees HK$'000	Salaries and bonuses HK$'000	Defined contribution pension costs HK$'000	Total HK$'000
Name of director				
Mr Chen Ying-Chieh	–	1,182	24	1,206
Mr Chen Hsien Min	–	1,399	–	1,399
Mr Chang Chih-Kai	–	657	–	657
Mr Hsiao Hsi-Ming	60	–	–	60
Mr Huang Shun-Tsai	60	–	–	60
Mr Kuo Jung-Cheung	60	–	–	60
	180	3,238	24	3,442

(c) Five highest paid individuals

The five individuals whose emoluments were the highest in the Group for the year include two (2005: nil) directors whose emoluments are presented above. The emoluments payable to the remaining three (2005: five) individuals during the year are as follows:

	2006 HK$'000	2005 HK$'000
Basic salaries and bonuses	**2,666**	9,877
Performance related incentive payments	**117**	1,217
Defined contribution pension costs	**5**	–
	2,788	11,094

The emoluments fell within the following bands:

	Number of individuals 2006	2005
Emolument bands		
HK$Nil to HK$1,000,000	**2**	–
HK$1,000,001 to HK$1,500,000	**1**	–
HK$1,500,001 to HK$2,000,000	**–**	1
HK$2,000,001 to HK$2,500,000	**–**	4

No emoluments have been paid by the Group to the directors or the five highest paid individuals as an inducement to join or upon joining the Group, or as compensation for loss of office. No directors or the five highest paid individuals waived or agreed to waive any emoluments during the year.

14. Goodwill

During the year, the Group acquired 36% and 43.75% additional equity interests in two subsidiaries engaging in the brand business at cash considerations of HK$40,874,000 and HK$34,506,000 respectively. Goodwill arose from the acquisitions was HK$15,079,000 and HK$10,404,000 respectively.

Impairment testing of goodwill

The Group performed an annual impairment test for goodwill allocated to the Group's various cash-generating units ("CGUs") by comparing their recoverable amount to their carrying amount as at the balance sheet date. The recoverable amount of a CGU was determined based on value-in-use calculations. These calculations used cash flow projections based on financial budgets approved by management covering a three-year period. The after tax discount rate and the estimated weighted average annual sales growth rate applied to the cash flow projections were both approximately 10%. The budgeted gross profit margin and net profit margin were determined by the management for each individual CGU based on past performance and its expectations for market development. Management believes that any reasonably foreseeable change in any of the above key assumptions would not cause the carrying amount of goodwill to exceed the recoverable amount significantly.

15. Land use rights

	Group	
	2006	2005
	HK$'000	HK$'000
Cost		
At 1 January	**31,476**	26,029
Exchange adjustment	**1,244**	571
Additions	**2,206**	4,876
Transfer from fixed assets	**8,156**	–
At 31 December	**43,082**	31,476
Accumulated amortization		
At 1 January	**12,279**	11,138
Exchange adjustment	**227**	102
Amortization for the year	**1,287**	1,039
At 31 December	**13,793**	12,279
Net book value		
At 31 December	**29,289**	19,197
At 1 January	**19,197**	14,891

Notes:

(a) As at both 31 December 2006 and 31 December 2005, all land use rights were held outside Hong Kong on leases of between 10 to 50 years.

(b) As at 31 December 2006, land use rights of carrying value of HK$1,617,000 (2005: HK$264,000) were pledged as security for the Group's short-term bank loans (Note 27).

16. Fixed assets

	Group						
	Leasehold buildings HK$'000	Leasehold improve-ments HK$'000	Construction-in-progress HK$'000	Plant and machinery HK$'000	Furniture, fixtures and equipment HK$'000	Motor vehicles HK$'000	Total HK$'000
Cost							
At 1 January 2005	127,099	45,499	14,520	103,783	40,559	20,921	352,381
Exchange adjustment	2,623	933	300	2,316	564	373	7,109
Additions	9,297	53,955	45,547	11,138	25,939	6,193	152,069
Transfer	8,088	–	(8,088)	–	–	–	–
Disposals	(4,987)	(2,248)	–	(7,794)	(4,524)	(2,457)	(22,010)
At 31 December 2005	142,120	98,139	52,279	109,443	62,538	25,030	489,549
Exchange adjustment	**5,348**	**3,681**	**1,967**	**4,436**	**1,990**	**973**	**18,395**
Additions	**1,954**	**75,900**	**38,749**	**8,304**	**15,279**	**3,766**	**143,952**
Transfer	**9,815**	**–**	**(17,971)**	**–**	**–**	**–**	**(8,156)**
Disposals	**–**	**(6,377)**	**–**	**(3,326)**	**(1,794)**	**(1,248)**	**(12,745)**
At 31 December 2006	**159,237**	**171,343**	**75,024**	**118,857**	**78,013**	**28,521**	**630,995**
Accumulated depreciation							
At 1 January 2005	27,801	7,886	–	86,056	17,978	11,589	151,310
Exchange adjustment	574	162	–	1,976	236	212	3,160
Charge for the year	4,894	28,241	–	5,990	6,413	3,365	48,903
Disposals	(1,889)	(662)	–	(7,748)	(3,694)	(2,420)	(16,413)
At 31 December 2005	31,380	35,627	–	86,274	20,933	12,746	186,960
Exchange adjustment	**1,181**	**1,335**	**–**	**3,610**	**670**	**492**	**7,288**
Charge for the year	**4,545**	**39,230**	**–**	**7,973**	**9,995**	**4,357**	**66,100**
Disposals	**–**	**(1,952)**	**–**	**(3,275)**	**(1,514)**	**(1,188)**	**(7,929)**
At 31 December 2006	**37,106**	**74,240**	**–**	**94,582**	**30,084**	**16,407**	**252,419**
Net book value							
At 31 December 2006	**122,131**	**97,103**	**75,024**	**24,275**	**47,929**	**12,114**	**378,576**
At 31 December 2005	110,740	62,512	52,279	23,169	41,605	12,284	302,589

Notes:

(a) As at 31 December 2006, leasehold buildings of carrying value of HK$16,647,000 (2005: HK$13,349,000) were pledged for the Group's short-term bank loans (Note 27).

(b) During the year ended 31 December 2006, motor vehicles of carrying value of HK$160,000 (2005: HK$242,000) were leased out under operating leases.

17. Deposits paid for acquisition of fixed assets

Deposits were made by the Group for the acquisition of leasehold buildings in China. As at 31 December 2006, the acquisition has not been completed and the Group was in the procedure of obtaining the relevant deed of title.

18. Investments in subsidiaries

	Company 2006 HK$'000	2005 HK$'000
Unlisted investments, at cost	**165,635**	165,635

The following is a list of the principal subsidiaries as at 31 December 2006:

Name	Place of incorporation/ operation	Particulars of issued/ paid-up capital	Interest held %	Principal activities
Alldevelop Holdings Limited	British Virgin Islands	1 share of US$1 each	100	Investment holding
Dafu Footwear Co., Ltd. Hanjiang Putian City [a]	China	US$3,180,000	90	Manufacture of footwear
Dasheng Footwear Co., Ltd. Putian City [b]	China	US$4,285,700	100	Manufacture of footwear
Daphne Marketing Co., Ltd.	Taiwan	NTD50,000,000	100	Retail distribution of footwear and accessories
Daxin Footwear Co., Ltd. Putian City [b]	China	US$2,522,372	100	Processing of footwear
Daxing Shoe Material Co., Ltd. Hanjiang Putian City [b]	China	US$1,499,925	100	Manufacture of footwear
Ever Alliance Holdings Limited	Hong Kong	10,000 ordinary shares of HK$1 each	94.75	Retail sales right holder of footwear and apparel
Gentlefit Trading Limited	Hong Kong	100 ordinary shares of HK$1 each; 13,055,667 non-voting deferred shares of HK$1 each [d]	100	Export trading of footwear, investment and trademarks holding
Jacaranda International Limited	British Virgin Islands/Taiwan	2 shares of US$1 each	100	Export trading of footwear
Ji Wei Shoe Industrial Co., Ltd. [b]	China	US$5,000,090	100	Manufacture of footwear

18. Investments in subsidiaries (Contiuned)

Name	Place of incorporation/ operation	Particulars of issued/ paid-up capital	Interest held %	Principal activities
Jiangxi Dachuan Footwear Co., Ltd. [b]	China	US$1,205,904	100	Processing of footwear
Modern City Development Limited	Hong Kong	100 ordinary shares of HK$1 each; 10,000 non-voting deferred shares of HK$1 each [d]	100	Investment holding
Prime Success (BVI) Limited	British Virgin Islands	5,000,000 shares of US$0.01 each	100	Investment holding
Putian Hanjiang Footwear Co., Ltd. [a]	China	US$6,000,000	75	Manufacture of footwear
Shanghai Guang Wei Industry & Commerce Co., Ltd. [a]	China	US$4,600,000	87.8	Manufacture of footwear
Shoebox Holdings Limited	Hong Kong	10,000 ordinary shares of HK$1 each	95	Retail sales right holder of footwear, apparel and accessories
Victoria Success Investment Co., Ltd. [b]	China	US$30,000,000	100	Distribution of footwear and accessories and investment holding
Victoria Success (Shanghai) Limited [b]	China	US$5,000,000	100	Manufacture of footwear
Victoria Success Shoes (Suqian) Co. Ltd. [b]	China	RMB3,000,000	100	Processing of footwear
Winson Union Limited	Hong Kong	10,000 ordinary shares of HK$1 each	100	Investment holding
Yangzhou Quanwei Industry & Commerce Co., Ltd. [b]	China	US$700,570	100	Processing of footwear

18. Investments in subsidiaries (Contiuned)

Notes:

(a) These Companies were established in China in the form of equity joint ventures.

(b) These Companies were established in China in the form of wholly foreign-owned enterprises.

(c) Other than investment in Prime Success (BVI) Limited which is held directly by the Company, all subsidiaries shown above are held indirectly by the Company.

(d) The non-voting deferred shares practically carry no rights to dividends, nor rights to receive notice, nor rights to attend and vote at any general meeting of the respective companies, nor rights to participate in any distribution on winding up.

(e) None of the subsidiaries had any debt securities outstanding at the end of the year or at any time during the year.

19. Amounts due from subsidiaries – Company

The amounts due from subsidiaries are unsecured, interest-free and repayable on demand.

20. Interest in an associated company

	Group	
	2006	2005
	HK$'000	HK$'000
Share of net assets	**2,418**	2,346
Unlisted investment, at cost	**2,340**	2,340

Details of the associated company as at 31 December 2006 are as follows:

Name	Place of incorporation/ operation	Particulars of paid-up capital	Interest held indirectly %	Principal activity
Dayong Shoe Material Co., Ltd. Hanjiang Putian City ("Dayong")	China	RMB5,457,000	30	Manufacture of shoe materials

A summary of financial information of the associated company is as follows:

	2006	2005
	HK$'000	HK$'000
Assets	**8,403**	8,028
Liabilities	**554**	311
Revenues	**10,180**	9,839
Profit	**701**	844

21. Available-for-sale financial assets

	Group	
	2006	2005
	HK$'000	HK$'000
Unlisted investments (Note (a))	**33,624**	33,437
Listed securities (Note (b))	**–**	–
	33,624	33,437

Notes:

(a) Unlisted investments comprise investment in Jingxing Shoe Industrial Co., Ltd. Putian City ("Jingxing") of HK$33,000,000 (2005: HK$33,000,000) and investment in Daen Shoe Material Co. Ltd. ("Daen") of HK$624,000 (2005: HK$437,000). The fair values of unlisted investments are estimated by the directors of the Company.

(i) Investment in Jingxing
The Group holds 30% interest in Jingxing which is a sino-foreign equity joint venture established in China for a term of 70 years commencing November 1991. Jingxing is engaged in the manufacturing and distribution of footwear products.

The directors do not regard Jingxing as an associated company of the Group as they are of the opinion that the Group cannot exercise significant influence in the financial and operational decisions of Jingxing.

In 2006, the Group entered into an agreement with an affiliate (the "Guarantor") of one of the joint venture partners in Jingxing whereby in return for a minimum annual payment of HK$3,000,000 by the Guarantor for each of the three years ended 31 December 2008, the Group agreed to surrender its right to the share of any profit in Jingxing for the same period. By virtue of this agreement, the amount receivable by the Group from the Guarantor for the year ended 31 December 2006 was HK$3,000,000 (2005: HK$3,000,000) which has been recognized in the profit and loss account.

(ii) Investment in Daen
The Group holds 16% interest in Daen which is an equity joint venture established in China. Daen is engaged in the manufacturing and distribution of footwear products in China.

(b) As at 31 December 2006, the Group holds approximately 14.4% interest in Sun Home Leather Corporation Limited ("Sun Home"), a company engaged in the manufacturing and trading of leather materials.

On 30 November 2001, Sun Home was delisted from the Taiwan Stock Exchange Corporation and authorized to be traded on Over-The-Counter market on the same date. The directors considered that the fair value of the investment in Sun Home was negligible and the securities were fully impaired in 2001. Since there were only infrequent and low volume of transactions of shares of Sun Home in 2006, the directors consider that there has no material change in fair value of the investment in Sun Home as at 31 December 2006.

The investment in Sun Home has been pledged to a bank to secure the Group's short-term bank loans (Note 27).

22. Inventories

	Group	
	2006	2005
	HK$'000	HK$'000
Raw materials	**71,433**	82,488
Work-in-progress	**51,352**	44,760
Finished goods	**561,669**	505,139
	684,454	632,387

23. Trade receivables

The ageing analysis of trade receivables by invoice date is as follows:

	Group	
	2006	2005
	HK$'000	HK$'000
0 – 30 days	**79,214**	93,188
31 – 60 days	**22,996**	19,668
61 – 90 days	**8,933**	4,439
91 – 120 days	**1,058**	3,578
121 – 180 days	**574**	875
181 – 360 days	**495**	704
Over 360 days	**–**	12
	113,270	122,464

Note:

(a) The carrying value of trade receivables approximated its fair value.

(b) The Group generally allows an average credit period of 30 to 60 days to its trade customers other than major and long standing customers with whom specific extended terms will be agreed between the Group and the relevant counter parties.

(c) As at 31 December 2006, the provision for impairment of trade receivables was HK$177,000 (2005: nil).

24. Derivative financial instruments

Derivative financial instruments represented foreign exchange forward contracts that are not qualified for hedge accounting under the requirements of HKAS 39 and are deemed as held for trading.

25. Cash and cash equivalents

	Group		Company	
	2006	2005	**2006**	2005
	HK$'000	HK$'000	**HK$'000**	HK$'000
Bank balances and cash				
Cash at banks and in hand	**138,744**	133,109	**266**	228
Deposits with banks within three months of maturity	**9,955**	13,377	**–**	–
	148,699	146,486	**266**	228
Bank overdrafts	**–**	(19)	**–**	–
	148,699	146,467	**266**	228

25. Cash and cash equivalents (Continued)

The carrying amounts of cash and cash equivalents are denominated in the following currencies:

	Group		Company	
	2006	2005	**2006**	2005
	HK$'000	HK$'000	**HK$'000**	HK$'000
Renminbi	**119,990**	109,785	**–**	–
US dollar	**21,738**	23,488	**6**	6
New Taiwanese dollar	**4,139**	4,442	**–**	–
Hong Kong dollar	**2,223**	4,598	**260**	222
Euro	**609**	4,154	**–**	–
	148,699	146,467	**266**	228

Note: The weighted average effective interest rate of deposits with banks within three months of maturity was 3.03% (2005: 3.01%) per annum.

26. Trade payables

The ageing analysis of trade payables including trade balances due to related parties by invoice date is as follows:

	Group	
	2006	2005
	HK$'000	HK$'000
0 – 30 days	**171,658**	168,464
31 – 60 days	**89,746**	79,853
61 – 90 days	**14,396**	13,166
91 – 120 days	**5,794**	4,729
121 – 180 days	**2,912**	15,451
181 – 360 days	**5,258**	2,784
Over 360 days	**6,730**	4,255
	296,494	288,702

27. Bank loans and overdrafts

	Group	
	2006	2005
	HK$'000	HK$'000
Bank loans and overdrafts		
– Secured (Note (b))	**52,326**	71,753
– Unsecured	**130,868**	61,309
	183,194	133,062

27. Bank loans and overdrafts (Continued)

The carrying amounts of the bank loans and overdrafts are denominated in the following currencies:

	Group	
	2006	2005
	HK$'000	HK$'000
Hong Kong dollar	**127,126**	30,770
New Taiwanese dollar	**25,358**	42,126
US dollar	**20,755**	25,628
Renminbi	**9,955**	34,538
	183,194	133,062

Notes:

(a) As at both 31 December 2006 and 2005, the Group's bank loans were repayable within one year. The carrying value of bank loans and overdrafts approximated its fair value.

(b) As at 31 December 2006, the Group's secured short-term bank loans were secured by certain land use rights (Note 15(b)) and leasehold buildings (Note 16(a)), listed securities of Sun Home classified under available-for-sale financial assets with nil (2005: nil) carrying value and a bank deposit of HK$6,000,000 (2005: HK$6,000,000).

(c) The weighted average effective interest rate of bank loans and overdrafts as at 31 December 2006 is 5.09% (2005: 4.60%) per annum.

28. Share capital

	2006	2005
	HK$'000	HK$'000
Authorized:		
10,000,000,000 ordinary shares of HK$0.10 each	**1,000,000**	1,000,000

	2006		2005	
	Number of ordinary shares	**Share capital HK$'000**	Number of ordinary shares	Share capital HK$'000
Issued and fully paid:				
At 1 January	**1,637,892,384**	**163,789**	1,567,892,384	156,789
Shares issued under share option scheme	**–**	**–**	70,000,000	7,000
At 31 December	**1,637,892,384**	**163,789**	1,637,892,384	163,789

In accordance with the Company's share option scheme (the "Scheme") adopted on 29 May 2003 for a period of ten years, the board of directors may grant options to eligible employees, officers, agents or consultants, including executive or non-executive directors, of the Group to subscribe for ordinary shares in the Company in accordance with the terms of the Scheme. No options were granted, exercised or cancelled under the Scheme during the year. There were no options outstanding as at 31 December 2006 and 31 December 2005.

29. Reserves

	Group								
	Share premium HK$'000	Capital redemption reserve HK$'000 (Note (a))	Fair value adjustment reserve HK$'000	Translation reserve HK$'000	Goodwill HK$'000 (Note (b))	Merger reserve HK$'000 (Note (c))	Other reserves HK$'000 (Note (d))	Retained profits HK$'000	Total HK$'000
At 1 January 2005	9,735	2,882	(4,000)	(12,415)	(36,782)	322	11,984	405,205	376,931
Shares issued under share option scheme	14,770	–	–	–	–	–	–	–	14,770
Currency translation differences	–	–	–	7,874	–	–	–	–	7,874
Transfer	–	–	–	–	–	–	2,246	(2,246)	–
Share of an associated company's reserve	–	–	–	(45)	–	–	4	(4)	(45)
Profit for the year	–	–	–	–	–	–	–	254,593	254,593
Dividends	–	–	–	–	–	–	–	(73,705)	(73,705)
At 31 December 2005	24,505	2,882	(4,000)	(4,586)	(36,782)	322	14,234	583,843	580,418
Currency translation differences	**–**	**–**	**–**	**19,153**	**–**	**–**	**–**	**–**	**19,153**
Transfer	**–**	**–**	**–**	**–**	**–**	**–**	**1,711**	**(1,711)**	**–**
Share of an associated company's reserve	**–**	**–**	**–**	**87**	**–**	**–**	**5**	**(5)**	**87**
Profit for the year	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**291,566**	**291,566**
Dividends	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**(73,705)**	**(73,705)**
At 31 December 2006	**24,505**	**2,882**	**(4,000)**	**14,654**	**(36,782)**	**322**	**15,950**	**799,988**	**817,519**

	Company				
	Share premium HK$'000	**Capital redemption reserve** HK$'000 (Note (a))	**Contributed surplus** HK$'000 (Note (e))	**Retained profits** HK$'000	**Total** HK$'000
At 1 January 2005	9,735	2,882	152,891	25,948	191,456
Shares issued under share option scheme	14,770	–	–	–	14,770
Profit for the year	–	–	–	97,185	97,185
Dividends	–	–	–	(73,705)	(73,705)
At 31 December 2005	24,505	2,882	152,891	49,428	229,706
Profit for the year	**–**	**–**	**–**	**36,607**	**36,607**
Dividends	**–**	**–**	**–**	**(73,705)**	**(73,705)**
At 31 December 2006	**24,505**	**2,882**	**152,891**	**12,330**	**192,608**

Notes:

(a) Capital redemption reserve
The capital redemption reserve represents the nominal amount of shares repurchased by the Company in 1999.

(b) Goodwill
The amount represents goodwill on acquisitions occurred prior to 1 January 2001 that was taken to reserves as deduction from equity. The goodwill will not recognized in the profit and loss account when all or part of the business to which the goodwill relates is disposed of or when a cash-generating unit to which the goodwill relates is impaired.

(c) Merger reserve
The merger reserve represents the difference between the aggregate nominal amount of the share capital of the subsidiaries at the date on which they were acquired by the Company and the nominal amount of the share capital issued by the Company as consideration for the acquisition pursuant to the corporate reorganization in 1995.

29. Reserves (Continued)

Notes: (Continued)

(d) Other reserves

Other reserves comprising general reserve fund of HK$9,060,000 (2005: HK$7,767,000) and enterprise expansion fund of HK$6,890,000 (2005: HK$6,467,000) required to be set up pursuant to the laws of China for the Company's subsidiaries and an associated company established in China. The general reserve fund can only be used to make up losses incurred, increase registered capital or used for collective welfare of employees. The enterprise expansion fund can only be used to increase registered capital.

(e) Contributed surplus

The contributed surplus of the Company represents the difference between the aggregate net assets of the subsidiaries acquired by the Company under the corporate reorganization in 1995 and the nominal amount of the Company's shares issued for the acquisition.

(f) Distributable reserves

The Company's reserves available for distribution to its shareholders comprise share premium, contributed surplus and retained profits. Under the Companies Law (Revised) of the Cayman Islands, share premium of the Company is available for paying distributions or dividends to shareholders subject to the provisions of its Articles of Association and provided that immediately following the distribution or payment of dividend, the Company is able to pay its debts as they fall due in the ordinary course of business. In accordance with the Company's Articles of Association, dividends shall be payable out of the profits or other reserves, including the share premium account, of the Company.

30. Deferred taxation

Deferred taxation is calculated in full on temporary differences under the liability method using the applicable tax rates.

The movement on the net deferred tax assets is as follows:

	Group	
	2006	2005
	HK$'000	HK$'000
At 1 January	**17,459**	17,981
Charged to profit and loss account (Note 9)	**17,664**	(522)
At 31 December	**35,123**	17,459

Deferred income tax assets are recognized for tax losses available to be carried forward to the extent that realization of the related tax benefit through the future taxable profits is probable. As at 31 December 2006, the Group has unrecognized tax losses of HK$24,195,000 (2005: HK$296,000) which will expire within the next five years to be carried forward against future taxable income.

The movements in deferred tax assets and liabilities (prior to offsetting of balances within the same taxation jurisdiction) during the year are as follows:

	Group									
Deferred tax assets	**Provisions**		**Decelerated tax depreciation**		**Deferred expenses**		**Tax losses**		**Total**	
	2006	2005	**2006**	2005	**2006**	2005	**2006**	2005	**2006**	2005
	HK$'000	HK$'000	**HK$'000**	HK$'000	**HK$'000**	HK$'000	**HK$'000**	HK$'000	**HK$'000**	HK$'000
At 1 January	**11,592**	11,501	**5,218**	6,155	**431**	672	**701**	–	**17,942**	18,328
Credited/(charged) to profit and loss account	**14,113**	91	**2,157**	(937)	**1,225**	(241)	**616**	701	**18,111**	(386)
At 31 December	**25,705**	11,592	**7,375**	5,218	**1,656**	431	**1,317**	701	**36,053**	17,942

30. Deferred taxation (Continued)

Deferred tax liabilities	Group					
	Accelerated tax depreciation		Others		Total	
	2006 HK$'000	2005 HK$'000	**2006 HK$'000**	2005 HK$'000	**2006 HK$'000**	2005 HK$'000
At 1 January	**483**	328	**–**	19	**483**	347
Charged/(credited) to profit and loss account	**447**	155	**–**	(19)	**447**	136
At 31 December	**930**	483	**–**	–	**930**	483

31. Consolidated cash flow statement

Reconciliation of operating profit to net cash generated from operations

	2006 HK$'000	2005 HK$'000
Operating profit	**400,606**	323,404
Interest income	**(3,830)**	(1,885)
Amortization	**1,287**	1,039
Depreciation	**66,100**	48,903
Loss on disposal of fixed assets	**4,595**	5,020
Fair value gain on derivative financial instruments	**(85)**	(268)
Gain on disposal of available-for-sale financial assets	**(280)**	–
Operating profit before working capital changes	**468,393**	376,213
Increase in inventories	**(52,067)**	(163,276)
Increase in trade receivable, other receivables, deposits and prepayments and other non-current assets	**(76,569)**	(66,135)
Increase in trade payables, other payables and accrued charges	**21,390**	77,946
Net cash generated from operations	**361,147**	224,748

32. Contingent liabilities

The Group had no material contingent liabilities as at both 31 December 2006 and 31 December 2005.

As at 31 December 2006, the Company has given guarantees to various banks to secure general banking facilities granted to certain subsidiaries amounting to HK$170,200,000 (2005: HK$123,800,000). As at 31 December 2006, the utilized amount of such facilities covered by the Company's guarantees was HK$117,326,000 (2005: HK$20,970,000). The directors considered that no significant liabilities would arise from the bank guarantees given which arose in the ordinary course of business.

33. Commitments

(a) Capital commitments for purchase of land use rights and fixed assets

	Group	
	2006 HK$'000	2005 HK$'000
Authorized but not contracted for	**58,632**	114,791
Contracted but not provided for	**33,061**	18,601
	91,693	133,392

33. Commitments (Contiuned)

(b) Commitments under operating leases

As at 31 December 2006, the Group had future aggregate minimum lease payments in respect of various production plants and facilities, warehouses, offices and distribution outlets under non-cancellable operating leases as follows:

	Group	
	2006	2005
	HK$'000	HK$'000
Not later than one year	**223,101**	180,094
Later than one year and not later than five years	**521,315**	366,110
Later than five years	**13,973**	13,350
	758,389	559,554

Payment obligations in respect of operating leases on properties with rentals vary with gross revenues are not included as future minimum lease payments.

(c) The Company did not have any material commitments as at 31 December 2006 (2005: nil).

34. Related party transactions and balances

In addition to the transactions and balances disclosed elsewhere in these accounts, the Group entered into the following related party transactions during the year:

(a) Transactions and balances with related companies

	Transactions		Balances at year end	
	2006	2005	**2006**	2005
	HK$000	HK$000	**HK$000**	HK$000
Purchases from				
– an associated company	**446**	–	**114**	41
– investee companies	**54,429**	23,024	**15,922**	887

Note: Purchases of shoe materials and footwear products from the associated company, Dayong, and investee companies, Sun Home, Jingxing and Daen, were conducted in the normal course of the Group's business. The terms of transactions were determined and agreed between the Group and the counter parties and all balances due were repayable according to trade terms.

(b) Key management personnel compensation

	2006	2005
	HK$'000	HK$'000
Salaries and bonuses	**10,162**	17,108
Defined contribution pension costs	**112**	68
	10,274	17,176

35. Post balance sheet event

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